KUB

Knoxville Utilities Board

Consolidated

Financial Statements and Supplemental Information
June 30, 2016 and 2015

KUB Board of Commissioners

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Knoxville Utilities Board
Index
June 30, 2016 and 2015

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Report of Independent Auditors

Board of Commissioners
Knoxville Utilities Board
Knoxville, Tennessee

We have audited the accompanying financial statements of the Knoxville Utilities Board (KUB), a component unit of the City of Knoxville, Tennessee, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise KUB's basic financial statements as listed in the index.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to KUB'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 KUB'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 KUB as of June 30, 2016 and 2015, and the changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Commissioners
Knoxville Utilities Board
Knoxville, Tennessee

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 26 and the required supplementary information on pages 62 through 64 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise KUB's basic financial statements. The schedule of insurance in force is presented for purposes of additional analysis and is not a required part of the basic financial statements. The schedule of expenditures of federal awards and state financial assistance is presented for purposes of additional analysis as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* and the State of Tennessee Comptroller of the Treasury Office and is also not a required part of the basic financial statements.

The schedule of expenditures of federal awards and state financial assistance is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards and state financial assistance is fairly stated in all material respects in relation to the basic financial statements as a whole.

The schedule of insurance in force has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express and opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 27, 2016, on our consideration of KUB's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering KUB's internal control over financial reporting and compliance.

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

Knoxville Utilities Board (KUB), comprised of the Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions, including setting rates. KUB's accounts are maintained in conformity with the Uniform System of Accounts of the Federal Energy Regulatory Commission (FERC), the Uniform System of Accounts of the National Association of Regulatory Utility Commissioners (NARUC), and the Governmental Accounting Standards Board (GASB), as applicable.

This discussion and analysis is designed to (a) assist the reader in focusing on significant financial issues, (b) provide an overview of KUB's financial activity, (c) identify major changes in KUB's financial position, and (d) identify any financial concerns.

The Management Discussion and Analysis (MD&A) focuses on the fiscal year ending June 30, 2016 activities, resulting changes and current known facts, and should be read in conjunction with KUB's consolidated financial statements.

Consolidated Highlights

System Highlights

As of June 30, 2016, KUB served 451,896 customers. KUB added 3,951 new customers in fiscal year 2016, representing growth of less than one percent.

KUB's electric system experienced a record peak in demand of 1,328 megawatt hours in February 2015. KUB's electric system had a strong year for reliability with only 1.82 hours of service interruption for the average customer in fiscal year 2016. The natural gas system's peak demand occurred February 2015 at 136,356 dekatherms.

The second of three annual rate increases for each Division previously adopted by the KUB Board of Commissioners went into effect in fiscal year 2016. These rate increases provide additional revenue to help fund each system's respective Century II infrastructure program.

KUB's electric system was impacted by an ice storm event in February 2015 that resulted in a cost of $2 million to the system. KUB received $1.6 million in reimbursements in fiscal year 2016 from the Federal Emergency Management Agency (FEMA) to offset the cost of the 2015 event.

KUB's electric system was awarded the Diamond level designation by the American Public Power Association's (APPA) Reliable Public Power Provider (RP3) program, the highest level of recognition of the program.

KUB's energy sales in fiscal year 2016 were impacted by the second mildest winter in Knoxville over the last forty years. Natural gas sales dropped approximately 10 percent from the prior year and electric sales volumes declined approximately 3 percent.

KUB's treatment plants continue to meet high standards of operation. KUB's Kuwahee, Eastbridge, Loves Creek and Fourth Creek wastewater treatment plants were awarded Operational Excellence awards from the Tennessee Kentucky Water Environment Association for having one or less permit violations within the 2015 calendar year. The treatment plants additionally won awards at various levels based on performance from the National Association of Clean Water Agencies for peak performance. The

Eastbridge wastewater treatment plant was awarded a Platinum award for continued outstanding compliance performance over multiple years. Kuwahee and Loves Creek wastewater treatment plants won Gold Awards for having no permit violations in 2015 and the Fourth Creek wastewater treatment plant was awarded Silver for having only one permit violation in 2015.

KUB continued to maintain certification with the National Biosolids Partnership following a rigorous review process and independent audit that was conducted in December 2015. (Biosolids are nutrient-rich organic matter produced by wastewater treatment that can be recycled as fertilizer).

Century II Infrastructure Program

Century II is KUB's proactive long-range program to improve and maintain the electric, natural gas, water and wastewater systems for its customers. It includes maintenance and asset replacement strategies for each system and establishes sustainable replacement cycles. Century II moves KUB into its second century of service by improving each system through sound planning, resource allocation, and continued, but accelerated, investment.

KUB's Century II programs were resumed in 2011, after a break due to the economic recession. At that time, the KUB Board of Commissioners endorsed ten year funding plans for the electric and water systems, which include a combination of rate increases and debt issues to fully fund the Century II programs. The Board adopted three years of electric and water rate increases to help fund those plans. All three of those rate increases, adopted in 2011, have gone into effect.

In 2013, the Board extended the funding approach for Century II to include the natural gas and wastewater systems. The Board formally endorsed and adopted by resolution, ten year funding plans for the natural gas and wastewater systems, which include a combination of rate increases and debt issues.

In April 2014, KUB management provided the Board an updated assessment of the overall condition of each utility system, including a recommendation for annual rate increases for each division for the next three fiscal years.

In June 2014, the Board approved the proposed three annual rate increases for all KUB Divisions, of which the first and second rate increases have gone into effect. The remaining electric rate increase will generate $5.2 million in additional annual revenue, while the gas rate increase will generate $1.8 million in additional annual revenue. The remaining water rate increase will produce $2 million in additional annual revenue and wastewater will produce $4.7 million of additional annual sales revenues.

In fiscal year 2015, KUB concluded the smart grid pilot project, of which a portion of the project was funded by a United States Department of Energy Smart Grid Investment Grant (SGIG). This grant was received by KUB in 2009 as part of the American Reinvestment and Recovery Act (ARRA). Based upon the success of that pilot, KUB formed a plan to move forward with a Century II Grid Modernization initiative, which includes advanced metering for all KUB customers, a telecommunication system linking critical KUB infrastructure, and an increased investment in automation technology to help operate KUB's energy and water distribution systems.

KUB is in the process of implementing a 15-year initiative to ensure KUB will continue to provide high-quality, reliable water service to its customers over the long-term. KUB maintains a single water treatment plant for its system. In lieu of building a second treatment facility to ensure capacity will be available to meet the needs of current and future water customers, KUB will invest approximately $120 million in various redundant facilities at its existing Mark B. Whitaker Water Treatment Plant over the next 11 years.

For the fiscal year, KUB stayed on track with its overall Century II capital budget and production goals. 2,208 poles and 13.3 miles of underground electric cable were replaced for the electric system. 4.2 miles of cast iron/ductile iron gas main were replaced for the natural gas system. 14.3 miles of galvanized water main and 7.2 miles of cast iron water main were replaced for the water system. 28 miles of wastewater system main were rehabilitated or replaced.

The natural gas South Loop project was completed in October 2015, which included the installation of a new 8 mile transmission main in the southwest portion of KUB's service territory. The South Loop will provide additional system capacity to meet the increased natural gas demands of the University of Tennessee, in addition to other potential growth opportunities in that portion of KUB's gas service territory.

Consent Decree

In February 2005, a Consent Decree was entered into federal court regarding the operation of KUB's wastewater system. Under the terms of the Consent Decree, the remediation of identified sanitary sewer overflows (SSOs) on KUB's wastewater system had to be completed by June 30, 2016. KUB completed all the requirements of the Consent Decree for the collection system two years in advance of the deadline.

The Consent Decree also required KUB to perform an evaluation of the wet weather performance and capacity of its wastewater treatment plants. In July 2007, KUB submitted a Composite Correction Plan (CCP) for its wastewater treatment plants to EPA for review. The development and filing of the CCP was a requirement of the federal order of February 2005. The CCP includes recommended improvements to KUB's Kuwahee and Fourth Creek treatment plants to address wet weather capacity issues noted in prior assessments. The EPA approved the CCP in January 2009 including a recommended schedule of plant improvements that extends beyond the expiration date of the original Consent Decree. An amendment to the Consent Decree incorporating and establishing this schedule was agreed to by all parties and was entered on June 23, 2009. The purpose of the Amendment is to allow KUB to complete a portion of work outlined in the CCP after the Consent Decree deadline of June 30, 2016. The CCP provides for a biologically enhanced high-rate clarification (the BEHRC) secondary treatment system to be installed at the Fourth Creek treatment plant by June 30, 2018 and at the Kuwahee treatment plant by June 30, 2021. The total cost of such improvements is estimated to be approximately $120 million.

KUB's funding plan for the Consent Decree includes long-term bonds and a series of rate increases phased in over the term of the order. Bond proceeds fund all types of wastewater capital projects, the majority of which are related to the Consent Decree. As of June 30, 2016, the Wastewater Division had issued $485 million in bonds to fund system capital improvements since the inception of the Consent Decree. The Board previously approved two 50 percent rate increases, which went into effect in April 2005 and January 2007. The Board also approved an 8 percent rate increase, which was effective in September 2008, two 12 percent rate increases, which were effective in April 2011 and October 2012, and three 6 percent rate increases effective October 2014, October 2015 and October 2016. KUB anticipates additional bond issues and rate increases over the next decade to help fund wastewater capital improvements.

KUB successfully completed the first cycle of Maintenance Operation Management (MOM) requirements one year before the deadline by inspecting 99.5% of manholes and gravity mains, smoke testing 99.9% of gravity mains, performing required inspections of pump stations and the related force mains, and completing all Corrective Action Plan/Engineering Report (CAP/ER) projects. KUB initiated the second MOM cycle that continues to focus on the prevention of SSOs. As part of the Century II initiative, formally known as the PACE10 program, KUB has installed storage tanks providing 34 million gallons of wastewater storage to control wet weather overflows and rehabilitated or replaced approximately 334.9 miles of collection system pipe. KUB also continues to maintain a proactive operations and maintenance plan for the wastewater collection system including inspection, grease control, and private lateral enforcement. The result of the PACE10/Century II initiative has been an 82 percent reduction in SSOs.

As of June 30, 2016, the Wastewater Division had completed its twelfth full year under the Consent Decree, spending $529.5 million on capital investments to meet Consent Decree requirements. During fiscal year 2016, the Wastewater Division incurred $37.3 million in total expenditures related to Consent Decree requirements, including $3.3 million for operating costs and $34 million in capital improvements which included the rehabilitation or replacement of 28 miles of wastewater main. During the fiscal year, $26.5 million was spent on sewer mini-basin rehabilitation and replacement. Trunk line rehabilitation and replacement accounted for $2 million of capital expenditures, while pump station improvements accounted for $4.6 million.

Financial Highlights

Fiscal Year 2016 Compared to Fiscal Year 2015

KUB's consolidated net position increased $34 million. This increase was $2 million less than the prior year's change in net position. A restatement to the fiscal year 2014's net position based on a change in method of accounting for the pension reduced the total net position by $0.8 million during fiscal year 2015. This change resulted in a net increase of $35.2 million or 3.9 percent in KUB's consolidated net position in fiscal year 2015.

Operating revenue decreased $30.3 million or 4 percent, the result of lower electric and natural gas sales volumes offset in part by additional revenues from system rate increases and a modest increase in billed water sales and wastewater volumes. Purchased energy expense (power and natural gas) decreased $39.9 million or 8.3 percent, the combined effect of $17.4 million decrease in purchased power and a decrease of $22.5 million in purchased gas. Margin from sales (operating revenue less purchased energy expense) was up $9.5 million or 3.3 percent compared with the prior fiscal year.

Operating expenses (excluding purchased power and purchased gas expense) increased $9.6 million, or 4.5 percent. Operating and maintenance (O&M) expenses were $1.2 million or one percent higher than the previous year. Depreciation expense increased $6.7 million or 10.8 percent. Taxes and tax equivalents increased $1.8 million or 6 percent, reflecting higher plant in service levels.

Interest income was $0.5 million more than the prior fiscal year. Interest expense increased $1.2 million or 3.1 percent, reflecting interest costs on revenue bonds issued during fiscal year 2015 to fund system capital improvements.

Capital contributions increased $0.6 million, the result of more contributed assets from developers.

Total plant assets (net) increased $92 million or 5.6 percent over the last fiscal year.

Long-term debt represented 50.4 percent of KUB's consolidated capital structure, compared to 52 percent last fiscal year. Capital structure equals long-term debt (including the current and long-term portion of revenue bonds and notes), plus net position.

Fiscal Year 2015 Compared to Fiscal Year 2014

KUB's consolidated net position increased $36 million. This increase was $6.2 million greater than the prior year's change in net position. A restatement to the prior fiscal year's net position based on a change in method of accounting for the pension reduced the total net position by $0.8 million during fiscal year 2015. This change resulted in a net increase of $35.2 million or 3.9 percent in KUB's consolidated net position.

Operating revenue increased $12 million or 1.6 percent, the result of additional revenue from electric, gas, water, and wastewater rate increases and modest increases in natural gas, water, and wastewater sales volumes. Purchased energy expense (power and natural gas) decreased $4.9 million or 1 percent, the net effect of $0.7 million increase in purchased power and a decrease of $5.6 million in purchased gas. Margin from sales (operating revenue less purchased energy expense) was up $16.9 million or 6.3 percent compared with the prior fiscal year.

Operating expenses (excluding purchased power and purchased gas expense) increased $12 million, or 5.9 percent. Operating and maintenance (O&M) expenses were $3.6 million or 3 percent higher than the previous year. Depreciation expense increased $5.8 million or 10.4 percent. Taxes and tax equivalents increased $2.6 million or 9.4 percent, reflecting higher plant in service levels and a property tax increase by the City of Knoxville.

Interest income was consistent with the prior fiscal year. Interest expense increased $0.9 million or 2.5 percent, reflecting interest costs on $163 million in revenue bonds issued during the fiscal year to fund system capital improvements.

Capital contributions decreased $0.1 million, the result of less contributed assets from developers.

Total plant assets (net) increased $102.3 million or 6.6 percent over the last fiscal year.

KUB sold six series of revenue bonds during fiscal year 2015 for the purpose of funding capital improvements totaling $163 million. The $85 million bond issue in April 2015 was accelerated to take advantage of the low interest rate environment which impacted the debt ratio and debt service coverage levels for fiscal year 2015. Long-term debt represented 52 percent of KUB's capital structure, compared to 49.2 percent last year. Capital structure equals long-term debt (including the current and long-term portion of revenue bonds and notes), plus net position.

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Knoxville Utilities Board Consolidated Financial Statements

KUB's financial performance is reported under three basic consolidated financial statements: the Statement of Net Position; the Statement of Revenues, Expenses and Changes in Net Position; and the Statement of Cash Flows.

Statement of Net Position

KUB reports its assets, deferred outflows of resources, liabilities, deferred inflows of resources and net position in the Statement of Net Position. Assets are classified as current, restricted, plant in service, or other assets.

Liabilities are classified as current, other, or long-term debt. Net position is classified as net investment in capital assets; restricted; or unrestricted. Net position tells the user what KUB has done with its accumulated earnings, not just the balance.

Net investment in capital assets reflects the book value of all capital assets less the outstanding balances of debt used to acquire, construct, or improve those assets.

Restricted net position includes assets that have been limited to specific uses by KUB's bond covenants or through resolutions passed by the KUB Board.

Unrestricted net position is a residual classification; the amount remaining after reporting net position as either invested in capital or restricted is reported there.

Statement of Revenues, Expenses and Changes in Net Position

KUB reports its revenues and expenses (both operating and non-operating) on the Statement of Revenues, Expenses and Changes in Net Position. In addition, any capital contributions or assets donated by developers are reported on this statement.

Total revenue less total expense equals the change in net position for the reporting period. Net position at the beginning of the period is increased or decreased, as applicable, by the change in net position for the reporting period.

The change in net position for the reporting period is added to the net position segment of the Statement of Net Position.

Statement of Cash Flows

KUB reports cash flows from operating activities, capital and related financing activities, and investing activities on the Statement of Cash Flows. This statement tells the user the sources and uses of cash during the reporting period.

The statement indicates the beginning cash balance and ending cash balance and how it was either increased or decreased during the reporting period.

The statement also reconciles cash flow to operating income as it appears on the Statement of Revenues, Expenses and Changes in Net Position.

Condensed Financial Statements

Statement of Net Position

The following table reflects the condensed consolidated Statement of Net Position for KUB compared to the prior year and the year preceding the prior year.

Statements of Net Position
As of June 30

(in thousands of dollars)	**2016**	**2015**	**2014**
Current, restricted and other assets	$ 318,650	$ 413,061	$ 347,698
Capital assets, net	1,743,105	1,651,147	1,548,874
Deferred outflows of resources	34,235	28,388	12,252
Total assets and deferred outflows of resources	2,095,990	2,092,596	1,908,824
Current and other liabilities	159,519	152,535	161,523
Long-term debt outstanding	972,366	1,005,062	853,887
Deferred inflows of resources	1,512	6,378	-
Total liabilities and deferred inflows of resources	1,133,397	1,163,975	1,015,410
Net position			
Net investment in capital assets	772,012	650,464	688,374
Restricted	16,201	14,892	13,163
Unrestricted	174,380	263,265	191,877
Total net position	$ 962,593	$ 928,621	$ 893,414

Normal Impacts on Statement of Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Net Position presentation.

- Change in net position (from Statement of Revenues, Expenses and Changes in Net Position): impacts (increase/decrease) current and other assets and/or capital assets and unrestricted net position.
- Issuing debt for capital: increases deferred outflows of resources and long-term debt.
- Spending debt proceeds on new capital: reduces current assets and increases capital assets.
- Spending of non-debt related current assets on new capital: (a) reduces current assets and increases capital assets and (b) reduces unrestricted net position and increases net investment in capital assets.
- Principal payment on debt: (a) reduces current and other assets and reduces long-term debt and (b) reduces unrestricted net position and increases net investment in capital assets.
- Reduction of capital assets through depreciation: reduces capital assets and net investment in capital assets.

Impacts and Analysis

Current, Restricted and Other Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Current, restricted and other assets decreased $94.4 million or 22.9 percent. The decrease was primarily attributable to the utilization of $46.1 million in bond proceeds to fund system capital projects. General fund cash (including cash and cash equivalents, short-term investments, and long-term investments) decreased $45.9 million. The net pension asset decreased $6 million due to the recognition of a net pension liability of $5 million during fiscal year 2016. Accounts receivable decreased $4.9 million. Gas storage decreased $1.4 million, reflecting lower commodity prices for natural gas for slightly higher storage volumes compared to the prior fiscal year.

These decreases were offset by an increase in inventories of $2.1 million and an increase of $4.6 million in operating contingency reserves. KUB under recovered its wholesale gas costs by $2.2 million in fiscal year 2016 compared to a $1.1 million over recovery in fiscal year 2015. The under recovery of costs will be collected from customers next fiscal year through adjustments to rates via the Purchased Gas Adjustment. Another offset to the decrease was the under recovery of $1.4 million in purchased power costs from electric system customers through its Purchased Power Adjustment mechanism in fiscal year 2016, as compared to a $0.5 million over recovery in fiscal year 2015. This under recovery of costs will be collected from customers next fiscal year through adjustments to rates via the Purchased Power Adjustment.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current, restricted and other assets increased $65.4 million or 18.8 percent. The increase was primarily attributable to a $45 million increase in unused bond proceeds. General fund cash (including cash and cash equivalents, short-term investments, and long-term investments) increased $11.8 million. Operating contingency reserves increased $7.8 million. Due to the adoption of a new accounting standard, GASB 68 (See Notes to the Financial Statements), the net pension asset increased $6 million. These increases were partially offset by a $3.5 million decline in other assets, $1.1 million decrease in prepaid expenses, a $0.8 million decrease in gas in storage, and a decrease in inventories of $0.7 million.

Capital Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Capital assets (net) increased $92 million or 5.6 percent. Major capital expenditures (reflected in both plant additions and work in progress) in fiscal year 2016 included $32.6 million related to wastewater Century II projects, $25.1 million for various electric distribution system improvements, $15.1 million for installation of new gas main and service extensions, $13.5 million for main replacement for the water system, $8.4 million for upgrades to various information systems, $8.4 million for utility asset replacements and relocations to accommodate Tennessee Department of Transportation (TDOT) highway improvement projects and $7.5 million for water plant and system improvements.

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Fiscal Year 2015 Compared to Fiscal Year 2014

Capital assets (net) increased $102.3 million or 6.6 percent. Major plant expenditures (reflected in both plant additions and work in progress) during fiscal year 2015 included $28.7 million for various electric distribution system improvements, $25.3 million for Century II projects for the wastewater collection system, $12.5 million for water main replacement, $8.4 million for information system upgrades, $7.8 million for water plant and system improvements, $6 million for gas main replacement and $6 million for pole replacements for the electric system.

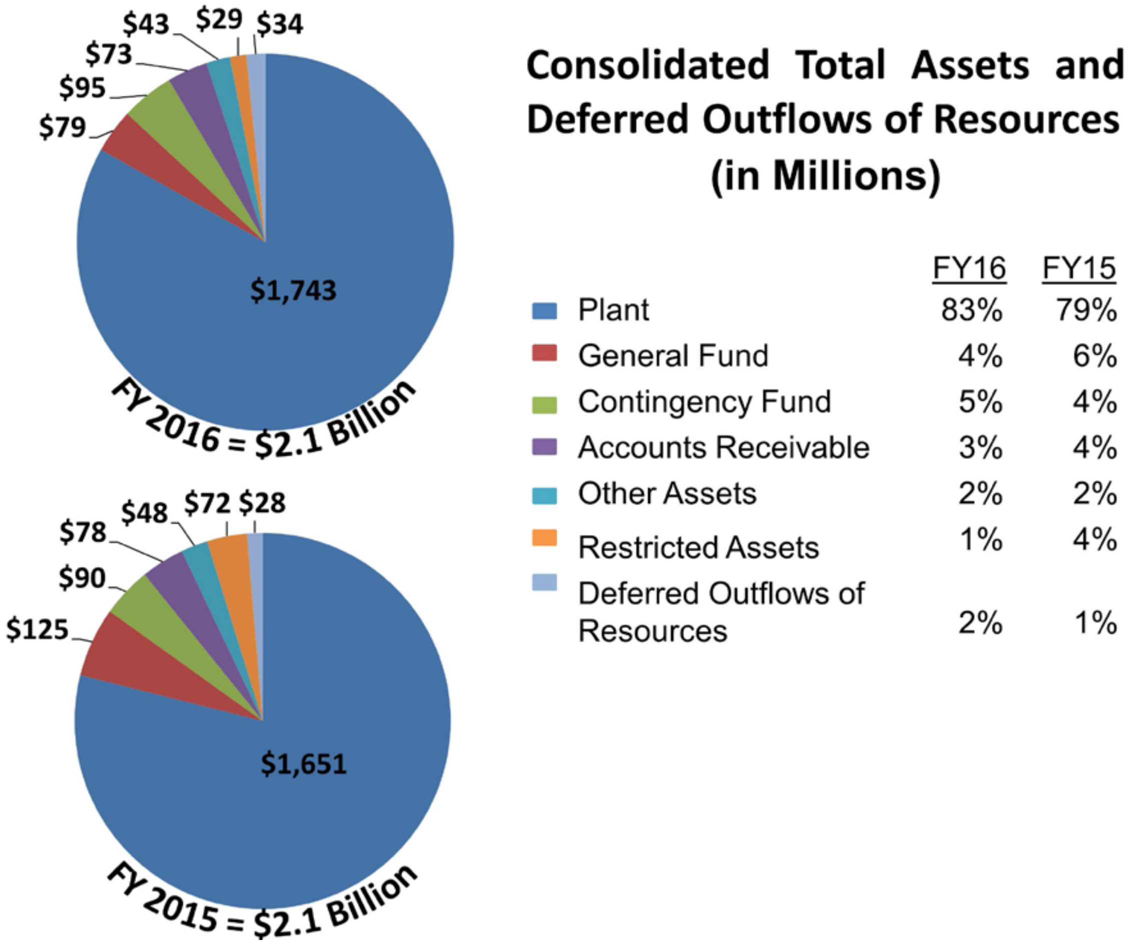
Deferred Outflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred outflows of resources increased $5.8 million compared to the prior year, reflecting an increase in pension outflow of $7.2 million and a $1.4 million decrease in unamortized bonds refunding costs when compared to the prior fiscal year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred outflows of resources increased $16.1 million compared to the prior year, reflecting amortization of deferred losses on bonds refunded during the fiscal year.



Current and Other Liabilities

Fiscal Year 2016 Compared to Fiscal Year 2015

Current and other liabilities increased $7 million or 4.6 percent. This was primarily due to an actuarially determined net pension obligation of $5 million recognized during fiscal year 2016. The current portion of revenue bonds increased $1.2 million and accrued interest on revenue bonds increased $1.5 million. Accrued expenses were $1.9 million higher than the prior fiscal year.

The increases were offset by the reductions to the over recovered purchased power cost and over recovered purchased gas cost liabilities of $0.5 million and $1.1 million, respectively. The over recoveries of cost were flowed back to KUB's electric and gas customers during fiscal year 2016 through adjustments to rates via the Purchased Power Adjustment and Purchased Gas Adjustment.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current and other liabilities decreased $9 million or 5.6 percent. KUB over recovered $1.1 million in wholesale gas costs from its customers in fiscal year 2015, as compared to a $1.3 million over recovery in fiscal year 2014. Over recovery of purchased power expenses decreased $3.9 million in fiscal year 2015. The over recovery of purchased power and gas costs will be refunded to KUB's electric and gas customers through future adjustments to electric and gas rates via the Purchased Power Adjustment and Purchased Gas Adjustment, respectively. Accrued expenses decreased $7.5 million and accounts payable decreased $2.5 million. This decrease was partially offset by an increase in the current portion of debt related to bonds of $4.1 million.

Long-term Debt

Fiscal Year 2016 Compared to Fiscal Year 2015

Long-term debt decreased $32.7 million or 3.3 percent. The decrease was primarily due to $31.1 million of long-term bond debt that shifted to current liabilities as payable within the next year. During the fiscal year, $29.8 million of bond debt was repaid.

Fiscal Year 2015 Compared to Fiscal Year 2014

Long-term debt increased $151.2 million or 17.7 percent. During the fiscal year, $26.2 million of bond debt was repaid. During the fiscal year, KUB issued $163 million in revenue bonds to fund capital improvements for the electric, water and wastewater systems. The increase was partially offset by the scheduled repayment of bond debt.

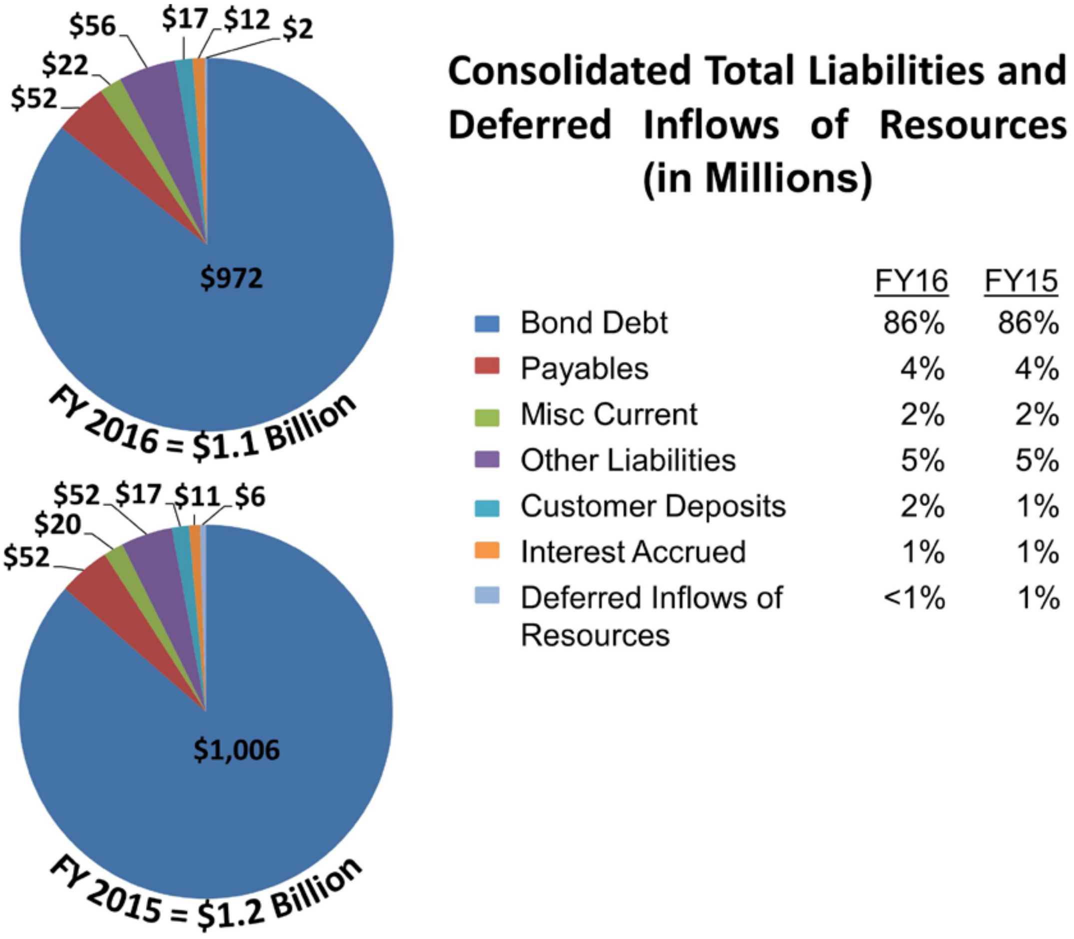
Deferred Inflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred inflows decreased $4.9 million compared to the prior fiscal year due to differences in pension inflows.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred inflows increased $6.4 million compared to the prior fiscal year due to the addition of pension inflow.



Consolidated Total Liabilities and Deferred Inflows of Resources (in Millions)

	FY16	FY15
Bond Debt	86%	86%
Payables	4%	4%
Misc Current	2%	2%
Other Liabilities	5%	5%
Customer Deposits	2%	1%
Interest Accrued	1%	1%
Deferred Inflows of Resources	<1%	1%

Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

Net position increased by $34 million in fiscal year 2016. Net investment in capital assets increased $121.5 million or 18.7 percent, the result of net capital assets increasing $92 million and a $32.7 million decrease in long term debt. Restricted net position increased $1.3 million compared to the prior year. Unrestricted net position decreased $88.9 million or 33.8 percent compared to the previous fiscal year, reflecting a decrease in unused bond proceeds and general fund cash.

Fiscal Year 2015 Compared to Fiscal Year 2014

Net position increased by $35.2 million in fiscal year 2015. Net investment in capital assets decreased $37.9 million or 5.5 percent, the net result of net capital assets increasing $102.3 million offset by the $137.4 million increase in long term debt from new bond issuances. Restricted net position increased $1.7 million compared to the prior year. Unrestricted net position increased $71.4 million or 37.2 percent compared to the previous fiscal year, reflecting increased unused bond proceeds and general fund cash.

Statement of Revenues, Expenses and Changes in Net Position

The following table reflects the condensed consolidated Statement of Revenues, Expenses and Changes in Net Position for KUB compared to the prior year and the year preceding the prior year.

Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended June 30

(in thousands of dollars)	**2016**	**2015**	**2014**
Operating revenues	$ 733,362	$ 763,704	$ 751,710
Less: Purchased energy expense	439,301	479,166	484,074
Margin from sales	294,061	284,538	267,636
Operating expenses			
Treatment	16,618	15,319	14,038
Distribution and collection	59,536	62,319	60,100
Customer service	13,893	13,725	12,607
Administrative and general	33,239	30,741	31,747
Depreciation	68,370	61,708	55,885
Taxes and tax equivalents	31,440	29,649	27,097
Total operating expenses	223,096	213,461	201,474
Operating income	70,965	71,077	66,162
Interest income	1,388	917	852
Interest expense	(39,143)	(37,968)	(37,033)
Other income/(expense)	(408)	1,340	(948)
Change in net position before capital contributions	32,802	35,366	29,033
Capital contributions	1,170	606	736
Change in net position	$ 33,972	$ 35,972	$ 29,769

Normal Impacts on Statement of Revenues, Expenses and Changes in Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Revenues, Expenses and Changes in Net Position presentation.

- Operating revenue is largely determined by volume of sales for the fiscal year. Any change (increase/decrease) in retail rates would also be a cause of change in operating revenue.

- Purchased energy expense is determined by volume of power purchases from TVA and volume of natural gas purchases for the fiscal year. Also, any change (increase/decrease) in wholesale power and/or gas rates would result in a change in purchased energy expense.

- Operating expenses (distribution, customer service, administrative and general) are normally impacted by changes in areas including, but not limited to, labor cost (staffing, wage rates), active employee and retiree medical expenses, and system maintenance.

- Depreciation expense is impacted by plant additions and retirements during the fiscal year.

- Taxes and equivalents are impacted by plant additions/retirements, changes in property tax rates, and gross margin levels.

- Interest income is impacted by level of interest rates and investments.

- Interest expense on debt is impacted by level of outstanding debt and the interest rate(s) on the outstanding debt.

- Other income/(expenses) is impacted by miscellaneous non-operating revenues and expenses.

- Capital contributions are impacted by a donation of facilities/infrastructure to KUB by developers and governmental agencies. The contributions are recognized as revenue and recorded as plant in service based on the fair market value of the asset(s).

Impacts and Analysis

Change in Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

KUB's consolidated net position increased $34 million. This increase was $2 million less than the prior year's change in net position. A restatement to the fiscal year 2014's net position based on a change in method of accounting for pension expense reduced the total net position by $0.8 million during fiscal year 2015.

Fiscal Year 2015 Compared to Fiscal Year 2014

KUB's consolidated net position increased $36 million. This increase was $6.2 million greater than the prior year's change in net position. A restatement to the prior fiscal year's net position based on a change in method of accounting for pension expense reduced the total net position by $0.8 million during fiscal year 2015. This change resulted in a net increase of $35.2 million or 3.9 percent in KUB's consolidated net position.

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Margin from Sales

Fiscal Year 2016 Compared to Fiscal Year 2015

Operating revenue was $30.3 million or 4 percent lower than the previous fiscal year. Sales in both the Electric and Gas Divisions were impacted by the second mildest winter in the last forty years. Electric Division operating revenue decreased $12.2 million due to the net effect of additional revenue from KUB's one percent electric rate increase, a 3.1 percent decline in total power sales, the flow through of TVA rate adjustments and the flow through of prior year over recovered purchased power costs to electric customers. Gas Division revenue decreased $25.7 million for the fiscal year, the net result of 10.2 percent lower billed sales due to the warmer winter, lower purchased gas commodity prices flowed through to customer rates and additional revenue generated from rate increases. Water Division revenue increased $3.1 million, the result of additional revenue from the water rate increases and a 0.8 percent increase in water sales volumes. Wastewater Division revenue was $4.4 million higher than the previous year due to additional revenue from wastewater rate increases, as well as a 1.1 percent increase in wastewater billed volumes.

Wholesale energy expense decreased $39.9 million or 8.3 percent. Purchased power expense decreased $17.4 million compared to last year, due to lower customer demand. Purchased gas expense was $22.5 million lower due to less customer demand and reduced commodity prices for natural gas during the fiscal year.

Margin from sales (operating revenue less purchased energy expense) increased $9.5 million compared to the previous year. The increase reflects additional revenue from the electric, natural gas, water, and wastewater rate increases offset by lower electric and natural gas sales volumes.

Fiscal Year 2015 Compared to Fiscal Year 2014

Operating revenue was $12 million or 1.6 percent higher than the previous fiscal year. Electric Division operating revenue increased $5.9 million, the net result of additional revenue from KUB's electric rate increases, the flow through of TVA rate adjustments and the flow through of prior year over recovered purchased power costs. Gas Division revenue decreased $3 million for the fiscal year, the net result of additional revenue from rate increases effective October 2013 and October 2014 and the flow through of lower wholesale gas commodity costs. Water Division revenue increased $4.8 million, the result of additional revenue from water rate increases and a 1.6 percent increase in water sales volumes. Wastewater Division revenue was $4.3 million higher than the previous year due to additional revenue from the wastewater rate increase effective October 2014 and a 0.9 percent increase in wastewater billed sales volumes.

Wholesale energy expense decreased $4.9 million or 1 percent. Purchased power expense increased $0.7 million compared to last year, the net effect of a 1.5 percent increase to wholesale rate from TVA, coupled with decreased fuel costs. Purchased gas expense was $5.6 million lower, due to lower commodity costs.

Margin from sales (operating revenue less purchased energy expense) increased $16.9 million compared to the previous year. The increase reflects a higher level of gas sales volumes and additional revenue from the electric, gas, water, and wastewater rate increases.

Operating Expenses

Fiscal Year 2016 Compared to Fiscal Year 2015

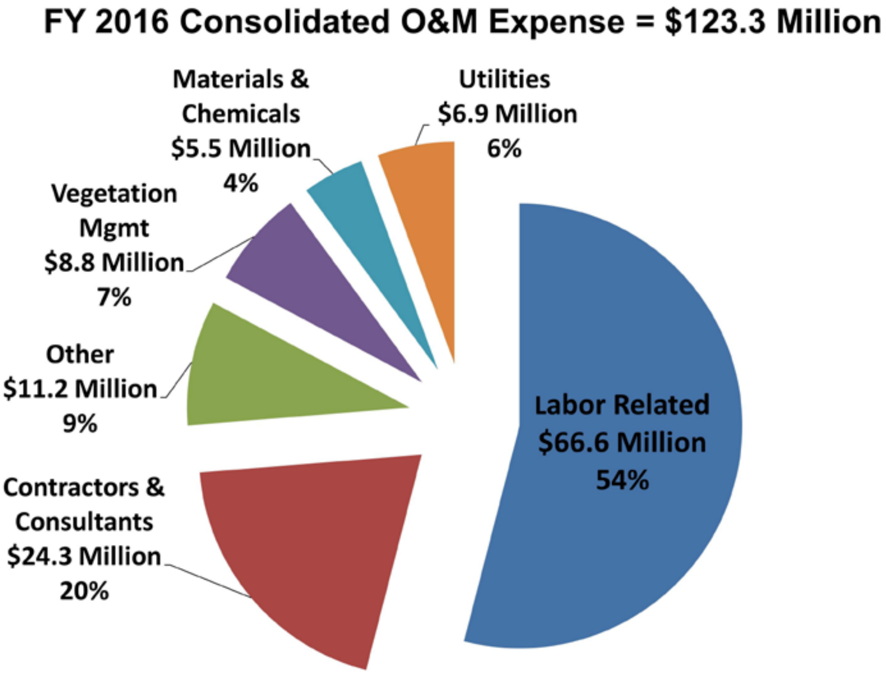
Operating expenses (excluding wholesale purchased energy expense) increased $9.6 million or 4.5 percent compared to fiscal year 2015. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as treatment, distribution and collection, customer service and administrative and general.

- Treatment expenses were $1.3 million or 8.5 percent higher than the prior year, reflecting higher labor related expenses for the water and wastewater system and increased outside contractor expenses for the wastewater system.

- Distribution and collection expenses decreased $2.8 million or 4.5 percent, primarily due to reduced use of outside contractors and consultants offset by increased labor related expenses.

- Customer service expenses rose $0.2 million or 1.2 percent.

- Administrative and general expenses increased $2.5 million or 8.1 percent, primarily due to an increase in pension expense.



- Depreciation expense increased $6.7 million or 10.8 percent. KUB added $94.5 million in assets during fiscal year 2015. A full year of depreciation expense was recorded on these capital investments and a partial year of depreciation expense was incurred on $213.7 million in assets placed in service during fiscal year 2016.

- Taxes and tax equivalents increased $1.8 million or 6 percent due to increased plant in service levels. Tax equivalent payments to taxing jurisdictions in which KUB's utility systems are located are based on a combination of net plant values and margin from sales.

Fiscal Year 2015 Compared to Fiscal Year 2014

Operating expenses (excluding wholesale purchased energy expense) increased $12 million or 5.9 percent compared to fiscal year 2014. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as treatment, distribution and collection, customer service and administrative and general.

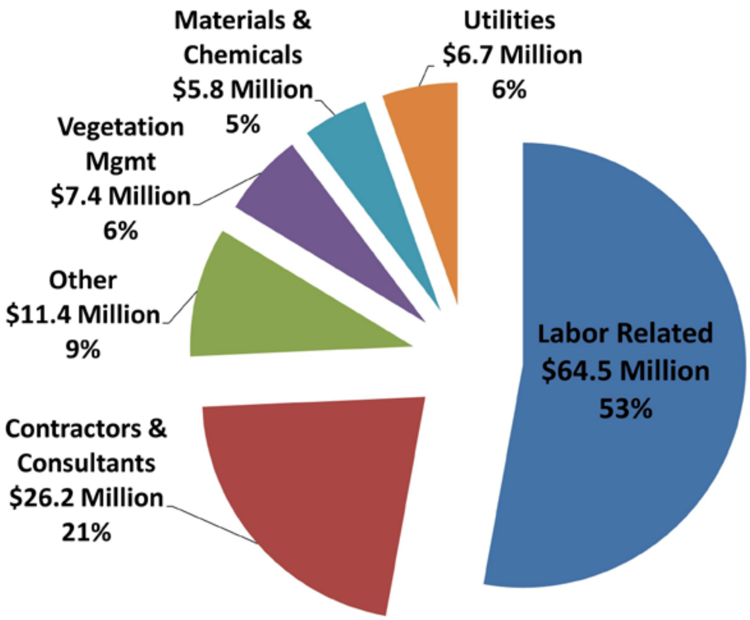
- Treatment expenses were $1.3 million or 9.1 percent higher than the prior year, reflecting an increase in consultant and contractor expenses for the water and wastewater systems.

- Distribution and collection expenses increased $2.2 million or 3.7 percent, primarily the result of restoration expenses related to the February 2015 ice storm, higher labor related expenses, vegetation management expenses, and outside consultant expenses.

- Customer service expenses rose $1.1 million or 8.9 percent, due to an increase in computer software expenses and consultant expense during the fiscal year.

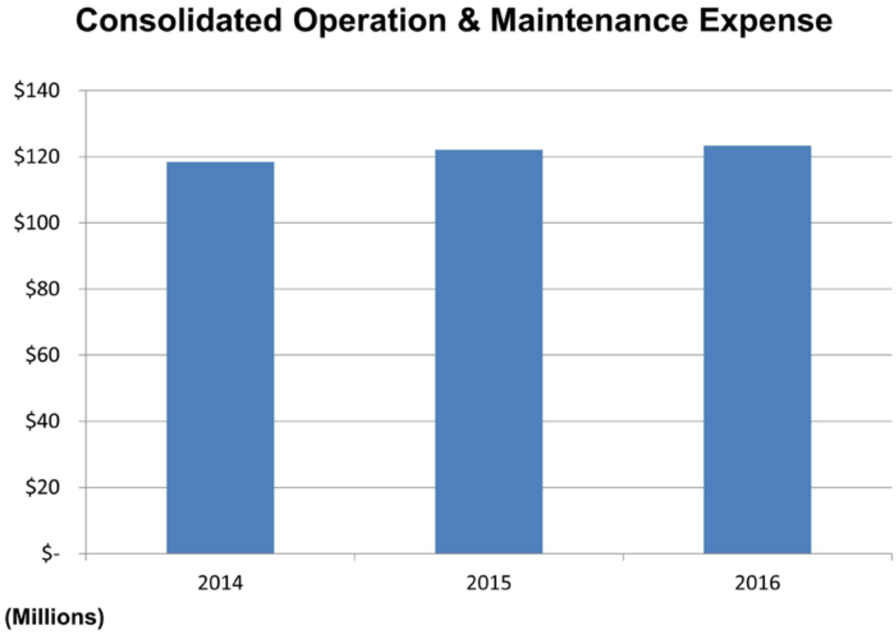
- Administrative and general expenses decreased $1 million or 3.2 percent, primarily due to a decrease in pension expense.

FY 2015 Consolidated O&M Expense = $122.1 Million



- Depreciation expense increased $5.8 million or 10.4 percent. KUB added $174 million in assets during fiscal year 2014. A full year of depreciation expense was recorded on these capital investments during fiscal year 2014 and a partial year of depreciation expense was incurred on $94.5 million in assets placed in service during fiscal year 2015.

- Taxes and tax equivalents increased $2.6 million or 9.4 percent. Tax equivalent payments to taxing jurisdictions in which KUB's utility systems are located are based on a combination of net plant values and margin from sales. The City of Knoxville's property tax rate increased this year and higher plant in service and margin levels both contributed to the growth in tax equivalent payments.



Other Income and Expense

Fiscal Year 2016 Compared to Fiscal Year 2015

Contributions in aid of construction increased $7.4 million compared to the prior fiscal year. This was primarily due to a $4 million contribution from the University of Tennessee, representing the remaining portion of the University's contribution for the natural gas South Loop project.

Interest income increased $0.5 million compared to the prior fiscal year.

Interest expense increased $1.2 million or 3.1 percent, reflecting interest expense from bonds issued in fiscal year 2015.

Other income (net) decreased $1.7 million. Reimbursements of $1.6 million were recognized as non-operating income in fiscal year 2015 for the February 2015 ice storm. KUB recorded a $0.8 million loss on disposition of assets in fiscal year 2016 compared to a $0.1 million loss in fiscal year 2015.

Capital contributions by developers were $0.6 million higher than last fiscal year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Contributions in aid of construction decreased $4.6 million compared to the prior fiscal year. This was due to a $3.9 million contribution from the University of Tennessee during the prior fiscal year, representing a portion of the University's contribution for the South Loop project, a new gas transmission main. The

South Loop project will provide additional capacity to meet the University's increased natural gas demand in the future.

Interest income was consistent with the prior fiscal year.

Interest expense increased $0.9 million or 2.5 percent, reflecting interest expense on $78 million in bonds issued in August 2014, and $85 million in bonds issued in April 2015.

Other income (net) increased $2.3 million, primarily due to $1.6 million in non-operating income from the accrual of the expected reimbursement of electric system restoration expenses related to the February 2015 ice storm. The loss on disposal of property decreased $0.5 million compared to the prior fiscal year.

Capital contributions by developers were $0.1 million lower than last fiscal year.

Capital Assets

Capital Assets
As of June 30
(Net of Depreciation)

(in thousands of dollars)

		2016		2015		2014
Production Plant (Intakes)	$	58	$	62	$	76
Pumping and Treatment Plant		194,450		174,660		177,256
Distribution and Collection Plant						
Mains and metering	$	755,850	$	685,480	$	670,953
Services and meters		92,121		89,086		85,654
Electric station equipment		56,487		34,643		32,797
Poles, towers and fixtures		104,867		93,780		84,332
Overhead conductors		84,937		79,199		73,663
Line transformers		59,587		56,774		55,600
Other accounts		195,751		192,417		191,564
Total Distribution & Collection Plant	**$**	1,349,600	**$**	1,231,379	**$**	1,194,563
General Plant		55,791		51,234		52,149
Total Plant Assets	**$**	1,599,899	**$**	1,457,335	**$**	1,424,044
Work In Progress		143,206		193,812		124,830
Total Net Plant	$	1,743,105	$	1,651,147	$	1,548,874

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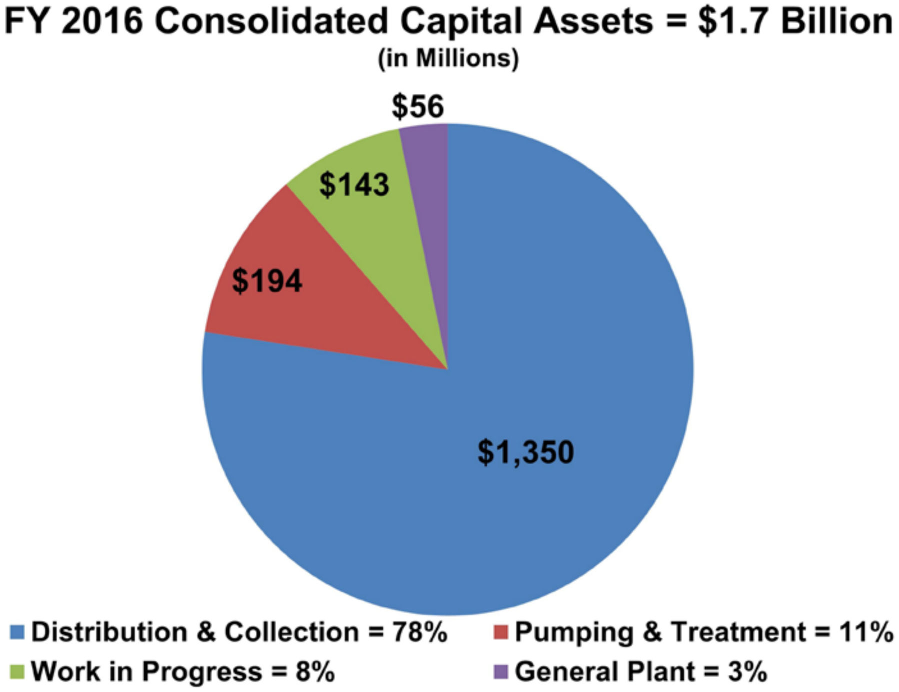
Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, KUB had $1.7 billion invested in capital assets, as reflected in the schedule of Capital Assets, which represents a net increase (including additions, retirements, and depreciation) of $92 million or 5.6 percent over the end of the last fiscal year.

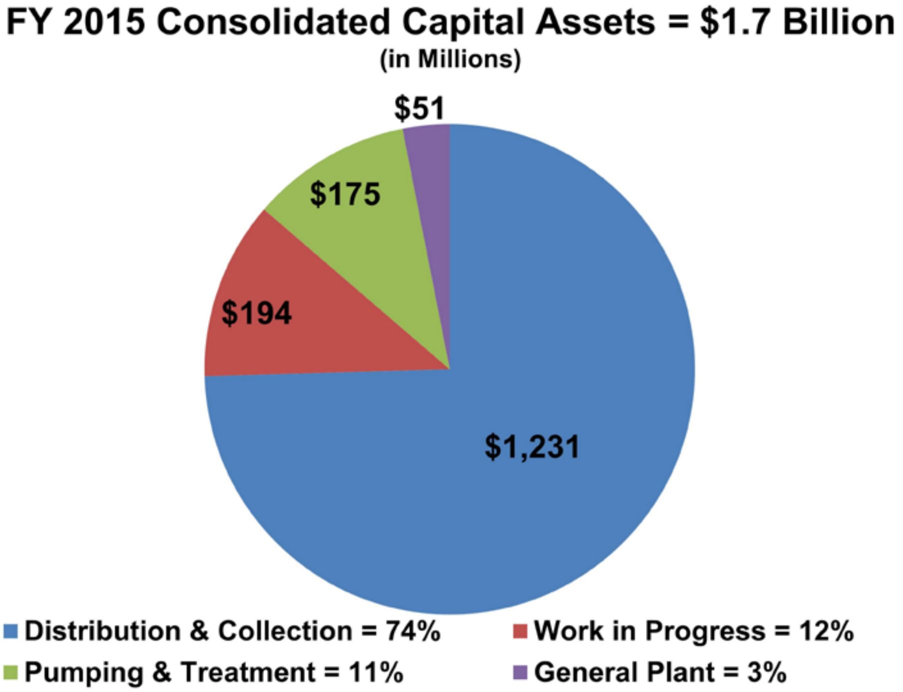


Major capital asset additions during the year were as follows:

- $32.6 million related to wastewater Century II projects
    - $15.8 million for sewer mini-basin rehabilitation and replacement
    - $7.7 million for sewer trunk line rehabilitation and replacement
    - $5.3 million for pump station design and construction
    - $3.8 million for wastewater treatment plant upgrades
- $25.1 million for various electric distribution system improvements
- $15.1 million for installation of new gas main and service extensions
- $13.5 million for main replacement for the water system
- $8.4 million for upgrades to various information systems
- $8.4 million for replacement and relocation of utility assets to accommodate TDOT highway improvement projects
- $7.7 million for pole replacements for the electric system
- $7.5 million for water plant and system improvements

Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, KUB had $1.7 billion invested in capital assets, as reflected in the schedule of Capital Assets, which represents a net increase (including additions, retirements, and depreciation) of $102.3 million or 6.6 percent over the end of the last fiscal year.



Major capital asset additions during the year were as follows:

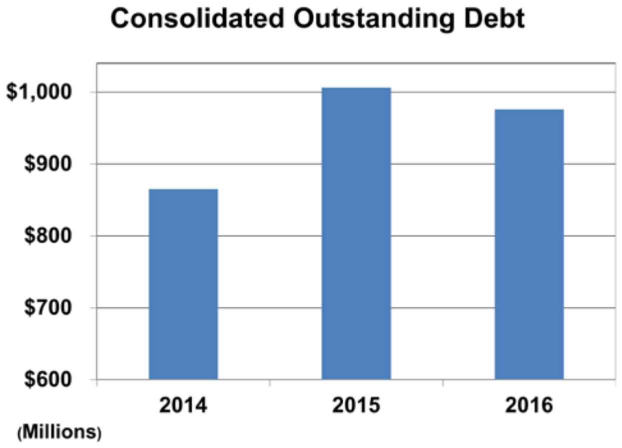
- $28.7 million for various electric distribution system improvements
- $25.3 million related to wastewater Century II projects
  - $20.4 million for sewer mini-basin rehabilitation and replacement
  - $2.6 million for pump station design and construction
  - $1.3 million for wastewater treatment plant upgrades
  - $1 million for sewer trunk line rehabilitation and replacement
- $12.5 million for main replacement for the water system
- $8.4 million for information system upgrades
- $7.8 million for water plant and system improvements
- $6 million for gas main replacement
- $6 million for pole replacements for the electric system

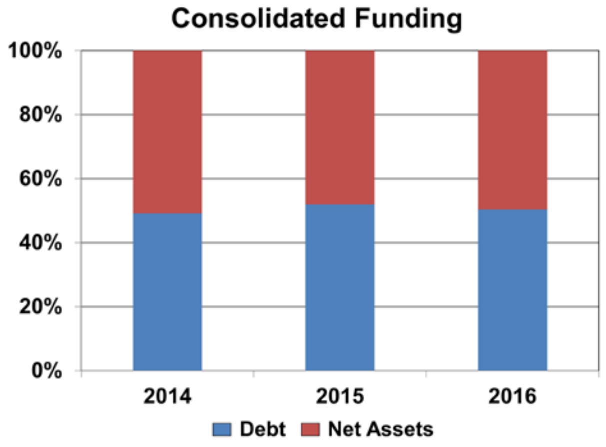
Debt Administration

KUB's outstanding debt was $976.4 million at June 30, 2016. No new debt was issued in fiscal year 2016. Debt as a percentage of capital structure was 50.4 percent in 2016, 52 percent in 2015 and 49.2 percent at the end of fiscal year 2014.

Outstanding Debt
As of June 30

(in thousands of dollars)	**2016**	**2015**	**2014**
Revenue bonds	$ 976,430	$ 1,006,260	$ 864,740
Total outstanding debt	$ 976,430	$ 1,006,260	$ 864,740





KUB will pay $365.1 million in principal payments over the next ten years, representing 37.4 percent of outstanding bonds.

Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, KUB had $976.4 million in outstanding debt (including the current portion of revenue bonds) compared to $1 billion last year, a decrease of $29.8 million. KUB's weighted average cost of debt as of June 30, 2016 was 3.95 percent.

KUB's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2016, Standard & Poor's rated the revenue bonds of the Water Division AAA, the Electric and Wastewater Divisions AA+ and the revenue bonds of the Gas Division AA. Moody's Investors Service rated the bonds of all four Divisions Aa2.

Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, KUB had $1 billion in outstanding debt (including the current portion of revenue bonds) compared to $864.7 million last year, an increase of $141.5 million. KUB's weighted average cost of debt as of June 30, 2015 was 3.95 percent.

During fiscal year 2015, $26.2 million in bonds were repaid.

In August 2014, KUB issued $78 million of new revenue bonds to fund capital system improvements, including $40 million for the electric system, $8 million for the water system and $30 million for the wastewater system.

In April 2015, KUB issued $85 million of new revenue bonds to fund capital system improvements, including $35 million for the electric system, $20 million for the water system and $30 million for the wastewater system.

In April 2015, KUB issued $193.2 million in revenue refunding bonds to refinance certain outstanding bonds, including $28.6 million for the electric system, $11.8 million for the gas system, $23 million for the water system and $129.8 million for the wastewater system. The refunding of certain bonds at lower interest rates will provide debt service savings of $19.2 million over the life of the bonds

KUB's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2015, Standard & Poor's rated the revenue bonds of the Water Division AAA, the Electric and Wastewater Divisions AA+ and the revenue bonds of the Gas Division AA. Moody's Investors Service rated the bonds of all four Divisions Aa2. The Standard and Poor's water rating represented an upgrade for water system bonds and the highest credit rating available from Standard and Poor's. In the rating report on the water system bonds, Standard & Poor's stated "the upgrade is based on the water system's extremely strong financial risk profile, which we view as sustainable over time after reviewing management's long-term financial forecast."

Impacts on Future Financial Position

KUB anticipates net customer growth of 2,550 customers during fiscal year 2017.

In June 2014, the KUB Board adopted three years of rate increases for all four Divisions to help fund the ongoing Century II infrastructure programs for each system. Two of those rate increases have gone into effect.

The remaining electric rate increase will be effective July 2016. The rate increase will provide $5.2 million in additional annual Electric Division revenue.

The remaining natural gas rate increase will be effective October 2016. The rate increase will result in $1.8 million in additional annual Gas Division revenue.

The remaining water rate increase will be effective July 2016. The rate increase will result in additional annual Water Division revenue of $2 million.

The remaining wastewater rate increase will be effective October 2016. The wastewater rate increase will provide additional annual revenue of $4.7 million.

In April 2016, KUB management presented the fiscal year 2017 budget to the KUB Board of Commissioners that accommodates the projected level of capital investment for the fiscal year. Over the course of the next ten years KUB plans to spend $108 million dollars on Grid Modernization. In July 2016, the four-year deployment of advanced meters began.

KUB sold $40 million in electric system revenue bonds in July 2016 for the purpose of funding electric system capital improvements. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.75 percent.

KUB sold $12 million in natural gas system revenue bonds in July 2016 for the purpose of funding natural gas system capital improvements. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.78 percent.

KUB sold $25 million in water system revenue bonds in July 2016 for the purpose of funding water system capital improvements. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.72 percent.

KUB sold $20.9 million in water system revenue refunding bonds in July 2016 for the purpose of refinancing existing debt at lower interest rates. KUB will realize a total debt service savings of $2.5 million over the life of the bonds ($2.2 million on a net present value basis). The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.07 percent.

As part of the rating process for the $25 million in revenue bonds and $20.9 million in revenue refunding bonds, Moody's upgraded its rating on KUB's water system bonds to Aa1 from Aa2. Aa1 is the second to highest bond credit rating assigned by Moody's Investors Service. In its formal rating report, Moody's stated "the upgrade to Aa1 reflects the well-managed financial operations of the water system that continues to provide for solid debt service coverage and liquidity, a mature service area, and a manageable debt profile." The AAA bond rating from Standard and Poor's was reaffirmed. In its formal rating report on the water bonds Standard and Poor's noted "based on our financial management assessment we view KUB to be "1" on a scale of 1-6, with "1" being the strongest."

KUB sold $20 million in wastewater system revenue bonds in July 2016 for the purpose of funding wastewater system capital improvements. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.72 percent.

KUB long-term debt includes $130.4 million of Build America Bond (BABs). The BABs were sold on a taxable basis with the United States Treasury providing a rebate to KUB for a percentage of the interest cost. The interest rebates were subject to federal sequestration during the fiscal year and were reduced by 6.8 percent. Any future actions by Congress may also affect the anticipated rebates for future fiscal years.

GASB Statement No. 82, *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73* is effective for fiscal years beginning after June 15, 2016. GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* and GASB No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* are effective for periods beginning after June 15, 2017. KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

No other facts, decisions, or conditions are currently known which would have a significant impact on KUB's financial position or results of operations during fiscal year 2016.

Financial Contact

KUB’s financial statements are designed to present users (citizens, customers, investors, and creditors) with a general overview of KUB’s financial position and results of operations for the fiscal years ending June 30, 2016 and 2015. If you have questions about the statements or need additional financial information, contact KUB’s Chief Financial Officer at 445 South Gay Street, Knoxville, Tennessee 37902.

Knoxville Utilities Board
Consolidated Statements of Net Position
June 30, 2016 and 2015

		2016		2015
Assets and Deferred Outflows of Resources				
Current assets:				
Cash and cash equivalents	$	78,946,397	$	124,892,534
Short-term contingency fund investments		25,699,396		6,296,090
Other current assets		859,383		1,638,388
Accrued interest receivable		43,237		43,229
Accounts receivable, less allowance of uncollectible accounts of $805,684 in 2016 and $720,939 in 2015		72,945,320		77,844,543
Inventories		10,524,829		8,421,065
Prepaid expenses		886,725		809,844
Gas storage		8,010,091		9,447,403
Total current assets		197,915,378		229,393,096
Restricted assets:				
Bond funds		28,935,445		26,154,107
Other funds		21,418		43,897
Unused bond proceeds		-		46,053,950
Total restricted assets		28,956,863		72,251,954
Plant in service		2,397,423,083		2,210,535,681
Less accumulated depreciation		(797,524,421)		(753,200,620)
		1,599,898,662		1,457,335,061
Retirement in progress		1,327,498		940,386
Construction in progress		141,878,991		192,871,763
Net plant in service		1,743,105,151		1,651,147,210
Other assets:				
Net pension asset		-		6,021,629
Long-term contingency fund investments		69,184,035		84,036,694
TVA conservation program receivable		8,153,192		10,109,135
Under recovered purchased power cost		1,379,643		-
Under recovered purchased gas cost		2,178,653		-
Other		10,882,837		11,248,778
Total other assets		91,778,360		111,416,236
Total assets		2,061,755,752		2,064,208,496
Deferred outflows of resources:				
Pension outflow		10,357,291		3,157,199
Unamortized bond refunding costs		23,877,411		25,230,799
Total deferred outflows of resources		34,234,702		28,387,998
Total assets and deferred outflows of resources	$	2,095,990,454	$	2,092,596,494

The accompanying notes are an integral part of these consolidated financial statements.

Knoxville Utilities Board
Consolidated Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Liabilities, Deferred Inflows, and Net Position		
Current liabilities:		
Current portion of revenue bonds	$ 31,050,000	$ 29,830,000
Sales tax collections payable	1,238,516	1,251,145
Accounts payable	50,663,005	50,651,280
Accrued expenses	21,610,050	19,729,155
Customer deposits plus accrued interest	17,135,891	16,465,292
Accrued interest on revenue bonds	12,755,853	11,306,248
Total current liabilities	134,453,315	129,233,120
Other liabilities:		
TVA conservation program	8,412,853	10,336,682
Accrued compensated absences	9,061,226	8,616,844
Customer advances for construction	2,247,599	2,305,058
Net pension liability	5,040,160	-
Over recovered purchased power cost	-	500,522
Over recovered purchased gas cost	-	1,063,761
Other	303,673	478,797
Total other liabilities	25,065,511	23,301,664
Long-term debt:		
Revenue bonds	945,380,000	976,430,000
Unamortized premiums/discounts	26,985,541	28,631,810
Total long-term debt	972,365,541	1,005,061,810
Total liabilities	1,131,884,367	1,157,596,594
Deferred inflows of resources:		
Pension inflow	1,512,267	6,378,310
Total deferred inflows of resources	1,512,267	6,378,310
Total liabilities and deferred inflows of resources	1,133,396,634	1,163,974,904
Net position		
Net investment in capital assets	772,012,085	650,464,457
Restricted for:		
Debt service	16,179,592	14,847,859
Other	21,418	43,896
Unrestricted	174,380,725	263,265,378
Total net position	962,593,820	928,621,590
Total liabilities, deferred inflows, and net position	$ 2,095,990,454	$ 2,092,596,494

The accompanying notes are an integral part of these consolidated financial statements.

Knoxville Utilities Board
Consolidated Statements of Revenues, Expenses and Changes in Net Position
June 30, 2016 and 2015

	2016	2015
Operating revenues		
Electric	$ 515,031,267	$ 527,233,806
Gas	88,193,346	113,850,059
Water	46,899,326	43,777,160
Wastewater	83,238,147	78,842,964
Total operating revenues	733,362,086	763,703,989
Operating expenses		
Purchased power	398,205,855	415,610,969
Purchased gas	41,095,212	63,555,513
Treatment	16,617,907	15,318,610
Distribution and collection	59,535,776	62,318,632
Customer service	13,893,287	13,725,067
Administrative and general	33,239,284	30,741,405
Provision for depreciation	68,369,697	61,708,086
Taxes and tax equivalents	31,439,759	29,648,873
Total operating expenses	662,396,777	692,627,155
Operating income	70,965,309	71,076,834
Non-operating revenues (expenses)		
Contributions in aid of construction	10,258,938	2,871,465
Interest and dividend income	1,388,168	916,983
Interest expense	(39,142,974)	(37,967,821)
Amortization of debt costs	(297,772)	(225,173)
Write-down of plant for costs recovered through contributions	(10,258,938)	(2,871,465)
Other	(110,775)	1,565,032
Total non-operating revenues (expenses)	(38,163,353)	(35,710,979)
Change in net position before capital contributions	32,801,956	35,365,855
Capital contributions	1,170,274	605,907
Change in net position	33,972,230	35,971,762
Net position, beginning of year, as previously reported	928,621,590	893,413,803
Change in method of accounting for pension	-	(763,975)
Net position, beginning of year, as restated	928,621,590	892,649,828
Net position, end of year	$ 962,593,820	$ 928,621,590

The accompanying notes are an integral part of these consolidated financial statements.

Knoxville Utilities Board
Consolidated Statements of Cash Flows
June 30, 2016 and 2015

		2016		2015
Cash flows from operating activities:				
Cash receipts from customers	$	735,166,499	$	761,548,382
Cash receipts from other operations		14,425,337		11,720,197
Cash payments to suppliers of goods or services		(524,357,750)		(569,272,217)
Cash payments to employees for services		(55,202,648)		(50,466,843)
Payment in lieu of taxes		(27,404,220)		(25,910,417)
Cash receipts from collections of TVA conservation loan program participants		3,067,056		3,046,131
Cash payments for TVA Conservation loan program		(3,034,941)		(3,071,013)
Net cash provided by operating activities		142,659,333		127,594,220
Cash flows from capital and related financing activities:				
Net proceeds from bond issuance		-		165,499,847
Principal paid on revenue bonds and notes payable		(29,830,000)		(26,240,000)
(Increase) decrease in unused bond proceeds		46,053,950		(44,998,540)
Interest paid on revenue bonds and notes payable		(37,693,370)		(37,130,082)
Acquisition and construction of plant		(171,820,155)		(168,110,486)
Changes in bond funds, restricted		(2,781,338)		(1,491,853)
Customer advances for construction		301,071		697,695
Proceeds received on disposal of plant		269,540		-
Cash received from developers and individuals for capital purposes		10,258,938		2,871,465
Net cash used in capital and related financing activities		(185,241,364)		(108,901,954)
Cash flows from investing activities:				
Purchase of investment securities		(10,460,222)		(20,286,901)
Maturities of investment securities		6,292,200		19,495,562
Interest received		1,388,160		903,509
Other property and investments		(584,244)		9,256
Net cash provided by (used in) investing activities		(3,364,106)		121,426
Net increase (decrease) in cash and cash equivalents		(45,946,137)		18,813,692
Cash and cash equivalents, beginning of year		124,892,534		106,078,842
Cash and cash equivalents, end of year	$	78,946,397	$	124,892,534
Reconciliation of operating income to net cash provided by operating activities				
Operating income	$	70,965,309	$	71,076,834
Adjustments to reconcile operating income to net cash provided by operating activities:				
Depreciation expense		70,236,319		63,406,737
Changes in operating assets and liabilities:				
Accounts receivable		4,980,351		1,848,310
Inventories		(2,103,762)		669,347
Prepaid expenses		1,360,432		881,113
TVA conservation program receivable		1,874,818		523,680
Other assets		576,770		(2,942,632)
Sales tax collections payable		(12,629)		52,021
Accounts payable and accrued expenses		1,332,656		(4,201,309)
TVA conservation program payable		(1,923,829)		(548,563)
Unrecovered purchased power cost		(1,880,165)		(3,912,247)
Underrecovered gas costs		(3,242,414)		(214,383)
Customer deposits plus accrued interest		670,600		732,639
Other liabilities		(175,123)		222,673
Net cash provided by operating activities	$	142,659,333	$	127,594,220
Noncash capital activities:				
Acquisition of plant assets through developer contributions	$	1,170,274	$	605,907

The accompanying notes are an integral part of these consolidated financial statements.

1. Description of Business:

Knoxville Utilities Board (KUB), comprised of the Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions including setting rates. KUB's accounts are maintained in conformity with the Uniform System of Accounts of the Federal Energy Regulatory Commission (FERC), the Uniform System of Accounts of the National Association of Regulatory Utility Commissioners (NARUC), and the Governmental Accounting Standards Board (GASB), as applicable.

2. Significant Accounting Policies:

Basis of Accounting

In conformity with Generally Accepted Accounting Principles (GAAP), KUB follows the provisions of GASB Statement No. 34 (Statement No. 34), *Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* as amended by GASB Statement No. 63 (Statement No. 63), *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position.* Statement No. 34 established standards for external financial reporting for all state and local governmental entities. Under Statement No. 63, financial statements include deferred outflows of resources and deferred inflows of resources, in addition to assets and liabilities, and will report *net position* instead of net assets. In addition, KUB follows GASB Statement No. 62 (Statement No. 62), *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* as it relates to certain items for regulatory accounting. Regulatory accounting allows a regulated utility to defer a cost (a regulatory asset) or recognize an obligation (a regulatory liability) if it is probable that through the rate making process, there will be a corresponding increase or decrease in future revenues. Accordingly, KUB has recognized certain regulatory assets and regulatory liabilities in the accompanying Statements of Net Position.

The consolidated financial statements are prepared on the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred. The accounting and financial reporting treatment applied is determined by measurement focus. The transactions are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the Statement of Net Position. Net position (i.e., total assets and deferred outflows of resources net of total liabilities and deferred inflows of resources) is segregated into net investment in capital assets, restricted for capital activity and debt service, and unrestricted components.

Recently Adopted New Accounting Pronouncements

In February 2015, the Governmental Accounting Standards Board (GASB) issued Statement No. 72 (Statement No. 72), *Fair Value Measurement and Application.* Statement No. 72 is intended to provide guidance for determining a fair value measurement for financial reporting purposes and for applying fair value to certain investments and disclosures related to all fair value measurements.

In June 2015, the GASB issued GASB Statement No. 73 (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 Provision of GASB Statements 67 and 68.* The requirements of this Statement will improve financial reporting by establishing a single framework for the presentation of information about pensions and enhance comparability.

In June 2015, the GASB issued GASB Statement No. 76 (Statement No. 76), *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to simplify the hierarchy of generally accepted accounting principles (GAAP) used to prepare financial statements of state and local governmental entities. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments,* and amends Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, paragraphs 64, 74, and 82.

In December 2015, the GASB issued GASB Statement No. 79 (Statement No. 79), *Certain External Investment Pools and Pool Participants.* This statement establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes.

Statements No. 72, 73, 76, and 79 are effective for fiscal years beginning after June 15, 2015.

Principles of Consolidation

The consolidated financial statements include the accounts of the Electric, Gas, Water and Wastewater Divisions. All significant intercompany balances and transactions have been eliminated in consolidation.

KUB issues separate financial reports, which include financial statements and required supplementary information, for the Electric, Gas, Water, and Wastewater Divisions. These reports may be obtained by writing Knoxville Utilities Board, P.O. Box 59017, Knoxville, TN 37950-9017.

Plant

Plant and other property are stated on the basis of original cost. The costs of current repairs and minor replacements are charged to operating expense. The costs of renewals and improvements are capitalized. The original cost of utility plant assets retired or otherwise disposed of and the cost of removal less salvage value is charged to accumulated depreciation. When other property is retired, the related asset and accumulated depreciation are removed from the accounts, and the gain or loss is included in the results of operations.

The provision for depreciation of plants in service is based on the estimated useful lives of the assets, which range from three to sixty-seven years, and is computed using the straight-line method. Pursuant to FERC/NARUC, the caption "Provision for depreciation" in the consolidated Statements of Revenues, Expenses and Changes in Net Position does not include depreciation for transportation equipment of $1,866,622 in fiscal year 2016 and $1,698,650 in fiscal year 2015. Under regulatory accounting, interest costs are expensed as incurred with construction of plant assets.

Operating Revenue

Operating revenue consists primarily of charges for services provided by the principal operations of KUB. Operating revenue is recorded when the service is rendered, on a cycle basis, and includes an estimate of unbilled revenue. Revenues are reported net of bad debt expense of $1,820,030 in fiscal year 2016 and $2,504,785 in fiscal year 2015.

Non-operating Revenue

Non-operating revenue consists of revenues that are related to financing and investing types of activities and result from non-exchange transactions or ancillary activities.

Expense

When an expense is incurred for purposes for which there are both restricted and unrestricted assets available, it is KUB’s policy to apply those expenses to restricted assets to the extent such are available and then to unrestricted assets.

Net Position

GASB Statement No. 63 requires the classification of net position into three components – net investment in capital assets; net position-restricted; and net position-unrestricted.

These classifications are defined as follows:

- Net investment in capital assets – This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt also should be included in this component of net position. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

- Net position-restricted – This component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported.

- Net position-unrestricted – This component of net position consists of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

Contributions in Aid of Construction and Capital Contributions

Contributions in aid of construction are cash collections from customers or others for a particular purpose, generally the construction of new facilities to serve new customers in excess of the investment KUB is willing to make for a particular incremental revenue source. KUB reduces the plant account balances to which contributions relate by the actual amount of the contribution and recognizes the contributions as non-operating revenue in accordance with Statement No. 62.

Capital contributions represent contributions of utility plant infrastructure constructed by developers and others in industrial parks and other developments, and transferred to KUB upon completion of construction and the initiation of utility service. In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, such contributions are recognized as revenues and capital assets upon receipt.

Inventories

Inventories, consisting of plant materials and operating supplies, are valued at the lower of average cost or replacement value.

Change in Method of Accounting for Pension

In June 2012, the Governmental Accounting Standards Board (GASB) issued Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, which revises existing standards of financial reporting for pensions. In addition, during November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, which requires deferred outflow of resources to be recognized for any contributions made subsequent to the measurement date of the beginning net pension liability. These standards were adopted by KUB in 2015 and resulted in a restatement of 2015 beginning net position of $763,975.

Pension Plan

KUB's employees are participants in the Knoxville Utilities Board Pension Plan as authorized by the Charter of the City of Knoxville §1107(J) (Note 10). KUB's policy is to fully fund the annual actuarially determined contributions. As required by GASB Statement No. 68, KUB measures net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30, 2016 and 2015 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 are based on a December 31, 2015 and 2014 measurement date, respectively.

Investments

Investments are carried at fair value as determined by quoted market prices at the reporting date.

Self-Insurance

KUB has established self-insurance programs covering portions of workers' compensation, employee health, environmental liability, general liability, property and casualty liability, and automobile liability claims. A liability is accrued for claims as they are incurred. When applicable, claims in excess of the self-insured risk are covered by KUB's insurance carrier. Additionally, KUB provides certain lifetime health benefits to eligible retired employees under a self-insurance plan administered by a third party.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates are based on historical experience and various other assumptions that KUB believes are reasonable under the circumstances. However, future events are subject to change and the best estimates and judgments routinely require adjustment. Estimates are used for, but not limited to, inventory valuation, allowance for uncollectible accounts, depreciable lives of plant assets, unbilled revenue volumes, pension trust valuations, OPEB trust valuations, insurance liability reserves, and potential losses from contingencies and litigation. Actual results could differ from those estimates.

Restricted and Designated Assets

Certain assets are restricted by bond resolutions for the construction of utility plant and debt repayment. Certain additional assets are designated by management for contingency purposes and economic development.

Cash Equivalents

For purposes of the Statements of Cash Flows, KUB considers all unrestricted and undesignated highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

Deferred Outflows and Inflows of Resources

Deferred outflows of resources are items previously reported as assets related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. Deferred inflows of resources are items previously reported as liabilities related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. Deferred outflows of resources also include employer pension contributions made subsequent to the measurement date of the net pension liability and before the end of the employer's reporting period in accordance with Statement No. 71. Deferred inflows and deferred outflows also include the net difference between projected and actual earnings on pension plan investments and differences between expected and actual experience in accordance with Statement No. 68.

Debt Premium/Discount

KUB records unamortized premium and discount on debt as a separate line item in the Long Term Debt section of the Financial Statements. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Debt Issuance Costs

In accordance with regulatory accounting, KUB records debt issuance costs as an Other Asset. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Deferred Gain/Loss on Refunding of Debt

KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. In accordance with FERC presentation, amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Compensated Absences

KUB accrues a liability for earned but unpaid paid-time off (PTO) days.

TVA Conservation Program

KUB previously served as a fiscal intermediary for TVA whereby loans were made to KUB customers by TVA to be used in connection with TVA's Energy Right Residential Program. While KUB still holds existing loans, no loans were made through this program after October 31, 2015.

Subsequent Events

KUB has evaluated events and transactions through October 27, 2016, the date these financial statements were issued, for items that should potentially be recognized or disclosed. KUB sold $40 million in electric system revenue bonds in July 2016 for the purpose of funding electric system capital improvements in fiscal year 2017. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.75 percent. KUB sold $12 million in natural gas system revenue bonds in July 2016 for the purpose of funding natural gas system capital improvements in fiscal year 2017. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.78 percent. KUB sold $25 million in water system revenue bonds in July 2016 for the purpose of funding water system capital improvements in fiscal year 2017. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.72 percent. KUB sold $20.9 million in water system revenue refunding bonds in July 2016 with an average interest rate of 2.5 percent to advance refund $19.9 million of outstanding bonds with an average interest rate of 4.18 percent. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.07 percent. The net proceeds of $22 million (after payment of $0.3 million in underwriting fees and other issuance costs plus premium of $1 million and an additional issuer equity contribution of $0.4 million) were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the bonds. As a result, the bonds will be considered defeased and the liability for those bonds will be removed from the financial statements. This refunding decreases total debt service payments over the next 17 years by $2.5 million resulting in an economic gain (difference between the present values of the debt service payments on the old and new debt) of $2.2 million. KUB sold $20 million in wastewater system revenue bonds in July 2016 for the purpose of funding wastewater system capital improvements in fiscal year 2017. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.72 percent.

Purchased Power Adjustment

In October 2002, the Board adopted a Purchased Power Adjustment (PPA) to address changes in wholesale power costs. The PPA was established in response to an amendment to KUB's power supply contract under which, among other things, TVA relinquished its regulatory authority over KUB retail electric rates. The PPA allows KUB to promptly adjust retail electric rates in response to wholesale rate changes or adjustments, thus ensuring that KUB will recover the costs incurred for purchased power. These changes in electric costs are reflected as adjustments to the base electric rates established by the Board. The rate-setting authority vested in the Board by the City Charter meets the "self-regulated" provisions of Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, and KUB meets the remaining criteria of Statement No. 62.

TVA implemented a fuel cost adjustment in October 2006 applied on a quarterly basis to wholesale power rates. TVA's quarterly fuel cost adjustment became a monthly fuel cost adjustment effective October 2009. KUB flows changes to wholesale power rates from TVA's fuel cost adjustment mechanism directly through to its retail electric rates via the PPA.

In April 2011, TVA modified its wholesale rate structure to demand and energy billing for its distributors. In response, KUB revised its PPA to include a deferred accounting component to ensure appropriate matching of revenue and expense and cost recovery. KUB will adjust its retail rates on an annual basis to flow any over or under recovery of wholesale power costs through to its customers via the PPA.

Under the PPA mechanism, KUB tracks the actual over/(under) recovered amount in the Over/(Under) Recovered Purchased Power Costs accounts. These accounts are rolled into the PPA rate adjustments thereby assuring that any over/(under) recovered amounts are promptly passed on to the KUB's electric customers. The amount of over/(under) recovered cost was ($1,379,643) at June 30, 2016 and $500,522 at June 30, 2015.

Purchased Gas Adjustment

In November 1990, the Board implemented a deferred Purchased Gas (Cost) Adjustment (PGA) mechanism, which allows KUB to flow changes in purchased gas costs through to its customers. These changes in gas costs are reflected as adjustments to the base gas rates established by the Board. The rate-setting authority vested in the Board by the City Charter meets the "self-regulated" provisions of GASB Statement No. 62 (Statement No. 62), *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*.

The PGA is intended to assure that KUB recovers the total cost of natural gas purchased, transported and/or reserved for delivery to its sales and transportation customers on an equitable basis. The PGA is also intended to assure that no excess or deficient cost recovery from KUB's customers occurs.

Under the PGA mechanism, KUB tracks the actual over/(under) recovered amount in the Over/(Under) Recovered Purchased Gas Costs accounts. These accounts are rolled into the PGA rate adjustment on June 30 of each year thereby assuring that any over/(under) recovered amounts are passed on to KUB's gas system customers. The amount of over/(under) recovered cost was ($2,178,653) at June 30, 2016 and $1,063,761 at June 30, 2015.

Recently Issued Accounting Pronouncements

In June 2015, the GASB issued two related Statements that affect accounting and financial reporting by state and local governments for postemployment benefits other than pensions (OPEB). GASB Statement No. 74 (Statement No. 74), *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* addresses reporting by OPEB plans that administer benefits on behalf of governments. GASB Statement No. 75 (Statement No. 75), *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* addresses reporting by governments that provide OPEB to their employees. Statement No. 74 is effective for fiscal years beginning after June 15, 2016, and Statement No. 75 is effective for fiscal years beginning after June 15, 2017.

In March 2016, the GASB issued GASB Statement No. 82 (Statement No. 82), *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to the presentation of payroll-related measures in required supplementary information, the selection of assumptions and treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes and the classification of payments made by employers to satisfy employee contribution obligations. Statement No. 82 is effective for fiscal years beginning after June 15, 2016.

KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

3. Deposits and Investments

KUB follows the provisions of Statement No. 40 of the Governmental Accounting Standards Board, *Deposit and Investment Risk Disclosures an amendment of GASB Statement No. 3*. This Statement establishes and modifies disclosure requirements for state and local governments related to deposit and investment risks. KUB classifies its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*.

KUB's investment policy provides the framework for the administration and investment of cash deposits. The investment policy follows Tennessee State law and defines the parameters under which KUB funds should be invested. State law authorizes KUB to invest in obligations of the United States Treasury, its agencies and instrumentalities; certificates of deposit; repurchase agreements; money market funds; and the State Treasurer's Investment Pool.

Interest Rate Risk. KUB's primary investment objectives are to place investments in a manner to ensure the preservation of capital, remain sufficiently liquid to meet all operating requirements, and maximize yield of return. KUB minimizes its exposure to interest rate risk by adhering to Tennessee State law requirements for the investment of public funds. This includes limiting investments to those types described above and limiting maturity horizons. The maximum maturity is four years from the date of investment. KUB also limits its exposure by holding investments to maturity unless cash flow requirements dictate otherwise.

Credit Risk. KUB's investment policy, as required by state law, is to apply the prudent-person rule: Investments are made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable income to be derived, as well as the probable safety of their capital. KUB's Agency Bond investments are rated Aaa by Moody's Investors Service.

Custodial Credit Risk. KUB's investment policy limits exposure to custodial credit risk by restricting investments to a standard set forth by State law. All deposits in excess of federal depository insurance limits are collateralized with government securities held in KUB's name by a third-party custodian bank(s) acting as KUB's agent(s), or through the State of Tennessee's collateral pool. Financial institutions that participate in the collateral pool are subject to special assessment; therefore, the deposits are considered insured. A portion of KUB's investments are generally held in the State of Tennessee Local Government Investment Pool (LGIP). The LGIP is a part of the State Pooled Investment Fund and is sponsored by the State of Tennessee Treasury Department. Tennessee Code Annotated ¶9-4-701 *et seq.* authorizes local governments to invest in the LGIP. None of KUB's investments are exposed to custodial credit risk.

Classification of deposits and investments per Statement of Net Position:

	2016	**2015**
Current assets		
Cash and cash equivalents	$ 78,946,397	$ 124,892,534
Short-term contingency fund investments	25,699,396	6,296,090
Other assets		
Long-term contingency fund investments	68,914,368	83,847,641
Restricted assets		
Unused bond proceeds	-	46,053,447
Bond fund	28,935,445	26,154,107
Other funds	21,418	43,897
	$ 202,517,024	$ 287,287,716

The above amounts do not include accrued interest of $269,667 in fiscal year 2016 and $189,556 in fiscal year 2015. Interest income is recorded on an accrual basis.

Investments and maturities of KUB's deposits and investments as held by financial institutions as of June 30, 2016:

	Deposit and Investment Maturities (in Years)		
	Fair Value	**Less Than 1**	**1-5**
Supersweep NOW and Other Deposits	$ 100,126,611	$ 100,126,611	$ -
State Treasurer's Investment Pool	15,439,274	15,439,274	-
Agency Bonds	107,268,539	25,699,396	81,569,143
Certificates of Deposits	13,393,246	10,968,246	2,425,000
	$ 236,227,670	$ 152,233,527	$ 83,994,143

KUB categorizes its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*. The hierarchy is based on the valuation inputs used to measure the fair value of an asset with a maturity at purchase greater than one year. 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.

KUB has the following recurring fair value measurements as of June 30, 2016:

- U.S. Agency bonds of $81,569,143, which have a maturity at purchase of greater than one year, are valued using quoted market prices (Level 1 inputs)

- Certificates of deposits of $2,425,000, which have a maturity at purchase of greater than one year, are valued at interest rates and yield curves observable at commonly quoted intervals (Level 2 inputs)

KUB measures investments with a maturity at purchase of one year or less at amortized cost, which is considered a fair value equivalent due to their nature. Investments in the State Treasurer's Investment Pool are measured at net asset value (NAV) per share.

4. Accounts Receivable

Accounts receivable consists of the following:

	2016	2015
Wholesale and retail customers		
Billed services	$ 42,412,998	$ 47,996,899
Unbilled services	26,904,562	25,602,160
Other	4,433,444	4,966,423
Allowance for uncollectible accounts	(805,684)	(720,939)
	$ 72,945,320	$ 77,844,543

5. Accounts Payable and Accruals

Accounts payable and accruals consist of the following:

	2016	2015
Trade accounts	$ 50,663,005	$ 50,651,280
Salaries and wages	2,129,489	1,509,808
Advances on pole rental	2,135,320	1,147,346
Self-insurance liabilities	1,758,352	1,699,525
Other current liabilities	15,586,889	15,372,476
	$ 72,273,055	$ 70,380,435

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6. Long-Term Obligations

Electric	**Balance June 30, 2015**	**Additions**	**Payments**	**Defeased**	**Balance June 30, 2016**	**Amounts Due Within One Year**
W-2005 - 3.0 - 4.5%	$ 31,350,000	$ -	$ 1,870,000	$ -	$ 29,480,000	$ 1,940,000
X-2006 - 4.0 - 5.0%	1,825,000	-	1,825,000	-	-	-
Y-2009 - 2.5 - 5.0%	6,875,000	-	1,600,000	-	5,275,000	1,675,000
Z-2010 - 1.45 - 6.35%	25,205,000	-	1,285,000	-	23,920,000	1,305,000
AA-2012 - 3.0 - 5.0%	34,840,000	-	990,000	-	33,850,000	2,540,000
BB-2012 - 3.0 - 4.0%	33,875,000	-	650,000	-	33,225,000	675,000
CC-2013 - 3.0 - 4.0%	9,535,000	-	50,000	-	9,485,000	450,000
DD-2014 - 2.0 - 4.0%	40,000,000	-	675,000	-	39,325,000	700,000
EE-2015 - 2.0 - 5.0%	28,550,000	-	125,000	-	28,425,000	150,000
FF-2015 - 2.0 - 5.0%	35,000,000	-	-	-	35,000,000	675,000
Total bonds	$ 247,055,000	$ -	$ 9,070,000	$ -	$ 237,985,000	$ 10,110,000
Unamortized premium	10,345,326	-	617,044	-	9,728,282	-
Total long term debt	$ 257,400,326	$ -	$ 9,687,044	$ -	$ 247,713,282	$ 10,110,000
Gas						
L-2005 - 3.0 - 4.75%	$ 10,715,000	$ -	$ 695,000	$ -	$ 10,020,000	$ 725,000
N-2007 - 4.0 - 5.0%	550,000	-	-	-	550,000	550,000
O-2010 - 2.0 - 3.0%	3,475,000	-	3,475,000	-	-	-
P-2010 - 3.3 - 6.2%	12,000,000	-	-	-	12,000,000	540,000
Q-2012 - 2.0 - 4.0%	23,345,000	-	700,000	-	22,645,000	2,065,000
R-2012 - 2.0 - 4.0%	9,600,000	-	200,000	-	9,400,000	400,000
S-2013 - 2.0 - 4.0%	11,480,000	-	50,000	-	11,430,000	570,000
T-2013 - 2.0 - 4.6%	24,600,000	-	200,000	-	24,400,000	500,000
U-2015 - 2.0 - 3.5%	11,780,000	-	100,000	-	11,680,000	100,000
Total bonds	$ 107,545,000	$ -	$ 5,420,000	$ -	$ 102,125,000	$ 5,450,000
Unamortized premium	3,794,404	-	305,551	-	3,488,853	-
Total long term debt	$ 111,339,404	$ -	$ 5,725,551	$ -	$ 105,613,853	$ 5,450,000
Water						
S-2005 - 3.5 - 5.0%	$ 6,735,000	$ -	$ 440,000	$ -	$ 6,295,000	$ 465,000
T-2007 - 4.0 - 5.5%	1,450,000	-	700,000	-	750,000	750,000
U-2009 - 3.0 - 4.5%	23,450,000	-	825,000	-	22,625,000	875,000
W-2011 - 2.0 - 4.0%	23,350,000	-	550,000	-	22,800,000	550,000
X-2012 - 3.0 - 5.0%	9,150,000	-	485,000	-	8,665,000	515,000
Y-2013 - 3.0 - 4.0%	9,235,000	-	265,000	-	8,970,000	280,000
Z-2013 - 2.0 - 5.0%	24,150,000	-	475,000	-	23,675,000	500,000
AA-2014 - 2.0 - 4.0%	7,875,000	-	150,000	-	7,725,000	150,000
BB-2015 - 2.0 - 5.0%	23,005,000	-	170,000	-	22,835,000	100,000
CC-2015 - 2.0 - 4.0%	20,000,000	-	350,000	-	19,650,000	375,000
Total bonds	$ 148,400,000	$ -	$ 4,410,000	$ -	$ 143,990,000	$ 4,560,000
Unamortized premium	2,866,890	-	164,708	-	2,702,182	-
Total long term debt	$ 151,266,890	$ -	$ 4,574,708	$ -	$ 146,692,182	$ 4,560,000
Wastewater						
2005 B - 3.0 - 5.0%	$ 16,045,000	$ -	$ 1,410,000	$ -	$ 14,635,000	$ 1,470,000
2008 - 4.0 - 6.0%	11,000,000	-	4,450,000	-	6,550,000	4,600,000
2010 - 6.3 - 6.5%	30,000,000	-	-	-	30,000,000	-
2010C - 1.18 - 6.1%	65,750,000	-	1,250,000	-	64,500,000	1,400,000
2012A - 2.0 - 4.0%	15,415,000	-	820,000	-	14,595,000	840,000
2012B - 1.25 - 5.0%	63,275,000	-	925,000	-	62,350,000	975,000
2013A - 2.0 - 4.0%	112,325,000	-	610,000	-	111,715,000	620,000
2014A - 2.0 - 4.0%	29,625,000	-	425,000	-	29,200,000	450,000
2015A - 3.0 - 5.0%	129,825,000	-	465,000	-	129,360,000	125,000
2015B - 3.0 - 5.0%	30,000,000	-	575,000	-	29,425,000	450,000
Total bonds	$ 503,260,000	$ -	$ 10,930,000	$ -	$ 492,330,000	$ 10,930,000
Unamortized premium	11,625,190	-	558,966	-	11,066,224	-
Total long term debt	$ 514,885,190	$ -	$ 11,488,966	$ -	$ 503,396,224	$ 10,930,000
Consolidated						
Total Bonds	$ 1,006,260,000	$ -	$ 29,830,000	$ -	$ 976,430,000	$ 31,050,000
Total unamortized premium	28,631,810	-	1,646,269	-	26,985,541	-
Total long term debt	$ 1,034,891,810	$ -	$ 31,476,269	$ -	$ 1,003,415,541	$ 31,050,000

Electric	Balance June 30, 2014	Additions	Payments	Defeased	Balance June 30, 2015	Amounts Due Within One Year
W-2005 - 3.0 - 4.5%	$ 33,140,000	$ -	$ 1,790,000	$ -	$ 31,350,000	$ 1,870,000
X-2006 - 4.0 - 5.0%	3,550,000	-	1,725,000	-	1,825,000	1,825,000
Y-2009 - 2.5 - 5.0%	35,900,000	-	1,525,000	27,500,000	6,875,000	1,600,000
Z-2010 - 1.45 - 6.35%	26,470,000	-	1,265,000	-	25,205,000	1,285,000
AA-2012 - 3.0 - 5.0%	35,795,000	-	955,000	-	34,840,000	990,000
BB-2012 - 3.0 - 4.0%	34,500,000	-	625,000	-	33,875,000	650,000
CC-2013 - 3.0 - 4.0%	9,585,000	-	50,000	-	9,535,000	50,000
DD-2014 - 2.0 - 4.0%	-	40,000,000	-	-	40,000,000	675,000
EE-2015 - 2.0 - 5.0%	-	28,550,000	-	-	28,550,000	125,000
FF-2015 - 2.0 - 5.0%	-	35,000,000	-	-	35,000,000	-
Total bonds	$ 178,940,000	$ 103,550,000	$ 7,935,000	$ 27,500,000	$ 247,055,000	$ 9,070,000
Unamortized premium	5,779,555	5,617,592	411,968	639,853	10,345,326	-
Total long term debt	$ 184,719,555	$ 109,167,592	$ 8,346,968	$ 28,139,853	$ 257,400,326	$ 9,070,000
Gas						
L-2005 - 3.0 - 4.75%	$ 11,380,000	$ -	$ 665,000	$ -	$ 10,715,000	$ 695,000
N-2007 - 4.0 - 5.0%	12,000,000	-	-	11,450,000	550,000	-
O-2010 - 2.0 - 3.0%	6,825,000	-	3,350,000	-	3,475,000	3,475,000
P-2010 - 3.3 - 6.2%	12,000,000	-	-	-	12,000,000	-
Q-2012 - 2.0 - 4.0%	24,030,000	-	685,000	-	23,345,000	700,000
R-2012 - 2.0 - 4.0%	9,800,000	-	200,000	-	9,600,000	200,000
S-2013 - 2.0 - 4.0%	11,530,000	-	50,000	-	11,480,000	50,000
T-2013 - 2.0 - 4.6%	24,800,000	-	200,000	-	24,600,000	200,000
U-2015 - 2.0 - 3.5%	-	11,780,000	-	-	11,780,000	100,000
Total bonds	$ 112,365,000	$ 11,780,000	$ 5,150,000	$ 11,450,000	$ 107,545,000	$ 5,420,000
Unamortized premium	3,434,514	701,501	296,934	44,677	3,794,404	-
Total long term debt	$ 115,799,514	$ 12,481,501	$ 5,446,934	$ 11,494,677	$ 111,339,404	$ 5,420,000
Water						
R-2005 - 3.5 - 5.0%	$ 255,000	$ -	$ 255,000	$ -	$ -	$ -
S-2005 - 3.5 - 5.0%	7,160,000	-	425,000	-	6,735,000	440,000
T-2007 - 4.0 - 5.5%	24,350,000	-	675,000	22,225,000	1,450,000	700,000
U-2009 - 3.0 - 4.5%	24,250,000	-	800,000	-	23,450,000	825,000
W-2011 - 2.0 - 4.0%	23,900,000	-	550,000	-	23,350,000	550,000
X-2012 - 3.0 - 5.0%	9,610,000	-	460,000	-	9,150,000	485,000
Y-2013 - 3.0 - 4.0%	9,260,000	-	25,000	-	9,235,000	265,000
Z-2013 - 2.0 - 5.0%	24,600,000	-	450,000	-	24,150,000	475,000
AA-2014 - 2.0 - 4.0%	-	8,000,000	125,000	-	7,875,000	150,000
BB-2015 - 2.0 - 5.0%	-	23,005,000	-	-	23,005,000	170,000
CC-2015 - 2.0 - 4.0%	-	20,000,000	-	-	20,000,000	350,000
Total bonds	$ 123,385,000	$ 51,005,000	$ 3,765,000	$ 22,225,000	$ 148,400,000	$ 4,410,000
Unamortized premium	1,518,734	1,493,612	102,471	42,985	2,866,890	-
Total long term debt	$ 124,903,734	$ 52,498,612	$ 3,867,471	$ 22,267,985	$ 151,266,890	$ 4,410,000
Wastewater						
2005 A - 4.0 - 5.0%	$ 36,550,000	$ -	$ -	$ 36,550,000	$ -	$ -
2005 B - 3.0 - 5.0%	17,395,000	-	1,350,000	-	16,045,000	1,410,000
2007 - 4.0 - 5.0%	75,000,000	-	-	75,000,000	-	-
2008 - 4.0 - 6.0%	30,975,000	-	4,300,000	15,675,000	11,000,000	4,450,000
2010 - 6.3 - 6.5%	30,000,000	-	-	-	30,000,000	-
2010C - 1.18 - 6.1%	66,850,000	-	1,100,000	-	65,750,000	1,250,000
2012A - 2.0 - 4.0%	16,215,000	-	800,000	-	15,415,000	820,000
2012B - 1.25 - 5.0%	64,150,000	-	875,000	-	63,275,000	925,000
2013A - 2.0 - 4.0%	112,915,000	-	590,000	-	112,325,000	610,000
2014A - 2.0 - 4.0%	-	30,000,000	375,000	-	29,625,000	425,000
2015A - 3.0 - 5.0%	-	129,825,000	-	-	129,825,000	465,000
2015B - 3.0 - 5.0%	-	30,000,000	-	-	30,000,000	575,000
Total bonds	$ 450,050,000	$ 189,825,000	$ 9,390,000	$ 127,225,000	$ 503,260,000	$ 10,930,000
Unamortized premium	4,154,409	8,539,211	312,636	755,794	11,625,190	-
Total long term debt	$ 454,204,409	$ 198,364,211	$ 9,702,636	$ 127,980,794	$ 514,885,190	$ 10,930,000
Consolidated						
Total Bonds	$ 864,740,000	$ 356,160,000	$ 26,240,000	$ 188,400,000	$ 1,006,260,000	$ 29,830,000
Total unamortized premium	14,887,211	16,351,916	1,124,009	1,483,309	28,631,810	-
Total long term debt	$ 879,627,211	$ 372,511,916	$ 27,364,009	$ 189,883,309	$ 1,034,891,810	$ 29,830,000

Debt service over remaining term of the debt is as follows:

Fiscal Year	Principal	Interest	Total
2017	31,050,000	38,413,632	69,463,632
2018	32,195,000	37,216,662	69,411,662
2019	33,415,000	35,933,587	69,348,587
2020	34,810,000	34,573,291	69,383,291
2021	36,200,000	33,141,894	69,341,894
2022-2026	197,410,000	141,956,861	339,366,861
2027-2031	192,140,000	104,499,778	296,639,778
2032-2036	149,440,000	72,309,054	221,749,054
2037-2041	150,245,000	43,627,770	193,872,770
2042-2046	105,150,000	14,594,919	119,744,919
2047-2050	14,375,000	1,076,675	15,451,675
Total	$ 976,430,000	$ 557,344,123	$ 1,533,774,123

The Divisions have pledged sufficient revenue, after deduction of all current operating expenses (exclusive of tax equivalents), to meet bond principal and interest payments of revenue bonds when due. Such bond requirements are being met through monthly deposits to the bond funds as required by the bond covenants. As of June 30, 2016 these requirements had been satisfied.

During fiscal year 2006, KUB's Electric Division issued Series W 2005 bonds in part to retire certain existing debt and fund electric system capital improvements. Concurrent with the issuance of these bonds, KUB transferred funds to an irrevocable trust to pay a portion of the Series U 2001 bonds, as such amounts mature. During fiscal year 2009, KUB's Electric Division issued Series Y 2009 bonds to fund electric system capital improvements. During fiscal year 2011, KUB's Electric Division issued series Z 2010 bonds to fund electric system capital improvements. The bonds were issued as federally taxable Build America Bonds with a 35 percent interest payment rebate to be received from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8 percent reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change. During fiscal year 2012, KUB's Electric Division issued Series AA 2012 bonds to retire a portion of outstanding Series V 2004 bonds. During fiscal year 2013, KUB's Electric Division issued Series BB 2012 bonds to fund electric system capital improvements. KUB's Electric Division also issued Series CC 2013 bonds to retire a portion of outstanding Series X 2006 bonds. During fiscal year 2015, KUB's Electric Division issued Series EE 2015 bonds to retire a portion of outstanding Series Y 2009 bonds. KUB's Electric Division also issued Series DD 2014 and Series FF 2015 to fund electric system capital improvements. In prior years, certain revenue bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the liability for the defeased bonds, $27.5 million at June 30, 2016, and the trust account assets are not included in the financial statements.

During fiscal year 2006, KUB's Gas Division issued Series L 2005 bonds in part to retire certain existing debt and fund gas system capital improvements. Concurrent with the issuance of these bonds, KUB transferred funds to an irrevocable trust to pay a portion of the Series J 2001 bonds, as such amounts mature. During fiscal year 2008, KUB's Gas Division issued Series N 2007 to fund gas system capital improvements. During fiscal year 2011, KUB's Gas Division issued Series P 2010 bonds to fund gas system capital improvements. The bonds were issued as federally taxable Build America Bonds with a 35 percent interest payment rebate to be received from the United States Government for each interest payment. Effective October 1, 2015, these bonds became subject to a 6.8 percent reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change. During fiscal year 2012, KUB's Gas Division issued Series Q 2012 bonds to retire Series K 2004 bonds. During fiscal year 2013, KUB's Gas Division issued Series R 2012 bonds to fund gas system capital improvements. KUB's Gas Division also issued Series S 2013 bonds to retire Series M 2006 outstanding bonds. During fiscal year 2014, KUB's Gas Division issued Series T 2013 to fund gas system capital improvements. During fiscal year 2015, KUB's Gas Division issued Series U 2015 bonds to retire Series N 2007 outstanding bonds. In prior years, certain revenue bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the liability for the defeased bonds, $11.5 million at June 30, 2016, and the trust account assets are not included in the financial statements.

During fiscal year 2006, KUB's Water Division issued Series S 2005 bonds to retire certain existing debt and fund water system capital improvements. Concurrent with the issuance of these bonds, KUB transferred funds to an irrevocable trust to pay a portion of the Series P 2001 bonds, as such amounts mature. During fiscal year 2008, KUB's Water Division issued Series T 2007 bonds to fund water system capital improvements. During fiscal year 2010, KUB's Water Division issued Series U 2009 bonds to fund water system capital improvements. During fiscal year 2012, KUB's Water Division issued Series W 2011 bonds to fund water system capital improvements. KUB's Water Division also issued Series X 2012 bonds to retire Series Q 2004 bonds. During fiscal year 2013, KUB's Water Division issued Series Y 2013 bonds to retire a portion of outstanding Series R 2005 bonds. During fiscal year 2014, KUB's Water Division issued Series Z 2013 bonds to fund water system capital improvements. During fiscal year 2015, KUB's Water Division issued Series BB 2015 bonds to retire a portion of outstanding Series T 2007 bonds. KUB's Water Division also issued Series AA 2014 and Series CC 2015 bonds to fund water system capital improvements. In prior years, certain revenue bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the liability for the defeased bonds, $22.2 million at June 30, 2016, and the trust account assets are not included in the financial statements.

During fiscal year 2006, KUB's Wastewater Division issued Series 2005B bonds in part to retire certain existing debt and fund wastewater system capital improvements. Concurrent with the issuance of these bonds, KUB transferred funds to an irrevocable trust to pay a portion of the Series 1998 bonds and Series 2001A bonds, as such amounts mature. During fiscal year 2009, KUB's Wastewater Division issued Series 2008 bonds to fund wastewater system capital improvements. During fiscal year 2010, KUB's Wastewater Division issued Series 2010 bonds to fund capital improvements. These bonds were issued as federally taxable Build America Bonds with a 35 percent interest payment rebate to be received from the United States Government for each interest payment. Effective October 1, 2015, these bonds became subject to a 6.8 percent reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change. During fiscal year 2011, KUB's Wastewater Division issued Series 2010C bonds to fund capital improvements. These bonds were issued as federally taxable Build America Bonds with a 35 percent interest payment rebate to be received from the United States Government for each interest payment. Effective October 1, 2015, these bonds became subject to a 6.8 percent reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change. During fiscal year 2012, KUB's Wastewater Division issued Series 2012A bonds to retire Series 2004A bonds. During fiscal year 2013, KUB's Wastewater Division issued Series 2012B bonds to fund wastewater system capital improvements. KUB's Wastewater Division also issued Series 2013A bonds to retire a portion of outstanding Series 2005A bonds. During fiscal year 2015, KUB's Wastewater Division issued Series 2015A bonds to retire a portion of outstanding Series 2005A, Series 2007, and Series 2008 bonds. KUB's Wastewater Division also issued Series 2014A and Series 2015B bonds to fund wastewater system capital improvements. In prior years, certain revenue bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the liability for the defeased bonds, $90.7 million at June 30, 2016, and the trust account assets are not included in the financial statements.

Other liabilities consist of the following:

	Balance June 30, 2015	Increase	Decrease	Balance June 30, 2016
TVA conservation program	$ 10,336,682	$ 1,174,926	$ (3,098,755)	$ 8,412,853
Accrued compensated absences	8,616,844	16,943,202	(16,498,820)	9,061,226
Customer advances for construction	2,305,058	1,499,982	(1,557,441)	2,247,599
Other	478,797	411,126	(586,250)	303,673
	$ 21,737,381	$ 20,029,236	$ (21,741,266)	$ 20,025,351

7. Lease Commitments

KUB has non-cancelable operating lease commitments for office equipment, property, and vehicles, summarized for the following fiscal years:

2017	$ 256,776
2018	241,790
2019	141,959
2020	8,189
Total operating minimum lease payments	$ 648,714

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8. Capital Assets

Capital asset activity was as follows:

	Balance June 30, 2015	Increase	Decrease	Balance June 30, 2016
Production Plant (Intakes)	$ 742,503	$ -	$ -	$ 742,503
Pumping and Treatment Plant	272,156,011	27,948,957	(2,131,084)	297,973,884
Distribution and Collection Plant				
Mains and metering	856,463,692	90,187,145	(11,856,977)	934,793,860
Services and meters	155,306,743	10,562,942	(4,890,909)	160,978,776
Electric station equipment	125,338,097	27,775,476	(880,406)	152,233,167
Poles, towers and fixtures	134,306,063	14,897,225	(1,142,671)	148,060,617
Overhead conductors	128,493,727	9,622,260	(1,341,285)	136,774,702
Line transformers	92,547,983	5,192,889	(897,720)	96,843,152
Other accounts	290,373,861	11,327,465	(1,291,052)	300,410,274
Total Distribution & Collection Plant	$ 1,782,830,166	$ 169,565,402	$ (22,301,020)	$ 1,930,094,548
General Plant	154,807,001	16,109,904	(2,304,757)	168,612,148
Total Plant Assets	$ 2,210,535,681	$ 213,624,263	$ (26,736,861)	$ 2,397,423,083
Less Accumulated Depreciation	(753,200,620)	(70,652,307)	26,328,506	(797,524,421)
Net Plant Assets	$ 1,457,335,061	$ 142,971,956	$ (408,355)	$ 1,599,898,662
Work In Progress	193,812,149	164,049,004	(214,654,664)	143,206,489
Total Net Plant	$ 1,651,147,210	$ 307,020,960	$ (215,063,019)	$ 1,743,105,151

	Balance June 30, 2014	Increase	Decrease	Balance June 30, 2015
Production Plant (Intakes)	$ 742,503	$ -	$ -	$ 742,503
Pumping and Treatment Plant	268,416,043	4,348,531	(608,563)	272,156,011
Distribution and Collection Plant				
Mains and metering	827,485,705	32,368,532	(3,390,545)	856,463,692
Services and meters	150,206,800	7,460,515	(2,360,572)	155,306,743
Electric station equipment	120,964,151	6,556,645	(2,182,699)	125,338,097
Poles, towers and fixtures	124,328,627	12,739,496	(2,762,060)	134,306,063
Overhead conductors	120,168,100	9,163,450	(837,823)	128,493,727
Line transformers	90,103,801	3,298,379	(854,197)	92,547,983
Other	282,320,215	8,891,602	(837,956)	290,373,861
Total Distribution & Collection Plant	$ 1,715,577,399	$ 80,478,619	$ (13,225,852)	$ 1,782,830,166
General Plant	146,172,851	10,527,779	(1,893,629)	154,807,001
Total Plant Assets	$ 2,130,908,796	$ 95,354,929	$ (15,728,044)	$ 2,210,535,681
Less Accumulated Depreciation	(706,864,663)	(63,051,875)	16,715,918	(753,200,620)
Net Plant Assets	$ 1,424,044,133	$ 32,303,054	$ 987,874	$ 1,457,335,061
Work In Progress	124,829,743	164,644,375	(95,661,969)	193,812,149
Total Net Plant	$ 1,548,873,876	$ 196,947,429	$ (94,674,095)	$ 1,651,147,210

9. Risk Management

KUB is exposed to various risks of loss related to active and retiree medical claims; injuries to workers; theft of, damage to, and destruction of assets; environmental damages; and natural disasters. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported.

These liabilities are included in accrued expenses in the Statement of Net Position. The liability is KUB's best estimate based on available information. At June 30, 2016 and 2015, the amount of these liabilities was $1,758,352 and $1,699,525, respectively, resulting from the following changes:

	2016	2015
Balance, beginning of year	$ 1,699,525	$ 1,572,570
Current year claims and changes in estimates	14,043,332	14,222,337
Claims payments	(13,984,505)	(14,095,382)
Balance, end of year	$ 1,758,352	$ 1,699,525

10. Pension Plan

Description of Plan

The Knoxville Utilities Board Pension Plan (the Plan) is a governmental plan as defined by the Employee Retirement Income Security Act of 1974 ("ERISA" or the "Act"), is not subject to any of the provisions of the Act, and was revised January 1, 2014 to include all prior approved amendments. The Plan is a single-employer contributory, defined benefit pension plan established by Knoxville Utilities Board ("KUB") Resolution No. 980 dated February 18, 1999, effective July 1, 1999, as authorized by the Charter of the City of Knoxville §1107(J). The Plan is designed to provide retirement, disability and death benefits to KUB employees. KUB administers the Plan through an Administrative Committee consisting of seven KUB employees that are appointed by KUB's President and CEO. Any amendments to the Plan involving costs not approved in the operating budget must be adopted by KUB's Board of Commissioners, upon recommendation by KUB's President and CEO. All other amendments to the Plan may be approved by KUB's President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The Plan issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017.

Effective January 1, 2011, KUB closed the Plan such that persons employed or re-employed by KUB on or after January 1, 2011, are not eligible to participate, but that eligible employees hired prior to January 1, 2011, who have not separated from service, shall continue as Participants and to accrue benefits under the Plan.

Participants in the Plan consisted of the following as of December 31:

	2015	2014
Inactive plan members:		
Terminated vested participants	39	40
Retirees and beneficiaries	628	627
Active plan members	692	725
Total	1,359	1,392

Retirement Benefits

The Plan provides three benefit arrangements for KUB participants, retirees, and beneficiaries.

The Plan provides pension benefits through the Career Equity Program ("CEP") for eligible employees hired on or after January 1, 1999, and for eligible former "City System Plan A" participants who elected CEP coverage as of July 1, 1999. The guaranteed pension benefit payable to a participant who has completed five or more years of service (or reached the normal retirement date, if earlier) upon termination of KUB employment shall be a lump sum equal to the participant's average compensation times their benefit percentage, as defined in the Plan document, or an annuity may be chosen by the participant.

In addition, the Plan provided retirement benefits through "Plan A" for former City System Plan A participants who elected not to participate in the CEP. Plan A is a closed plan and is not available to KUB employees hired after July 1, 1999. Plan A provides for early retirement benefits with 25 years of service and normal retirement benefits at age 62 or later. Benefits provided to Plan A participants include several different forms of monthly annuity payments.

The Plan also provides retirement benefits through "Plan B" for former "City System Plan B" participants. Plan B is a closed plan providing benefits to participants not covered by Social Security. Benefits provided to Plan B participants include several different forms of monthly annuity payments available to participants.

Effective January 1, 2012, KUB began to provide for additional monthly supplements, which will not be subject to cost of living adjustments, to certain former employees and surviving dependents of former employees who are eligible for and have elected coverage under the KUB retiree medical plan and are eligible for Medicare. This was done to address the loss of drug coverage under the KUB retiree medical plan and to assist such individuals in obtaining prescription drug coverage under Medicare Part D.

Contributions

Participation in Plan A requires employee contributions of 3% of the first $4,800 of annual earnings and 5% of annual earnings in excess of $4,800. Plan B participants may not make contributions to the Plan. KUB contributions are determined by the enrolled actuary of the Plan and equal the amount necessary to provide the benefits under the Plan determined by the application of accepted actuarial methods and assumptions. The method of funding shall be consistent with Plan objectives.

Plan Funding

KUB maintains a Funding Policy for the Plan in accordance with Tennessee State Law. The primary goal of the Policy is to document the method KUB has adopted to provide assurance that future KUB and employee contributions and current Plan assets will be sufficient to fund all benefits expected to be paid to current active, inactive and retired Plan participants and their beneficiaries. Per the Funding Policy, KUB fully funds its annual Actuarially Determined Contribution.

Investments

The Plan's investments are held by State Street Bank and Trust Company (the "Trustee"). The Plan's policy in regard to the allocation of invested assets is established by the Investment Committee and approved by the KUB Board of Commissioners and may only be amended by the KUB Board of Commissioners. It is the policy of the Investment Committee to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes. The following was the Plan's adopted asset allocation policy as of December 31, 2015:

Asset Class	Target Allocation
Domestic equity – large cap	20% - 50%
Domestic equity – mid cap	0% - 15%
Domestic equity – small cap	0% - 15%
Domestic equity - convertible securities	0% - 10%
Non-U.S. equity	0% - 20%
Real estate equity	0% - 10%
Fixed income – aggregate bonds	5% - 25%
Fixed income – long-term bonds	10% - 25%
Cash and deposits	0% - 5%

Contributions of $5,669,380 and $6,314,399 for 2014 and 2013, respectively, were made during KUB's fiscal years ending June 30, 2016 and 2015, respectively. The contribution was determined as part of the January 1, 2014 valuation using the Individual Entry Age Normal funding method. The objective under this method is to fund each participant's benefits under the Plan as payments which are level as a percentage of salary, starting on the original participation date (employment date) and continuing until the assumed retirement, termination, disability or death. The actuarial valuation for the Plan year ending December 31, 2015 resulted in an actuarially determined contribution of $4,816,913 for the fiscal year ending June 30, 2017, based on the Plan's current funding policy.

Subsequent to June 30, 2016, the actuarial valuation for the Plan year ending December 31, 2016 was completed. The actuarial valuation resulted in an actuarially determined contribution of $3,756,283 for the fiscal year ending June 30, 2018, based on the Plan's current funding policy. For the Plan year ending December 31, 2016, the Plan's actuarial funded ratio was 103.04 percent.

The actuarial valuations for the Plan years ending December 31, 2015 and 2016, which determine the actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Implementation of GASB 68

In fiscal year 2015, KUB adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*("GASB 68"), which requires measurement of the net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 will be based on the December 31, 2015 and 2014 measurement date, respectively.

GASB 68 requires certain disclosures related to the net pension liability of the Plan as disclosed below:

		2015		2014
Total pension liability	$	204,502,350	$	202,773,764
Plan fiduciary net position		199,462,190		(208,795,394)
Plan's net pension liability (asset)	$	5,040,160	$	(6,021,630)
Plan fiduciary net position as a percentage of the total pension liability		97.54%		102.97%

Changes in Net Pension Liability are as follows:

	Total Pension Liability (a)	Increase (Decrease) Plan Fiduciary Net Position (b)	Net Pension Liability (a) - (b)
Balances at December 31, 2014	$ 202,773,764	$ 208,795,394	$ (6,021,630)
Changes for the year:			
Service cost	4,157,062	-	4,157,062
Interest	14,812,784	-	14,812,784
Differences between Expected and Actual Experience	(1,890,334)	-	(1,890,334)
Changes of Assumptions	-	-	-
Contributions - employer	-	5,991,887	(5,991,887)
Contributions - rollovers	-	482,060	(482,060)
Contributions - member	-	5,486	(5,486)
Net investment income	-	(64,551)	64,551
Benefit payments	(15,350,926)	(15,350,926)	-
Administrative expense	-	(397,160)	397,160
Net changes	1,728,586	(9,333,204)	11,061,790
Balances at December 31, 2015	$ 204,502,350	$ 199,462,190	$ 5,040,160

Actuarial Assumptions

The total pension liability was determined by an actuarial valuation as of December 31, 2015 and 2014, using the following actuarial assumptions, applied to all periods included in the measurement:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.80% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the January 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation
Inflation	2.8 percent

The actuarial assumptions used in the December 31, 2015 valuation were based on the results of an actuarial experience study for the period January 1, 2009 through December 31, 2013.

The long-term expected rate of return on Plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of Plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the Plan’s target asset allocation as of December 31, 2015 and 2014 are summarized in the following table. The real rate of return reported for fixed income is for aggregate fixed income. The Plan has both aggregate and long duration fixed income.

	Long Term Expected Real Rate of Return	
Asset Class	**2015**	**2014**
Domestic equity	7.2%	6.0%
Non-U.S. equity	7.4%	7.0%
Real estate equity	6.5%	5.7%
Fixed income	3.7%	1.8%
Cash and deposits	2.6%	0.5%

Discount rate

The discount rate used to measure the total pension liability was 7.5 percent as of January 1, 2015 and 2014. The projection of cash flows used to determine the discount rate assumed that participant contributions will be made at the current contribution rate and that KUB contributions will be made at rates equal to the actuarially determined contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the net pension liability to changes in the discount rate

The following presents the net pension liability of the Plan as of December 31, 2015, calculated using the discount rate of 7.5 percent, as well as what the Plan’s net pension liability would be if it were calculated using a discount rate that is one percent lower (6.5 percent) or one percent higher (8.5 percent) than the current rate:

	1% Decrease (6.5%)	**Current Discount Rate (7.5%)**	**1% Increase (8.5%)**
Plan's net pension liability	$ 17,128,897	$ 5,040,160	$ (5,963,331)

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

For the year ended June 30, 2015, KUB recognized pension expense of $2,749,905.

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in expense over the average expected remaining service life of all active and inactive members. As of the measurement date, this recognition period was 3.72 years. However, there were no experience gains or losses, and there were no assumption changes during the measurement year.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment gain of $7,972,887. $1,594,577 of that gain was recognized in the current year and an identical amount will be recognized in each of the next four years, resulting in a deferred inflow of resources of $6,378,310.

The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over the next five years. In addition, KUB recorded a deferred outflow of resources of $3,157,199 at June 30, 2015 for employer contributions made between December 31, 2014 and June 30, 2015.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ -
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	-	6,378,310
Contributions subsequent to measurement date	3,157,199	-
Total	$ 3,157,199	$ 6,378,310

For the year ended June 30, 2016, KUB recognized pension expense of $4,665,035.

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in the pension expense over the average expected remaining service life of all active and inactive members, determined as of the beginning of the measurement period. As of December 31, 2014, this average was 5.00 years. During the measurement year, there were no assumption or benefit changes. There was an experience gain of $1,890,334 with $378,067 of that recognized in the current year and in each of the next four years.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment loss of $15,382,915. $3,076,583 of that loss was recognized in the current year and an identical amount will be recognized in each of the next four years. Unrecognized investment gains from prior periods were $6,378,310 of which $1,594,577 was recognized as a reduction in pension expense in the current year.

Experience gains this year created a deferred inflow of resources of $1,512,267. The combination of unrecognized investment losses this year along with unrecognized net investment gains from prior periods results in a deferred outflow of resources as of December 31, 2015 of $7,522,599. The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over future years. In addition, KUB recorded a deferred outflow of resources of $2,834,692 at June 30, 2016 for employer contributions made between December 31, 2015 and June 30, 2016.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ 1,512,267
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	7,522,599	-
Contributions subsequent to measurement date	2,834,692	-
Total	$ 10,357,291	$ 1,512,267

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

Year ended June 30:	
2017	$ 3,938,630
2018	1,103,939
2019	1,103,938
2020	2,698,517
Thereafter	-

11. Defined Contribution Plan

The KUB Asset Accumulation 401(k) Plan (the “401(k) Plan”) is a defined contribution 401(k) employee retirement savings plan covering eligible KUB employees established by the KUB Board of Commissioners in accordance with the Charter of the City of Knoxville, Tennessee. The 401(k) Plan’s assets are held in trust under an agreement between KUB and Fidelity Management Trust Company. Employees hired prior to January 1, 2011 may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. Employees hired on or after January 1, 2011 have an enhanced 401(k) due to the closure of the Defined Benefit Pension Plan. They may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. They also receive a nonelective KUB contribution of from 3 percent to 6 percent, depending on years of service, whether they contribute or not.

Matching contributions were previously remitted to the KUB Pension Plan (a separate defined benefit plan) in the name of the participant for employees hired prior to January 1, 2011. As of December 9, 2015, these Pension match assets moved from the KUB Pension Plan to the 401(k) Plan. Effective December 9, 2015, all matching contributions are remitted to the 401(k) Plan. The match and nonelective contributions for employees hired on or after January 1, 2011 are paid directly by KUB. KUB funded 401(k) matching contributions and nonelective contributions of $1,739,057 and $1,593,350, respectively, for the years ended June 30, 2016 and 2015.

12. Other Post-Employment Benefits (OPEB)

The Governmental Accounting Standards Board (GASB) established standards for the measurement, recognition, and reporting of other post-employment benefits (OPEB). OPEB includes post-employment benefits other than pension, which, for KUB, is presently limited to post-employment health care. GASB Statement No. 45 (Statement No. 45) requires the recognition of the accrued OPEB liability for the respective year, plus the disclosure of the total unfunded liability.

KUB currently provides post-employment health care benefits to 585 former employees and 593 covered dependents. The cost of coverage is shared with retirees and beneficiaries. KUB recognizes its share of the cost of post-employment health care benefits as an expense as claims are paid.

KUB amended its Group Health Plan in 1999, eliminating post-employment health care benefits for all employees hired on or after July 1, 1999. As of June 30, 2016, 356 active employees were eligible for individual and dependent coverage at separation. To qualify, the employee must meet the Rule of 80 (age plus years of service) with a minimum of 20 years of service, and be enrolled in medical coverage on their last day.

In May 2006, the State of Tennessee adopted Tennessee Code Annotated, Title 8, Chapter 50, Part 12 authorizing governmental entities to establish Trusts for the purpose of pre-funding their respective OPEB liabilities.

Although Statement No. 45 does not require pre-funding of the liability, KUB has determined that it is in the long-term economic interest of KUB and its ratepayers to establish a Trust to pre-fund KUB’s OPEB liability.

Knoxville Utilities Board Other Post-Employment Benefits Trust (the “Trust”) is a single-employer Other Post-Employment Benefits Plan established by the Knoxville Utilities Board (KUB) Board of Commissioners through Resolution No. 1168, as amended, dated October 18, 2007. The applicable documentation was submitted to the State Funding Board and, in December 2007, the State Funding Board approved the Trust. The Trust was also approved by the Internal Revenue Service in June 2008. KUB administers the Trust through a Board of Trustees consisting of seven KUB employees that are appointed by KUB’s President and CEO. Any amendments to the Trust involving costs not approved in the operating budget must be approved by KUB’s Board of Commissioners, upon recommendation by KUB’s President and CEO. All other amendments to the Trust may be approved by KUB’s President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The investment of all deposits to the Trust is governed by an Investment Policy, which was adopted by the KUB Board and approved by the State Funding Board.

KUB makes annual contributions to the Trust at an actuarially determined rate. Based on the date of retirement, certain retired plan members are required to contribute specified amounts monthly to maintain health insurance. Those who retired prior to July 1983 have no required monthly premiums for themselves or dependents. The retirees, or their surviving dependents, who retired between August 1983 and January 1998 are required to pay $250 per month for pre-Medicare family health insurance. For individuals who retired after January 1998, the required monthly premium for pre-Medicare health insurance is $250 for single coverage and $500 for family coverage. There is currently no premium for Medicare eligible retirees or dependents.

An actuarial valuation of KUB’s Postretirement Benefit Plan was performed for the Trust as of January 1, 2014 for fiscal year June 30, 2015 and January 1, 2015 for fiscal year June 30, 2016. The following table presents the OPEB cost for the year, the amount contributed to the Trust, and changes in the net OPEB obligation for fiscal year ending June 30:

		2016	**2015**
a)	Net OPEB Obligation/(Asset) at beginning of fiscal year	$ (174,410)	$ (177,322)
b)	Annual Required Contribution (ARC)	953,221	3,497,372
c)	Interest on Net OPEB Obligation/(Asset)	(13,081)	(14,186)
d)	Adjustment to ARC	(16,427)	(17,098)
e)	Annual OPEB Cost **(b+c-d)**	956,567	3,500,284
f)	Employer Contributions	953,221	3,497,372
g)	Net OPEB Obligation/(Asset) at end of fiscal year **(a+e-f)**	$ (171,064)	$ (174,410)

KUB's annual OPEB cost, the percentage of annual OPEB cost contributed to the Trust, and the net OPEB obligation for fiscal year 2016 and the two preceding years were as follows:

Schedule of Employer Contributions

Actuarial Valuation Date	**Employer Fiscal Year**	**Annual Required Contribution**	**Fiscal Year Actual Contribution**	**Percentage Contributed**	**Net OPEB Obligation**
1/1/2012	6/30/2014	3,327,412	4,057,091	121.93%	(177,322)
1/1/2013	6/30/2015	3,497,372	3,497,372	100.00%	(174,410)
1/1/2014	6/30/2016	953,221	953,221	100.00%	(171,064)

Total contributions to the OPEB Trust for the fiscal year ended June 30, 2016 were $953,221. The contribution to the Trust was consistent with the annual required contribution, as determined by the Postretirement Benefit Plan's actuarial valuation as of January 1, 2014, which was $953,221. As of June 30, 2016, the employer's OPEB obligation has been exceeded by $171,064.

The annual required contribution for the fiscal year ending June 30, 2017, as determined by the Plan's actuarial valuation as of January 1, 2015 is $620,015.

The actuarial valuation for the Plan as of January 1, 2016 has been completed. The valuation determined that the Plan's actuarial accrued liability was $45,118,624. The actuarial value of the Plan's assets was $48,510,796. As a result, the Plan's unfunded actuarial accrued liability was ($3,392,172). The Plan's actuarial funded ratio was 108 percent. Due to the future implementation of GASB 75, the contributions made for fiscal year ending June 30, 2018 will be the actuarially determined contribution instead of the annual required contribution and the actuarial cost method used to determine the contributions will change from the projected unit credit cost method to the entry age normal cost method. The actuarially determined contribution for fiscal year ending June 30, 2018 will be zero. See Required Supplementary Information for OPEB Schedule of Funding Progress.

The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution and actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

The required schedule of funding progress immediately following the notes to the financial statements presents multi-year trend information about whether the actuarial value of Trust assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point.

Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

Identification of actuarial methods and significant assumptions used to determine the annual required contribution for the fiscal year ending June 30, 2016:

I. Actuarial cost method	Projected unit credit cost method
II. Actuarial value of assets	Smoothed market value with phase-in method using a smoothing period of 5 years
III. Investment return	7.5%, based on the expected portfolio return
Projected salary increases	N/A
Healthcare cost Trend:	
Medicare	2014 - 2030+, ranging from 4.5% to 7.45%
Non-Medicare	2014 - 2030+, ranging from 4.5% to 8.75%
IV. Amortization method	Level dollar closed (30-year)
Remaining amortization period	22 years

The Trust issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017.

13. Related Party Transactions

KUB, in the normal course of operations, is involved in transactions with the City of Knoxville. Such transactions for the years ended June 30, 2016 and 2015 are summarized as follows:

	2016	**2015**
City of Knoxville		
Amounts billed by KUB for utilities and related services	$ 14,383,228	$ 14,250,324
Payments by KUB in lieu of property tax	17,428,232	16,535,897
Payments by KUB for services provided	2,183,335	1,804,675

With respect to these transactions, accounts receivable from the City of Knoxville included in the balance sheet at year end were:

	2016	**2015**
Accounts receivable	$ 902,254	$ 869,815

14. Natural Gas Supply Contract Commitments

For fiscal year 2016, the Gas Division hedged 67 percent of its total gas purchases via gas supply contracts. As of June 30, 2016, the Gas Division had hedged the price on approximately 20 percent of its anticipated gas purchases for fiscal year 2017.

KUB contracts separately for the purchase, transportation and storage of natural gas. Purchase commitments for the next five years are as follows:

Firm obligations related to purchased gas – demand

	2017	**2018**	**2019**	**2020**	**2021**
Transportation					
Tennessee Gas Pipeline	$ 3,269,844	$ 3,269,844	$ 3,269,844	$ 1,089,948	$ -
East Tennessee Natural Gas	10,066,388	10,066,388	10,066,388	2,748,496	-
Storage					
Tennessee Gas Pipeline	1,787,976	1,787,976	1,787,976	595,992	-
East Tennessee Natural Gas	757,460	757,460	757,460	-	-
Saltville Natural Gas	1,870,560	1,548,030	580,440	435,330	-
Demand Total	$ 17,752,228	$ 17,429,698	$ 16,462,108	$ 4,869,766	$ -

Firm obligations related to purchased gas – commodity

	2017	**2018**	**2019**	**2020**	**2021**
Baseload					
Conoco	$ 5,719,700	$ -	$ -	$ -	$ -
Shell Energy	739,680	-	-	-	-
BP	6,104,693	6,181,363	5,874,650	1,801,950	-
CNX	1,709,713	1,648,048	-	-	-
Commodity Total	$ 14,273,786	$ 7,829,411	$ 5,874,650	$ 1,801,950	$ -

The total commodity values presented here are based upon firm supply obligations with each individual natural gas supplier. The firm obligations value for Conoco, Shell Energy, and BP are based upon firm supply obligations and locked prices with those suppliers. The firm obligations value for the CNX contract is based upon firm supply obligations and the applicable four month NYMEX strip prices on June 30, 2016.

15. Other Commitments and Contingencies

In the normal course of business, there are various lawsuits pending against KUB. Management has reviewed these lawsuits with counsel, who is vigorously defending KUB's position and is of the opinion that the ultimate disposition of these matters will not have a material adverse effect on KUB's financial position, results of operations or cash flows.

In February 2005, a Consent Decree was entered into federal court regarding the operation of KUB’s wastewater system. Under the terms of the Consent Decree, the remediation of identified sanitary sewer overflows (SSOs) on KUB’s wastewater system had to be completed by June 30, 2016. KUB completed all the requirements of the Consent Decree for the collection system two years in advance of the deadline.

The Consent Decree also required KUB to perform an evaluation of the wet weather performance and capacity of its wastewater treatment plants. In July 2007, KUB submitted a Composite Correction Plan (CCP) for its wastewater treatment plants to EPA for review. The development and filing of the CCP was a requirement of the federal order of February 2005. The CCP includes recommended improvements to KUB's Kuwahee and Fourth Creek treatment plants to address wet weather capacity issues noted in prior assessments. The EPA approved the CCP in January 2009 including a recommended schedule of plant improvements that extends beyond the expiration date of the original Consent Decree. An amendment to the Consent Decree incorporating and establishing this schedule was agreed to by all parties and was entered on June 23, 2009. The purpose of the Amendment is to allow KUB to complete a portion of work outlined in the CCP after the Consent Decree deadline of June 30, 2016. The CCP provides for a biologically enhanced high-rate clarification (the BEHRC) secondary treatment system to be installed at the Fourth Creek treatment plant by June 30, 2018 and at the Kuwahee treatment plant by June 30, 2021. The total cost of such improvements is estimated to be approximately $120 million.

KUB's funding plan for the Consent Decree includes long-term bonds and a series of rate increases phased in over the term of the order. Bond proceeds fund all types of wastewater capital projects, the majority of which are related to the Consent Decree. As of June 30, 2016, the Wastewater Division had issued $485 million in bonds to fund system capital improvements since the inception of the Consent Decree. The Board previously approved two 50 percent rate increases, which went into effect in April 2005 and January 2007. The Board also approved an 8 percent rate increase, which was effective in September 2008, two 12 percent rate increases, which were effective in April 2011 and October 2012, and three 6 percent rate increases effective October 2014, October 2015 and October 2016. KUB anticipates additional bond issues and rate increases over the next decade to help fund wastewater capital improvements.

KUB successfully completed the first cycle of Maintenance Operation Management (MOM) requirements one year before the deadline by inspecting 99.5% of manholes and gravity mains, smoke testing 99.9% of gravity mains, performing required inspections of pump stations and the related force mains, and completing all Corrective Action Plan/Engineering Report (CAP/ER) projects. KUB initiated the second MOM cycle that continues to focus on the prevention of SSOs. As part of the Century II initiative, formally known as the PACE10 program, KUB has installed storage tanks providing 34 million gallons of wastewater storage to control wet weather overflows and rehabilitated or replaced approximately 334.9 miles of collection system pipe. KUB also continues to maintain a proactive operations and maintenance plan for the wastewater collection system including inspection, grease control, and private lateral enforcement. The result of the PACE10/Century II initiative has been an 82 percent reduction in SSOs.

As of June 30, 2016, the Wastewater Division had completed its twelfth full year under the Consent Decree, spending $529.5 million on capital investments to meet Consent Decree requirements. During fiscal year 2016, the Wastewater Division incurred $37.3 million in total expenditures related to Consent Decree requirements, including $3.3 million for operating costs and $34 million in capital improvements which included the rehabilitation or replacement of 28 miles of wastewater main. During the fiscal year, $26.5 million was spent on sewer mini-basin rehabilitation and replacement. Trunk line rehabilitation and replacement accounted for $2 million of capital expenditures, while pump station improvements accounted for $4.6 million.

16. Segment Information

The following financial information represents identifiable activities for which the revenue bonds and other revenue backed debt are outstanding for the respective Divisions:

Condensed Statement of Net Position

	2016			
	Electric	**Gas**	**Water**	**Wastewater**
Assets and Deferred Outflows of Resources				
Current assets	$ 105,152,996	$ 28,023,783	$ 20,524,335	$ 44,214,264
Restricted assets	14,749,362	3,149,495	3,356,910	7,701,096
Net capital assets	511,260,136	263,531,420	281,257,624	687,055,971
Other assets	37,107,982	16,503,157	10,007,552	28,159,669
Total assets	$ 668,270,476	$ 311,207,855	$ 315,146,421	$ 767,131,000
Deferred outflows of resources	8,543,965	3,004,672	3,273,002	19,413,063
Total assets and deferred outflows of resources	$ 676,814,441	$ 314,212,527	$ 318,419,423	$ 786,544,063
Liabilities and Deferred Inflows of Resources				
Current liabilities	$ 87,318,966	$ 16,464,233	$ 10,801,558	$ 19,868,558
Other liabilities	16,598,461	3,410,619	2,295,413	2,761,018
Long-term debt	237,603,282	100,163,853	142,132,182	492,466,224
Total liabilities	$ 341,520,709	$ 120,038,705	$ 155,229,153	$ 515,095,800
Deferred inflows of resources	725,888	257,085	196,595	332,699
Total liabilities and deferred inflows of resources	$ 342,246,597	$ 120,295,790	$ 155,425,748	$ 515,428,499
Net position				
Net investment in capital assets	$ 268,462,479	$ 159,696,458	$ 138,069,365	$ 205,783,783
Restricted	10,120,406	1,820,408	1,522,884	2,737,312
Unrestricted	55,984,959	32,399,871	23,401,426	62,594,469
Total net position	$ 334,567,844	$ 193,916,737	$ 162,993,675	$ 271,115,564

Condensed Statement of Net Position

	2015			
	Electric	**Gas**	**Water**	**Wastewater**
Assets and Deferred Outflows of Resources				
Current assets	$ 113,395,720	$ 45,488,784	$ 27,984,680	$ 42,523,912
Restricted assets	33,517,297	3,119,403	12,903,096	22,712,158
Net capital assets	480,797,659	248,032,207	258,138,759	664,178,585
Other assets	43,446,286	14,911,384	14,195,562	38,863,004
Total assets	$ 671,156,962	$ 311,551,778	$ 313,222,097	$ 768,277,659
Deferred outflows of resources	5,410,730	1,925,346	2,459,219	18,592,703
Total assets and deferred outflows of resources	$ 676,567,692	$ 313,477,124	$ 315,681,316	$ 786,870,362
Liabilities and Deferred Inflows of Resources				
Current liabilities	$ 85,227,269	$ 16,716,438	$ 9,361,281	$ 17,928,132
Other liabilities	16,261,143	3,352,842	1,634,788	2,052,891
Long-term debt	248,330,326	105,919,404	146,856,890	503,955,190
Total liabilities	$ 349,818,738	$ 125,988,684	$ 157,852,959	$ 523,936,213
Deferred inflows of resources	3,061,589	1,148,096	829,180	1,339,445
Total liabilities and deferred inflows of resources	$ 352,880,327	$ 127,136,780	$ 158,682,139	$ 525,275,658
Net position				
Net investment in capital assets	$ 228,768,196	$ 138,973,111	$ 110,579,425	$ 172,143,725
Restricted	9,091,195	1,801,334	1,375,362	2,623,864
Unrestricted	85,827,974	45,565,899	45,044,390	86,827,115
Total net position	$ 323,687,365	$ 186,340,344	$ 156,999,177	$ 261,594,704

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Condensed Statement of Revenues, Expenses and Changes in Net Position

	2016			
	Electric	**Gas**	**Water**	**Wastewater**
Operating revenues	$ 521,369,202	$ 88,441,144	$ 47,453,401	$ 83,645,509
Operating expenses	472,905,855	65,567,807	27,052,009	36,048,577
Provision for depreciation	29,490,370	11,481,432	9,055,221	18,342,674
Total operating expenses	502,396,225	77,049,239	36,107,230	54,391,251
Operating income	18,972,977	11,391,905	11,346,171	29,254,258
Non-operating expense	(8,270,894)	(3,815,512)	(5,652,869)	(20,424,080)
Change in net position before capital contributions	10,702,083	7,576,393	5,693,302	8,830,178
Capital contributions	178,396	-	301,196	690,682
Change in net position	10,880,479	7,576,393	5,994,498	9,520,860
Net position				
Beginning of year	323,687,365	186,340,344	156,999,177	261,594,704
End of year	$ 334,567,844	$ 193,916,737	$ 162,993,675	$ 271,115,564

Condensed Statement of Revenues, Expenses and Changes in Net Position

	2015			
	Electric	**Gas**	**Water**	**Wastewater**
Operating revenues	$ 533,205,845	$ 114,168,784	$ 44,173,190	$ 79,206,028
Operating expenses	489,617,790	86,845,366	26,315,917	35,189,854
Provision for depreciation	25,887,777	10,894,826	7,794,763	17,130,721
Total operating expenses	515,505,567	97,740,192	34,110,680	52,320,575
Operating income	17,700,278	16,428,592	10,062,510	26,885,453
Non-operating expense	(6,642,081)	(4,272,667)	(5,309,339)	(19,486,890)
Change in net position before capital contributions	11,058,197	12,155,925	4,753,171	7,398,563
Capital contributions	11,611	4,353	232,696	357,246
Change in net position	11,069,808	12,160,278	4,985,867	7,755,809
Net position				
Beginning of year, as previously reported	312,984,264	174,317,582	152,112,627	253,999,330
Change in method of accounting for pension	(366,707)	(137,516)	(99,317)	(160,435)
Net position, beginning of year, as restated	312,617,557	174,180,066	152,013,310	253,838,895
End of year	$ 323,687,365	$ 186,340,344	$ 156,999,177	$ 261,594,704

Condensed Statement of Cash Flows

	2016			
	Electric	**Gas**	**Water**	**Wastewater**
Net cash provided by operating activities	$ 50,904,883	$ 22,442,923	$ 20,792,761	$ 48,518,765
Net cash used in capital and related financing activities	(59,358,278)	(36,629,153)	(32,331,239)	(56,922,694)
Net cash provided by (used in) investing activities	(1,226,670)	(1,040,540)	(373,199)	(723,696)
Net increase (decrease) in cash and cash equivalents	(9,680,065)	(15,226,770)	(11,911,677)	(9,127,625)
Cash and cash equivalents, beginning of year	44,471,851	26,262,919	21,304,494	32,853,270
Cash and cash equivalents, end of year	$ 34,791,786	$ 11,036,149	$ 9,392,817	$ 23,725,645

Condensed Statement of Cash Flows

	2015			
	Electric	**Gas**	**Water**	**Wastewater**
Net cash provided by operating activities	$ 38,410,104	$ 28,984,668	$ 17,603,576	$ 42,595,872
Net cash used in capital and related financing activities	(22,524,068)	(46,023,953)	(17,392,294)	(22,961,641)
Net cash provided by (used in) investing activities	(2,886,436)	(712,007)	5,914,751	(2,194,880)
Net increase (decrease) in cash and cash equivalents	12,999,600	(17,751,292)	6,126,033	17,439,351
Cash and cash equivalents, beginning of year	31,472,251	44,014,211	15,178,461	15,413,919
Cash and cash equivalents, end of year	$ 44,471,851	$ 26,262,919	$ 21,304,494	$ 32,853,270

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Knoxville Utilities Board
Required Supplementary Information - Schedule of Funding Progress
June 30, 2016
(Unaudited)

Other Post-Employment Benefits (OPEB)

	Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a)/(b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b)-(a)]/(c)
	January 1, 2008	$ -	$ 108,329,141	$ 108,329,141	0%	$ 31,234,509	346.8%
	January 1, 2009	14,593,487	100,726,738	86,133,251	14%	31,846,091	270.5%
	January 1, 2010	21,275,643	58,475,364	37,199,721	36%	30,069,028	123.7%
	January 1, 2011	40,749,815	64,289,254	23,539,439	63%	28,878,791	81.5%
	January 1, 2012	37,907,357	61,603,466	23,696,109	62%	28,269,123	83.8%
	January 1, 2013	38,571,803	63,341,531	24,769,728	61%	27,566,340	89.9%
	January 1, 2014	43,409,955	46,889,808	3,479,853	93%	26,724,154	13.0%
*	January 1, 2015	47,705,478	47,745,640	40,162	100%	25,816,884	0.2%
*	January 1, 2016	48,510,796	45,118,624	(3,392,172)	108%	25,243,127	(13.4%)

***** The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Knoxville Utilities Board
Required Supplementary Information - Schedule of Changes in Net Pension Liability and Related Ratios
June 30, 2016
(Unaudited)

	Year ended December 31	
	2015	**2014**
Total pension liability		
Service cost	$ 4,157,062	$ 4,092,808
Interest	14,812,784	14,698,657
Differences between expected and actual experience	(1,890,334)	-
Benefit payments, including refunds of member contributions	(15,350,926)	(15,533,167)
Net change in total pension liability	1,728,586	3,258,298
Total pension liability - beginning	202,773,764	199,515,466
Total pension liability - ending (a)	$ 204,502,350	$ 202,773,764
Plan fiduciary net position		
Contributions - employer	$ 5,991,887	$ 5,908,541
Contributions - participants	487,546	475,854
Net investment income	(95,430)	22,292,369
Other additions	30,879	29,733
Benefit payments, including refunds of member contributions	(15,274,926)	(15,405,167)
Administrative expense	(397,160)	(378,085)
Death benefits	(76,000)	(128,000)
Net change in plan fiduciary net position**	(9,333,204)	12,795,245
Plan fiduciary net position - beginning**	208,795,394	196,000,149
Plan fiduciary net position - ending (b)**	$ 199,462,190	$ 208,795,394
Plan's net pension liability - ending (a) - (b)	$ 5,040,160	$ (6,021,630)
Plan fiduciary net position as a percentage of the total pension liability	97.54%	102.97%
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Plan's net pension liability as a percentage of covered-employee payroll	9.95%	(11.98%)

Notes to Schedule:

* Information not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented in 2014.

** Excludes amounts related to 401(k) matching contributions.

Knoxville Utilities Board
Required Supplementary Information - Schedule of Employer Pension Contributions
June 30, 2016
(Unaudited)

	Year ended December 31 2015	 2014
Annual required contribution	$ 5,991,887	$ 5,908,541
Contribution in relation to the annual required contribution	5,991,887	5,908,541
Contribution deficiency	$ -	$ -
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Contributions as a percentage of covered-employee payroll	11.82%	11.76%

Notes to Schedule:

Valuation Dates:	January 1, 2013 and January 1, 2014
Timing:	Actuarially determined contributions for a plan year are based upon 50% of the amounts determined at the actuarial valuations for each of the two prior plan years.

Key methods and assumptions used to determine contribution rates:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014.
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.8% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the Janaury 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation.
Inflation:	2.8 percent

* Schedule of Employer Contribution information is not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented 2014.

Knoxville Utilities Board

Supplemental Information –
Schedule of Expenditures of Federal Awards and State Financial Assistance
June 30, 2016 Schedule 1

KUB was awarded a grant from Tennessee Emergency Management Agency (as a flow through from FEMA) for reimbursement for costs related to storms in 2015. The schedule below shows the expenditures for the current fiscal year.

Program Name	Federal/State Agency	CFDA Number	Contract Number	Expenditures
U.S. Department of Homeland Security	Tennessee Emergency Management	97.036	34101-06616	$ 1,325,524
		Total Program 97.036		$ 1,325,524
		Total Federal Awards		$ 1,325,524

NOTE 1 - BASIS OF PRESENTATION

The Schedule of Expenditures of Federal Awards and State Financial Assistance includes the federal award related grant activity of Knoxville Utilities Board and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Section I -- Summary of Auditors' Results

Financial Statements

Type of auditors' report issued:	Unmodified
Internal control over financial reporting: Material weakness(es) identified?	None reported
Significant deficiency(s) identified not considered to be material weaknesses?	None reported
Noncompliance material to financial statements:	None reported

Federal Awards

Internal control over major programs: Material weakness(es) identified?	None reported
Significant deficiency(s) identified not considered to be material weaknesses?	None reported
Type of auditors' report issued on compliance for major programs:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with Title 2 U.S. Code of Federal Regulations Part 200?	None reported

Identification of major programs:

CFDA	Name of Program
97.036	Tennessee Emergency Management

Dollar threshold used to distinguish between Type A and Type B programs:	$750,000
Auditee qualified as low-risk auditee?	No

Section II -- Financial Statement Findings

None reported.

Section III -- Federal Award Findings and Questioned Costs

None reported.

Section IV – Summary Schedule of Prior Year Audit Findings

Not applicable as there were no prior year findings reported.

Section V – Corrective Action Plan

Not applicable as there were no current year findings reported.

Knoxville Utilities Board
Supplemental Information - Schedule of Insurance in Force
June 30, 2016
(Unaudited) Schedule 3

Crime
Covers losses resulting from employee dishonesty, robbery, burglary, and computer fraud. Limits of coverage - $5,000,000; $250,000 retention.

Directors' and Officers' Liability Insurance
Covers KUB personnel appropriately authorized to make decisions on behalf of KUB (including but not limited to Commissioners, President and CEO, Senior Vice Presidents, Vice Presidents, and Directors) for wrongful acts. Limits of coverage - $20,000,000; $1,000,000 corporate deductible, $0 individual deductible.

Employment Practices Liability
Coverage for costs related to actual or alleged employment practices violations for amounts exceeding specified amount ($500,000). Limits of coverage - $10,000,000.

Fiduciary
Covers losses resulting from wrongful acts related to KUB's Pension, 401(k), and OPEB Trust funds. Limits of coverage - $10,000,000; $150,000 deductible.

Pollution Legal Liability
New conditions coverage for losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - $20,000,000.

Property Insurance
This coverage provides protection of KUB's property for fire, extended coverage, vandalism and malicious mischief, and coverage on boilers and machinery. Also included are flood and earthquake damage and mechanical failure. Limits of coverage - $250,000,000 per occurrence (subject to certain sublimits); $2,500,000 deductible per occurrence.

Travel Accident
Covers losses related to employees' business travel. Limits of coverage - $1,500,000 aggregate.

Excess Insurance for General Liability
As a government entity, KUB's liability is limited under the Tennessee Governmental Tort Liability Act (TCA §29-20-403). KUB is self-insured for up to the first $700,000 of any accident and has insurance of $1,000,000 above this retention.

Excess Insurance for Workers' Compensation
Covers all losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - Statutory; stop loss coverage applies for aggregate losses over $5,000,000.

Employee Health Plan Stop Loss Coverage
KUB's employee health plan is self-funded. KUB has purchased stop loss insurance, which covers KUB's exposure to annual expenses in excess of $400,000 per individual participant.

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

Board of Commissioners
Knoxville Utilities Board
Knoxville, Tennessee

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Knoxville Utilities Board (KUB), a component unit of the City of Knoxville, Tennessee, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise KUB's basic financial statements, and have issued our report thereon dated October 27, 2016.

Internal Control over Financial Reporting

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

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

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

Board of Commissioners
Knoxville Utilities Board
Knoxville, Tennessee

Compliance and Other Matters

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

Purpose of Report

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

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

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Report of Independent Auditors on Compliance for Each Major Program and on Internal Control over Compliance Required by the Uniform Guidance

Board of Commissioners
Knoxville Utilities Board
Knoxville, Tennessee

Report on Compliance for the Major Federal Program

We have audited the Knoxville Utilities Board's (KUB), a component unit of the City of Knoxville, Tennessee, compliance with the types of compliance requirements described in the OMB Compliance Supplement that could have a direct and material effect on KUB's major federal program for the year ended June 30, 2016. KUB's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for KUB's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about KUB's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of KUB's compliance.

Board of Commissioners
Knoxville Utilities Board
Knoxville, Tennessee

Opinion on the Major Federal Program

In our opinion, KUB complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2016.

Report on Internal Control over Compliance

Management of KUB is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered KUB's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of KUB's internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

KUB
Knoxville Utilities Board

Electric Division

Financial Statements and Supplemental Information
June 30, 2016 and 2015

KUB Board of Commissioners

Nikitia Thompson - Chair

Sara Hedstrom Pinnell - Vice Chair

Dr. Jerry W. Askew

Kathy Hamilton

Celeste Herbert

Eston Williams

John Worden

Management

Mintha Roach
President and
Chief Executive Officer

Bill Elmore
Executive Vice President and
Chief Operating Officer

Mark Walker
Senior Vice President and
Chief Financial Officer

Susan Edwards
Senior Vice President and
Chief Administrative Officer

Eddie Black
Senior Vice President

Mike Bolin
Vice President

Julie Childers
Vice President

Derwin Hagood
Vice President

Dawn Mosteit
Vice President

Paul Randolph
Vice President

Dennis Upton
Vice President

Knoxville Utilities Board Electric Division

Index

June 30, 2016 and 2015

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Report of Independent Auditors

Board of Commissioners
Electric Division of the Knoxville Utilities Board
Knoxville, Tennessee

We have audited the accompanying financial statements of the Electric Division (the Division) of the Knoxville Utilities Board, a component unit of the City of Knoxville, Tennessee, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements as listed in the index.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Division'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 Division'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 the Electric Division of the Knoxville Utilities Board as of June 30, 2016 and 2015, and the changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Commissioners
Electric Division of the Knoxville Utilities Board
Knoxville, Tennessee

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 24 and the required supplementary information on pages 52 through 54 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Division's basic financial statements. The supplemental information on schedules 3 through 5, as listed on the index, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards and state financial assistance is presented for purposes of additional analysis as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, and the State of Tennessee Comptroller of the Treasury Office and is also not a required part of the basic financial statements.

The schedule of expenditures of federal awards and state financial assistance is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards and state financial assistance is fairly stated in all material respects in relation to the basic financial statements as a whole.

The supplemental information on schedules 3 through 5 have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 27, 2016, on our consideration of the Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

Knoxville Utilities Board (KUB), comprised of the Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions. The Electric Division (Division) provides services to certain customers in Knox County and in seven surrounding counties in East Tennessee. The Division's accounts are maintained in conformity with the Uniform System of Accounts of the Federal Energy Regulatory Commission and the Governmental Accounting Standards Board, as applicable. The financial statements present only the Electric Division and do not purport to, and do not, present fairly the consolidated financial position of Knoxville Utilities Board at June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Division's discussion and analysis is designed to (a) assist the reader in focusing on significant financial issues, (b) provide an overview of the Division's financial activity, (c) identify major changes in the Division's financial position, and (d) identify any financial concerns.

The Division's Management Discussion and Analysis (MD&A) focuses on the fiscal year ending June 30, 2016 activities, resulting changes and current known facts, and should be read in conjunction with the Division's financial statements.

Electric Division Highlights

System Highlights

KUB serves 202,843 electric customers over a 688 square mile service area and maintains 5,321 miles of service lines and 63 electric substations to provide 5.6 million megawatt hours to its customers annually.

KUB's electric system experienced a record peak in demand of 1,328 megawatt hours in February 2015. KUB's electric system had a strong year for reliability with only 1.82 hours of service interruption for the average customer in fiscal year 2016.

KUB has added 4,487 electric system customers over the past three years representing annual growth of less than one percent.

The typical residential customer's average monthly electric bill was $101.78 as of June 30, 2016, representing an increase of $0.49 or 0.5 percent compared to June 30, 2015. The increase in the monthly bill during fiscal year 2016 was the net result of the flow through of TVA wholesale rate adjustments, previously over recovered wholesale power costs and KUB's one percent electric rate increase, which added $1.00 to the monthly residential customer charge.

KUB's electric system was impacted by an ice storm event in February 2015 that resulted in a cost of $2 million to the system. KUB received $1.6 million in reimbursements in fiscal year 2016 from the Federal Emergency Management Agency (FEMA) to offset the cost of the 2015 event.

KUB's electric system was awarded the Diamond level designation by the American Public Power Association's (APPA) Reliable Public Power Provider (RP3) program, the highest level of recognition of the program.

Century II Infrastructure Program

Century II is KUB's proactive long-range program to improve and maintain its electric, natural gas, water and wastewater systems for its customers. It includes the maintenance and asset replacement strategies for each utility system and establishes sustainable replacement cycles. Century II moves KUB into its second century of service by improving each system through sound planning, resource allocation, and continued, but accelerated, investment.

KUB's Century II programs were resumed in 2011, after a break due to the economic recession. At that time, the KUB Board of Commissioners endorsed a ten year funding plan for the Electric Division, which includes a combination of rate increases and debt issues to fully fund the electric system's Century II program.

In April 2014, KUB management provided the Board an updated assessment of the overall condition of each utility system, including a recommendation for annual rate increases for each division for the next three fiscal years.

In June 2014, the Board approved the proposed three annual rate increases for the Electric Division. The first and second rate increases went into effect in July 2014 and July 2015. In July 2016, the third and final rate increase will go into effect and will generate $5.2 million in additional annual Electric Division revenue.

In fiscal year 2015, KUB concluded the smart grid pilot project, of which a portion of the project was funded by a United States Department of Energy Smart Grid Investment Grant (SGIG). This grant was received by KUB in 2009 as part of the American Reinvestment and Recovery Act (ARRA). Based upon the success of that pilot, KUB formed a plan to move forward with a Century II Grid Modernization initiative, which includes advanced metering for all KUB customers, a telecommunication system linking critical KUB infrastructure, and an increased investment in automation technology to help operate KUB's energy and water distribution systems.

During the fiscal year, KUB replaced 2,208 poles, exceeding the target level of 2,000, and replaced 13.3 miles of underground electric cable while staying on track with Century II goals and within the Electric Division's total capital budget.

Financial Highlights

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division's net position during the year increased $10.9 million compared to an $11.1 million increase last fiscal year. A restatement to fiscal year 2014's net position based on a change in method of accounting for pension expense reduced the total net position by $0.4 million during fiscal year 2015. This change resulted in a net increase of $10.7 million in the Division's net position during fiscal year 2015.

Operating revenue decreased $11.8 million or 2.2 percent over the prior fiscal year. The decrease in operating revenue was the net result of additional revenue from KUB's one percent electric rate increase, the flow through of TVA rate adjustments, a 3.1 percent decline in total power sales, and the flow through of prior year over recovered purchase power costs to electric customers. KUB flows changes to wholesale power rates directly through to its retail electric rates via its Purchased Power Adjustment.

Seventy nine percent of Electric Division sales revenue was used to purchase electric power from TVA for the fiscal year ended June 30, 2016. Purchased power expense decreased $17.2 million compared to last year, due a very mild winter that resulted in a 3.1 percent decline in total power sales. Lower sales mitigated the impact of a 1.5 percent wholesale power rate increase from TVA.

Margin on electric sales (operating revenue less purchased power expense) increased $5.3 million or 4.7 percent, reflecting additional revenue from the KUB electric rate increases.

Operating expenses (excluding purchased power expense) increased $4.1 million or 4.2 percent. Depreciation expense increased $3.6 million or 13.9 percent. Taxes and tax equivalents were $0.7 million, or 4.8 percent, higher than the prior fiscal year. Operating and maintenance (O&M) expenditures decreased $0.3 million or 0.5 percent.

Interest income was $0.2 million more than the prior fiscal year. Interest expense increased $0.7 million or 8.3 percent, primarily due to the additional interest accrued on long-term bonds issued in August 2014 and April 2015.

Capital contributions increased $0.2 million, reflecting a higher level of electric system assets provided to KUB during the fiscal year.

Total plant assets (net) increased $30.5 million or 6.3 percent over the end of the last fiscal year reflecting pole replacements and other distribution system improvements as part of KUB's Century II electric program.

Long-term debt represented 41.6 percent of the Division's capital structure as of June 30, 2016, compared to 43.3 percent last year. Capital structure equals long-term debt (including the current and long-term portion of any revenue bonds and notes) plus net position.

The Division's bond covenants require a debt service coverage ratio of at least 1.2 times the maximum principal and interest payments over the life of the Division's outstanding bonds. Current year debt coverage for the fiscal year was 3.57. Maximum debt service coverage was 3.28.

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division's net position during the year increased $11.1 million compared to a $12 million increase last fiscal year. A restatement to the prior fiscal year's net position based on a change in method of accounting for pension expense reduced the total net position by $0.4 million during fiscal year 2015. This change resulted in a net increase of $10.7 million in the Division's net position.

Operating revenue increased $5.4 million or one percent over the prior fiscal year. The increase in operating revenue was the net result of additional revenue from KUB's one percent electric rate increase, the flow through of TVA rate adjustments and the flow through of prior year over recovered purchase power costs to electric customers. KUB flows changes to wholesale power rates directly through to its retail electric rates via its Purchased Power Adjustment.

Eighty-one percent of Electric Division sales revenue was used to purchase electric power from TVA for the fiscal year ended June 30, 2015. Purchased power expense increased $0.2 million compared to last year, due to a 1.5 percent wholesale power rate increase from TVA effective October 2014.

Margin on electric sales (operating revenue less purchased power expense) increased $5.2 million or 4.8 percent, reflecting additional revenue from the KUB electric rate increase.

Operating expenses (excluding purchased power expense) increased $6.8 million or 7.6 percent. Operating and maintenance (O&M) expenditures increased $2.7 million or 5.1 percent. Depreciation expense increased $2.7 million or 11.6 percent. Taxes and tax equivalents were $1.4 million, or 10.6 percent, higher than the prior fiscal year.

Interest income was consistent with the prior fiscal year. Interest expense increased $0.8 million or 10.5 percent, primarily due to the additional interest accrued on long-term bonds issued in August 2014 and April 2015.

Capital contributions decreased $0.3 million, reflecting fewer electric system assets provided to KUB during the fiscal year.

Total plant assets (net) increased $35.3 million or 7.9 percent over the end of the last fiscal year reflecting pole replacements and other distribution system improvements as part of KUB's Century II electric program.

KUB sold two series of electric system revenue bonds during fiscal year 2015 for the purpose of funding electric system capital improvements totaling $75 million. The $35 million bond issue in April 2015 was accelerated to take advantage of the low interest rate environment which impacted the Division's debt rate and debt service coverage levels for fiscal year 2015. Long-term debt represented 43.3 percent of the Division's capital structure as of June 30, 2015, compared to 36.4 percent last year. Capital structure equals long-term debt (including the current and long-term portion of any revenue bonds and notes) plus net position.

The Division's bond covenants require a debt service coverage ratio of at least 1.2 times the maximum principal and interest payments over the life of the Division's outstanding bonds. Current year debt coverage for the fiscal year was 3.8. Maximum debt service coverage was 3.06.

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Knoxville Utilities Board Electric Division - Financial Statements

The Division’s financial performance is reported under three basic financial statements: the Statement of Net Position; the Statement of Revenues, Expenses and Changes in Net Position; and the Statement of Cash Flows.

Statement of Net Position

The Division reports its assets, deferred outflows of resources, liabilities, deferred inflows of resources and net position in the Statement of Net Position. Assets are classified as current, restricted, electric plant in service, or other assets.

Liabilities are classified as current, other, or long-term debt. Net position is classified as net investment in capital assets; restricted; or unrestricted. Net position tells the user what the Division has done with its accumulated earnings, not just the balance.

Net investment in capital assets is the net book value of all capital assets less the outstanding balances of debt used to acquire, construct, or improve those assets.

Restricted net position includes assets that have been limited to specific uses by the Division’s bond covenants or through resolutions passed by the KUB Board.

Unrestricted net position is a residual classification; the amount remaining after reporting net position as either invested in capital or restricted is reported there.

Statement of Revenues, Expenses and Changes in Net Position

The Division reports its revenues and expenses (both operating and non-operating) on the Statement of Revenues, Expenses and Changes in Net Position. In addition, any capital contributions or assets donated by developers are reported on this statement.

Total revenue less total expense equals the change in net position for the reporting period. Net position at the beginning of the period is increased or decreased, as applicable, by the change in net position for the reporting period.

The change in net position for the reporting period is added to the net position segment of the Statement of Net Position.

Statement of Cash Flows

The Division reports its cash flows from operating activities, capital and related financing activities, and investing activities on its Statement of Cash Flows. This statement tells the user the Division’s sources and uses of cash during the reporting period.

The statement indicates the Division’s beginning cash balance and ending cash balance and how it was either increased or decreased during the reporting period.

The statement also reconciles cash flow back to operating income as it appears on the Statement of Revenues, Expenses and Changes in Net Position.

Condensed Financial Statements

Statement of Net Position

The following table reflects the condensed Statement of Net Position for the Electric Division compared to the prior year and the year preceding the prior year.

Statements of Net Position
As of June 30

(in thousands of dollars)	**2016**	**2015**	**2014**
Current, restricted and other assets	$ 157,010	$ 190,359	$ 151,636
Capital assets, net	511,260	480,798	445,495
Deferred outflows of resources	8,544	5,411	1,415
Total assets and deferred outflows of resources	676,814	676,568	598,546
Current and other liabilities	103,918	101,489	108,777
Long-term debt outstanding	237,603	248,330	176,785
Deferred inflows of resources	726	3,062	-
Total liabilities and deferred inflows of resources	342,247	352,881	285,562
Net position			
Net investment in capital assets	268,462	228,768	262,995
Restricted	10,120	9,091	7,956
Unrestricted	55,985	85,828	42,033
Total net position	$ 334,567	$ 323,687	$ 312,984

Normal Impacts on Statement of Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Net Position presentation.

- Change in net position (from Statement of Revenues, Expenses and Changes in Net Position): impacts (increase/decrease) current and other assets and/or capital assets and unrestricted net position.
- Issuing debt for capital: increases deferred outflows of resources and long-term debt.
- Spending debt proceeds on new capital: reduces current assets and increases capital assets.
- Spending of non-debt related current assets on new capital: (a) reduces current assets and increases capital assets and (b) reduces unrestricted net position and increases net investment in capital assets.
- Principal payment on debt: (a) reduces current and other assets and reduces long-term debt and (b) reduces unrestricted net position and increases net investment in capital assets.
- Reduction of capital assets through depreciation: reduces capital assets and net investment in capital assets.

Impacts and Analysis

Current, Restricted and Other Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Current, restricted and other assets decreased $33.3 million or 17.5 percent. The decrease in current assets reflects the utilization of $20.5 million in bond proceeds, a decrease in general fund cash of $9.7 million and a decrease in accounts receivable of $4.1 million.

KUB under recovered $1.4 million in purchased power costs from its customers through its Purchased Power Adjustment mechanism in fiscal year 2016, as compared to a $0.5 million over recovery in fiscal year 2015. This under recovery of costs will be collected from customers next fiscal year through adjustments to rates via the Purchased Power Adjustment.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current, restricted and other assets increased $38.7 million or 25.5 percent. The increase in current assets reflects $20.5 million more in unused bond proceeds, an increase in general fund cash of $13 million, and a $3.2 million rise in operating contingency reserves.

Capital Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Capital assets, net of depreciation, increased $30.5 million or 6.3 percent. Major capital expenditures included $25.1 million for distribution system improvements, $7.7 million for pole replacements, $7 million for installation or replacement of electric services, $4.9 million for Grid Modernization, $4.1 million for upgrades to various information systems, $1.8 million for replacement and relocation of electric system assets to accommodate Tennessee Department of Transportation (TDOT) highway improvement projects, $1.4 million for trucks and equipment, and $1.4 million for street lighting improvements.

Fiscal Year 2015 Compared to Fiscal Year 2014

Capital assets, net of depreciation, increased $35.3 million or 7.9 percent. Major capital expenditures included $28.7 million for distribution system improvements, $6 million for pole replacements, $5.9 million for installation or replacement of electric services, $4 million for a new substation and $4 million for information system upgrades.

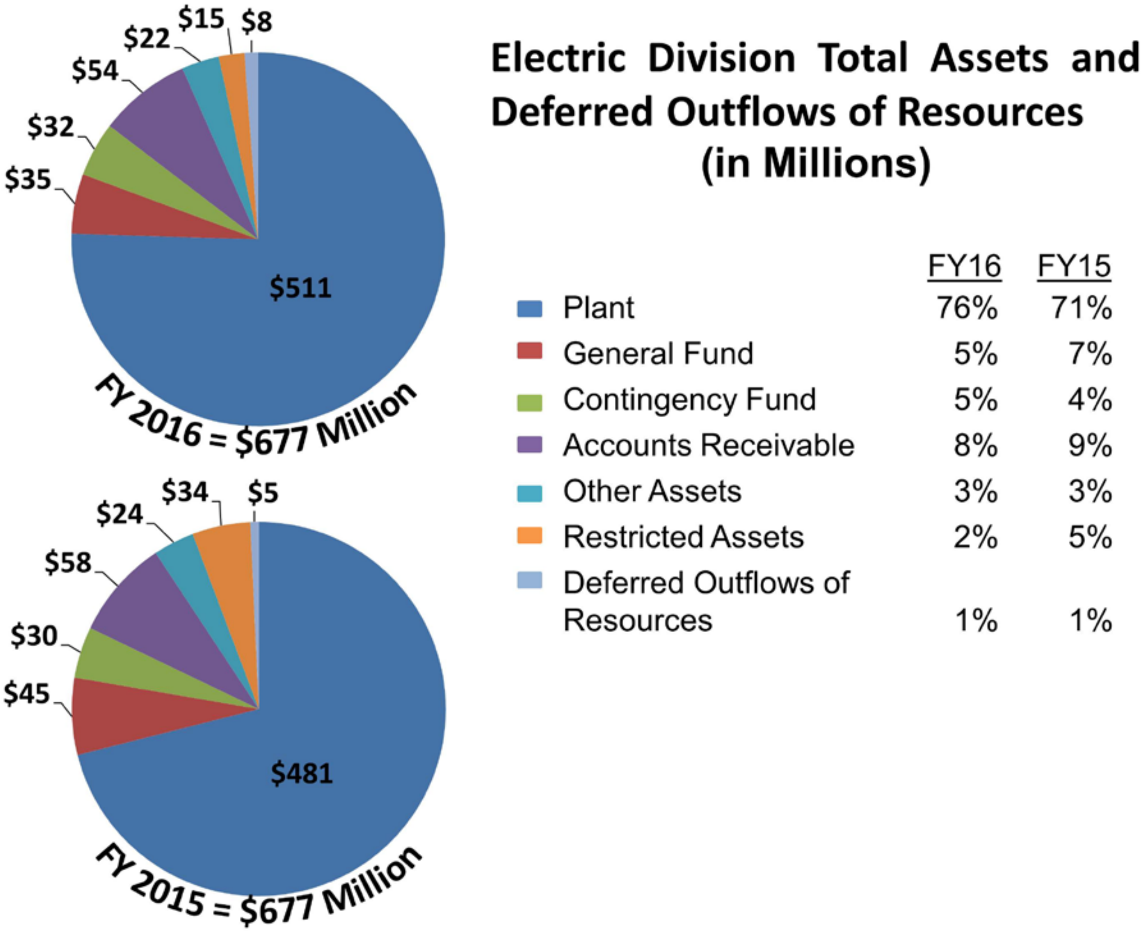
Deferred Outflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred outflows of resources increased $3.1 million compared to the prior fiscal year primarily due to an increase in pension outflow of $3.5 million.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred outflows of resources increased $4 million compared to the prior fiscal year, reflecting a $2.5 million increase in the amortization of deferred losses on bonds primarily attributable to bonds refunded in April 2015. Pension outflow increased $1.5 million.



Current and Other Liabilities

Fiscal Year 2016 Compared to Fiscal Year 2015

Current and other liabilities increased $2.4 million or 2.4 percent, due in part to an actuarially determined net pension obligation of $2.4 million recognized in fiscal year 2016. Accounts payable decreased $1.9 million, which was offset by a $1.7 million increase in accrued expenses. The outstanding balance on TVA conservation loans declined by $1.9 million, as KUB ceased issuance of any new loans in fiscal year 2016.

KUB over recovered $0.5 million in wholesale power costs from its customers in fiscal year 2015, as compared to a $1.4 million under recovery in fiscal year 2016. This over recovery of costs was flowed back to KUB's electric customers during fiscal year 2016 through adjustments to rates via the Purchased Power Adjustment.

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Fiscal Year 2015 Compared to Fiscal Year 2014

Current and other liabilities decreased $7.3 million or 6.7 percent, due in part to a $4.1 million decrease in accrued expenses from recognizing a $2.9 million net pension asset during the fiscal year compared to a $3 million pension contribution liability in the prior year. Accounts payable declined $1.4 million. The outstanding balance on TVA conservation loans fell $0.5 million. KUB over recovered $0.5 million in purchased power costs from its customers in fiscal year 2015, which was $3.9 million less than last fiscal year. The $0.5 million over recovery in fiscal year 2015 will be flowed back to KUB's electric customers next fiscal year through adjustments to electric rates via the Purchased Power Adjustment. Those decreases were offset by a $1.1 million increase in the current portion of revenue bonds payable.

Long-Term Debt

Fiscal Year 2016 Compared to Fiscal Year 2015

Long-term debt decreased $10.7 million or 4.3 percent primarily due to $10.1 million of long-term bond debt that shifted to current liabilities as payable within the next year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Long-term debt increased $71.5 million or 40.5 percent due to new debt issuances of $40 million in August 2014 and $35 million in April 2015 for the purpose of funding electric system capital improvements. The increase was partially offset by the scheduled repayment of bond debt.

Deferred Inflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred inflows decreased $2.3 million compared to the prior fiscal year due to differences in pension inflows.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred inflows increased $3.1 million compared to the prior fiscal year due to the change in valuation of pension liability creating a deferred inflow.

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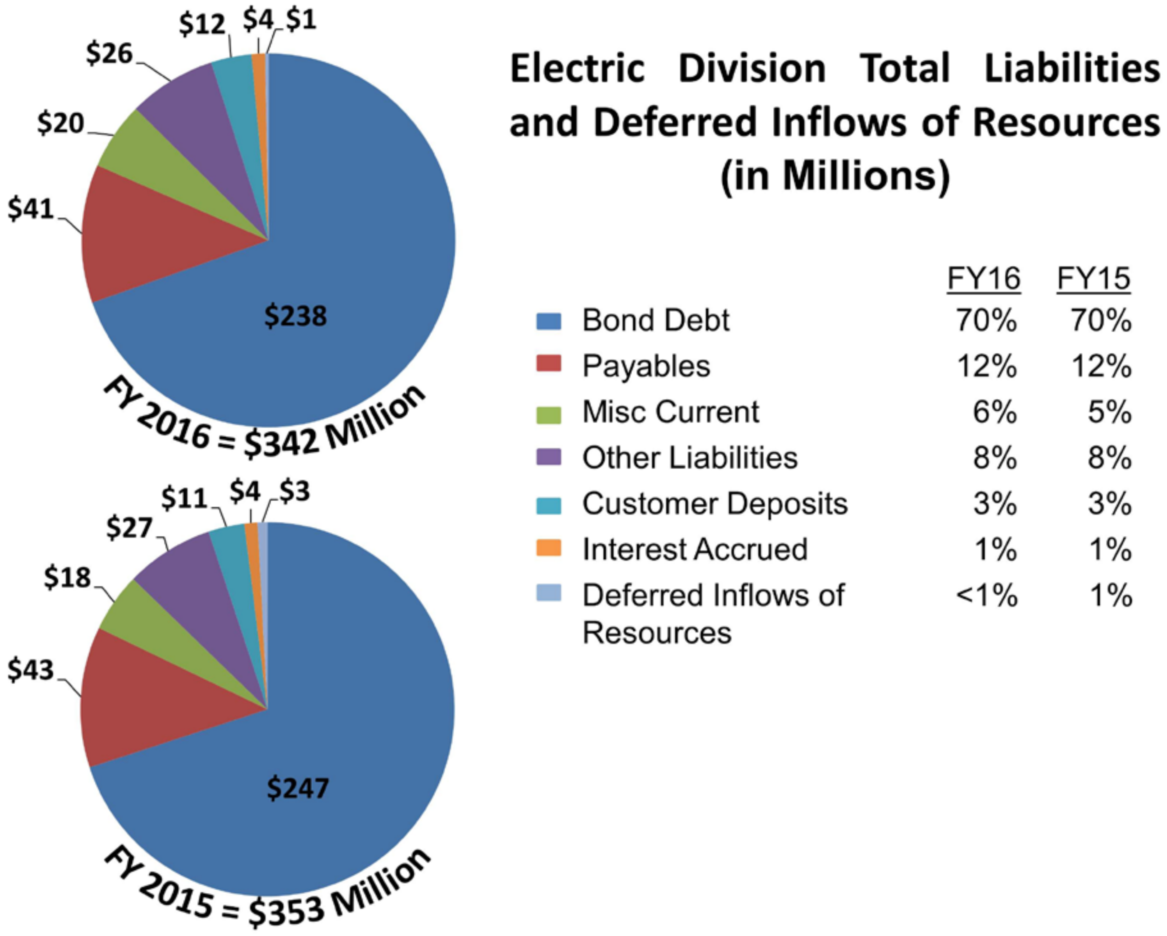

Electric Division Total Liabilities and Deferred Inflows of Resources (in Millions)

		FY16	FY15
🟦	Bond Debt	70%	70%
🟥	Payables	12%	12%
🟩	Misc Current	6%	5%
🟪	Other Liabilities	8%	8%
🟦	Customer Deposits	3%	3%
🟧	Interest Accrued	1%	1%
🟦	Deferred Inflows of Resources	<1%	1%

Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

Unrestricted net position decreased $29.8 million, primarily due to the $33.3 million decrease in current and other assets. Restricted net position increased $1 million, due to the net increase of the electric bond fund and the associated interest payable. Net investment in capital assets increased by $39.7 million or 17.4 percent. The increase was primarily the result of an increase of $30.5 million in net electric plant additions.

Fiscal Year 2015 Compared to Fiscal Year 2014

Unrestricted net position increased $43.8 million, primarily due to the $38.7 million increase in current and other assets. Restricted net position increased $1.1 million, due to the net increase of the electric bond fund and the associated interest payable. Net investment in capital assets decreased by $34.2 million or 13 percent. The decrease was primarily the result of an increase of $35.3 million of net electric plant additions offset by an increase of $68.1 million in long-term debt from new bond issuances.

Statement of Revenues, Expenses and Changes in Net Position

The following table reflects the condensed Statement of Revenues, Expenses and Changes in Net Position for the Electric Division compared to the prior year and the year preceding the prior year.

Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended June 30

(in thousands of dollars)	2016	2015	2014
Operating revenues	$ 521,369	$ 533,206	$ 527,833
Less: Purchased power expense	402,604	419,773	419,558
Margin from sales	118,765	113,433	108,275
Operating expenses			
Distribution	33,062	34,408	32,905
Customer service	6,589	6,546	5,858
Administrative and general	14,856	13,822	13,351
Depreciation	29,490	25,888	23,190
Taxes and tax equivalents	15,795	15,069	13,627
Total operating expenses	99,792	95,733	88,931
Operating income	18,973	17,700	19,344
Interest income	549	322	290
Interest expense	(9,258)	(8,549)	(7,739)
Other income/(expense)	438	1,585	(213)
Change in net position before capital contributions	10,702	11,058	11,682
Capital contributions	178	12	306
Change in net position	$ 10,880	$ 11,070	$ 11,988

Normal Impacts on Statement of Revenues, Expenses and Changes in Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Revenues, Expenses and Changes in Net Position presentation.

- Operating revenue is largely determined by the volume of electric power sales for the fiscal year. Any change (increase/decrease) in retail electric rates would also be a cause of change in operating revenue.

- Purchased power expense is determined by volume of power purchases from TVA for the fiscal year. Also, any change (increase/decrease) in TVA wholesale power rates would result in a change in purchased power expense.

- Operating expenses (distribution, customer service, administrative and general) are normally impacted by changes in areas including, but not limited to, labor costs (staffing, wage rates), active employee and retiree medical costs, and overhead line maintenance (tree trimming, pole inspection, etc.).

- Depreciation expense is impacted by plant additions and retirements during the fiscal year.

- Taxes and tax equivalents are impacted by plant additions/retirements, changes in property tax rates, and margin (operating revenue less purchased power expense) levels.

- Interest income is impacted by the level of interest rates and investments.

- Interest expense on debt is impacted by the level of outstanding debt and the interest rates on the outstanding debt.

- Other income/(expenses) is impacted by miscellaneous non-operating revenues and expenses.

- Capital contributions are impacted by a donation of facilities/infrastructure to KUB by developers and governmental agencies. The contributions are recognized as revenue and recorded as plant in service based on the fair market value of the asset(s).

Impacts and Analysis

Change in Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division's net position increased $10.9 million, which was $0.2 million less than last year's $11.1 million increase. A restatement to fiscal year 2014's net position based on a change in method of accounting for the pension reduced the total net position by $0.4 million during fiscal year 2015 to $10.7 million. The lower earnings were attributable to the net effect of a $5.3 million increase in margin on sales, a $4.1 million rise in operating expenses, a $0.7 million increase in interest expense and a $1.1 million decrease in other income.

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division's net position increased $11.1 million, which was $0.9 million less than last year's $12 million increase. A restatement to the prior fiscal year's net position based on a change in method of accounting for the pension reduced the total net position by $0.4 million during fiscal year 2015 to $10.7 million. The lower earnings were attributable to the net effect of a $5.2 million increase in margin on sales, a $6.8 million rise in operating expenses, a $0.8 million increase in interest expense, a $1.8 million increase in other income and a $0.3 million decrease in capital contributions.

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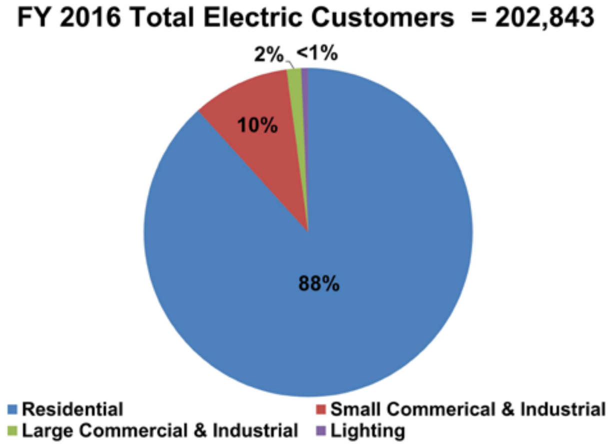
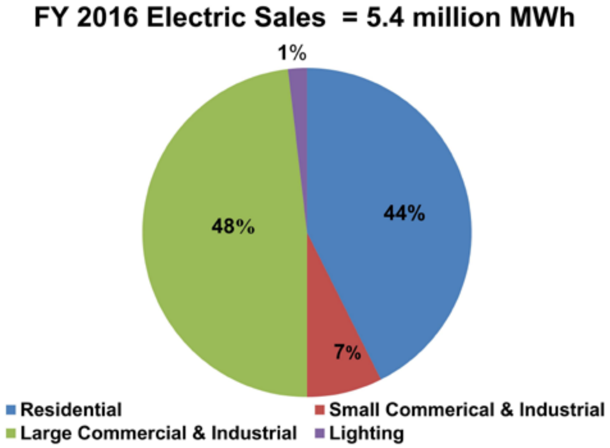
Margin from Sales

Fiscal Year 2016 Compared to Fiscal Year 2015

Margin on electric sales grew $5.3 million, reflecting higher revenues due to the July 2014 and July 2015 rate increases.

Operating revenue decreased $11.8 million or 2.2 percent, reflecting the net result of additional revenue from KUB’s one percent electric rate increase effective July 2015 and the flow through of TVA rate adjustments, offset by the second mildest winter in the last forty years. The milder winter resulted in a 3.1 percent decline in total power sales volumes. Purchased power expense decreased $17.2 million over last year. Power sales of 5.4 million MWh were 0.1 million MWh less than the prior fiscal year.





Residential customers represented 88 percent of total electric system customers and accounted for 44 percent of electric sales volumes for the year. Large commercial and industrial customers accounted for the largest portion of total sales volumes for the year, which was consistent with the prior year due to a steady customer base. KUB’s ten largest electric customers accounted for 16.2 percent of KUB’s billed volumes. Those ten customers represent five industrial and five commercial customers, including two governmental customers. Sales to Gerdau Ameristeel, KUB’s largest industrial customer, accounted for 5.7 percent of total electric system sales.

KUB has added 4,487 electric system customers over the past three years, representing annual growth of less than one percent.

Electric sales volumes have remained consistent over the past three years with fiscal year 2016 residential sales being impacted by the mild winter.

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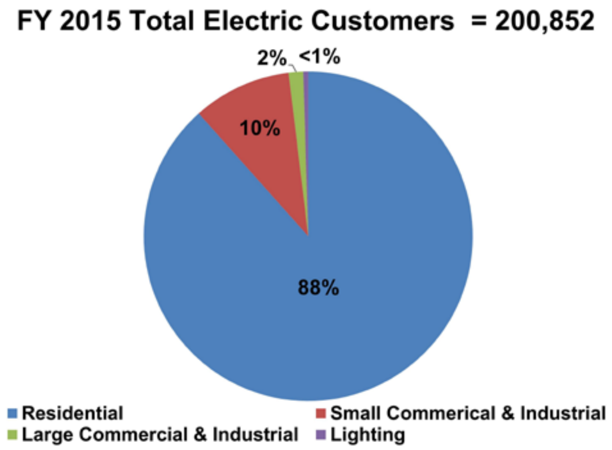
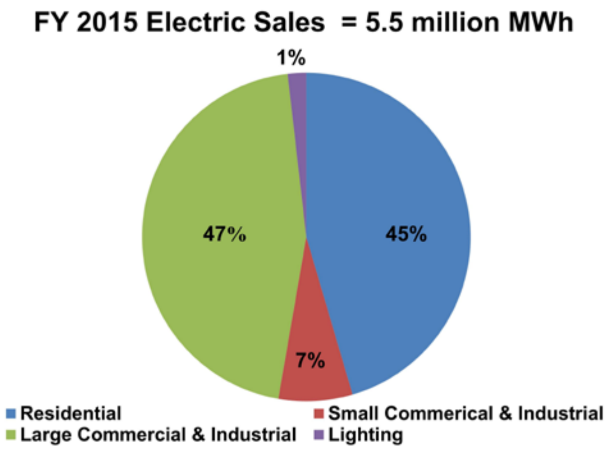
Fiscal Year 2015 Compared to Fiscal Year 2014

Margin on electric sales grew $5.2 million, reflecting higher revenues due to the October 2013 and July 2014 rate increases.

Operating revenue increased $5.4 million or 1 percent, reflecting the net result of additional revenue from KUB's one percent electric rate increase effective July 2014, and the flow through of TVA rate adjustments. Purchased power expense increased $0.2 million over last year. Power sales of 5.5 million MWh were consistent with the prior fiscal year.



FY 2015 Total Electric Customers = 200,852



FY 2015 Electric Sales = 5.5 million MWh

Residential customers represented 88 percent of total electric system customers and accounted for 45 percent of electric sales volumes for the year. Large commercial and industrial customers accounted for the largest portion of total sales volumes for the year, which was consistent with the prior year due to a steady customer base. KUB's ten largest electric customers accounted for 15.6 percent of KUB's billed volumes. Those ten customers represent five industrial and five commercial customers, including two governmental customers. Sales to Gerdau Ameristeel, KUB's largest industrial customer, were 295 MWh or 5.3 percent of total electric system sales.

Electric sales volumes in fiscal year 2015 were consistent with the previous fiscal year.

KUB has added 3,194 electric system customers over the past three years, representing annual growth of less than one percent.

Electric sales volumes have increased 1.5 percent since fiscal year 2013. Large commercial and industrial sales have increased 0.2 percent over the same period of time.

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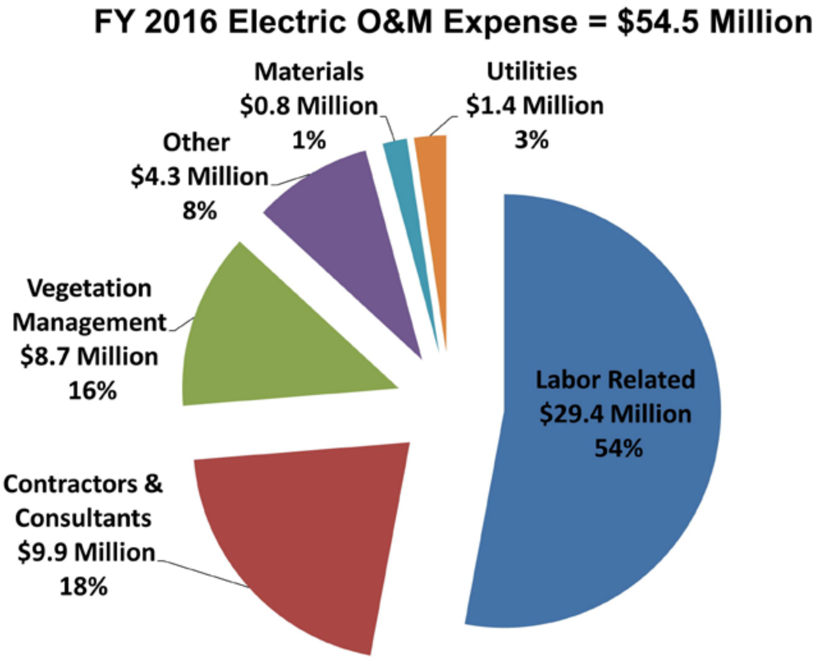
Operating Expenses

Fiscal Year 2016 Compared to Fiscal Year 2015

Operating expenses (excluding purchased power expense) increased 4.1 million, or 4.2 percent, compared to fiscal year 2015. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as distribution, customer service and administrative and general.

- Distribution expenses decreased $1.3 million or 3.9 percent, primarily from reduced outside contractor and consultant use.
- Customer service expenses were consistent with the prior year.
- Administrative and general expenses increased $1 million or 7.5 percent, primarily due to higher pension expense.

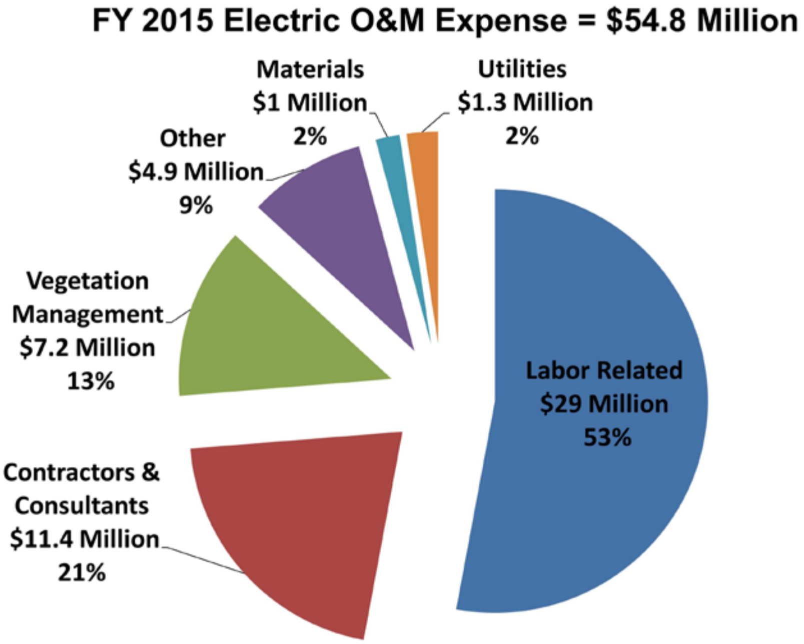

FY 2016 Electric O&M Expense = $54.5 Million

- Depreciation expense for fiscal year 2016 increased $3.6 million or 13.9 percent. This increase was primarily attributable to Century II initiatives, substation upgrades and the impairment of meters due to the Grid Modernization project that calls for accelerated depreciation of meters being replaced over the next four years as part of the project.
- Taxes and tax equivalents were $0.7 million higher than the prior fiscal year primarily due to increased plant in service levels.

Fiscal Year 2015 Compared to Fiscal Year 2014

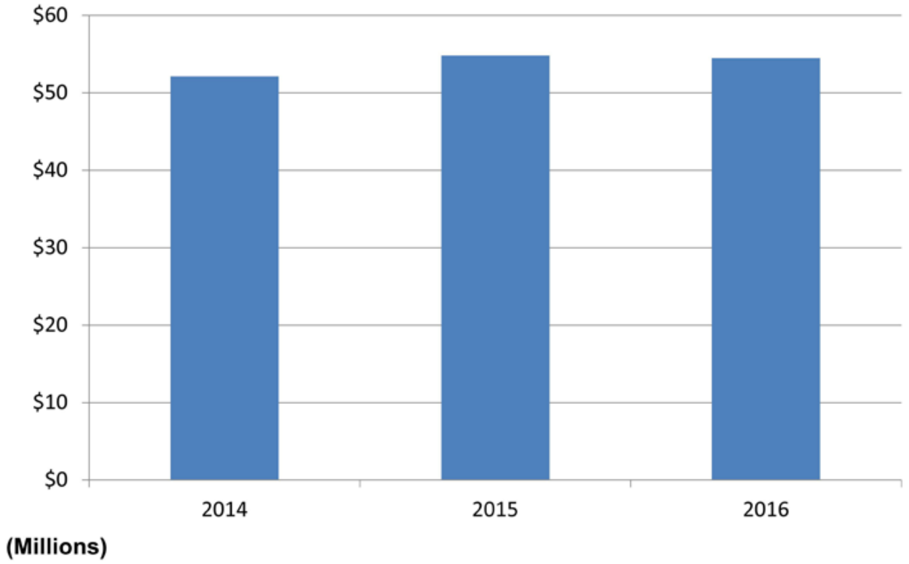
Operating expenses (excluding purchased power expense) increased $6.8 million, or 7.6 percent, compared to fiscal year 2014. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as distribution, customer service and administrative and general.

- Distribution expenses increased $1.5 million or 4.6 percent, primarily from electric system restoration expenses related to the February 2015 ice storm.
- Customer service expenses were up $0.7 million compared with the prior year, primarily due to increased computer software expenses and outside consultant expenses.
- Administrative and general expenses increased $0.5 million or 3.5 percent, primarily due to an increase in the Division's portion of shared costs.



- Depreciation expense for fiscal year 2015 increased $2.7 million or 11.6 percent. This increase was primarily attributable to Grid Modernization related software, meters and meter testing equipment and substation improvements.
- Taxes and tax equivalents were $1.4 million higher than the prior fiscal year due to an increase in tax equivalent payments to the City of Knoxville, Knox County, and other taxing jurisdictions. The City of Knoxville's property tax rate increased this year and higher plant in service levels contributed to the growth in tax equivalent payments.

Electric Division Operation & Maintenance Expense



Other Income and Expense

Fiscal Year 2016 Compared to Fiscal Year 2015

Interest income increased $0.2 million compared to the the prior fiscal year.

Interest expense increased $0.7 million or 8.3 percent, primarily due to the additional interest accrued on long-term revenue bonds issued in August 2014 and April 2015.

Other income (net) decreased $1.1 million, primarily due to the recognition of $1.6 million in non-operating income for future reimbursement of restoration expenses related to the February 2015 ice storm in fiscal year 2015.

The Division's capital contributions increased $0.2 million due to more donated assets compared to the prior fiscal year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Interest income was consistent with the prior fiscal year.

Interest expense increased $0.8 million or 10.5 percent, primarily due to the additional interest accrued on long-term revenue bonds issued in August 2014 and April 2015.

Other income (net) increased $1.8 million, primarily due to an accrual of $1.6 million in non-operating income for future reimbursement of restoration expenses related to the February 2015 ice storm.

The Division's capital contributions decreased $0.3 million due to less donated assets compared to the prior fiscal year.

Capital Assets

Capital Assets
As of June 30
(Net of Depreciation)

(in thousands of dollars)

	2016	2015	2014
Distribution Plant			
Services and Meters	$ 15,719	$ 17,964	$ 16,851
Electric Station Equipment	56,487	34,643	32,797
Poles, Towers and Fixtures	104,867	93,780	84,332
Overhead Conductors	84,937	79,199	73,663
Line Transformers	59,587	56,774	55,600
Other Accounts	113,141	108,888	106,894
Total Distribution Plant	$ 434,738	$ 391,248	$ 370,137
General Plant	29,590	27,312	27,288
Total Plant Assets	$ 464,328	$ 418,560	$ 397,425
Work In Progress	46,932	62,238	48,070
Total Net Plant	$ 511,260	$ 480,798	$ 445,495

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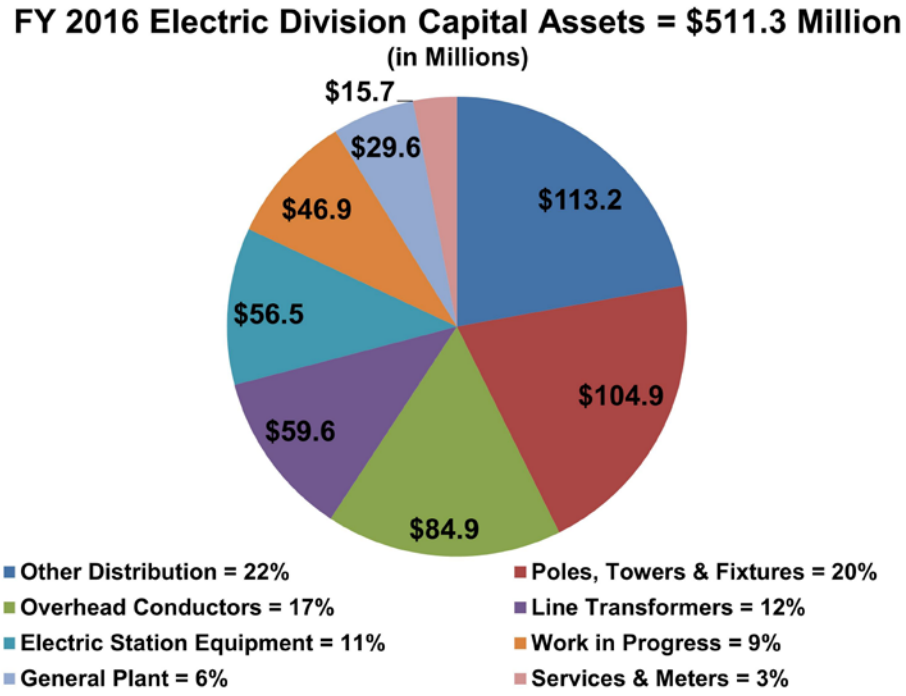
Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, the Division had $511.3 million invested in a variety of capital assets, as reflected in the schedule of capital assets, which represents a net increase (including additions, retirements, and depreciation) of $30.5 million or 6.3 percent over the end of the last fiscal year.

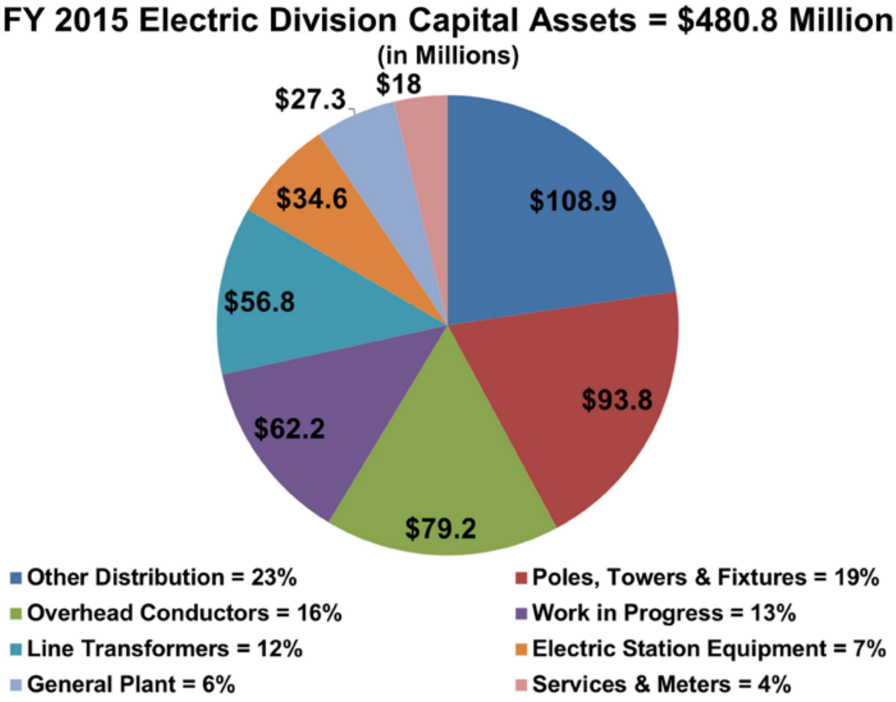


Major capital asset expenditures during the year were as follows:

- $25.1 million for electric distribution system improvements
- $7.7 million for pole replacements
- $7 million for installation of new electric services and the upgrade or replacement of existing services
- $4.9 million for Grid Modernization
- $4.1 million for upgrades to various information systems
- $1.8 million for the replacement and relocation of electric system assets to accommodate TDOT highway improvement projects
- $1.4 million for trucks and equipment
- $1.4 million for street lighting improvements

Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, the Division had $480.8 million invested in a variety of capital assets, as reflected in the schedule of capital assets, which represents a net increase (including additions, retirements, and depreciation) of $35.3 million or 7.9 percent over the end of the last fiscal year.



Major capital asset expenditures during the year were as follows:

- $28.7 million for various electric distribution improvements
- $6 million for pole replacements
- $5.9 million for installation of new electric services and the upgrade or replacement of existing services
- $4.5 million for new Cherokee Trail substation
- $4 million for information systems upgrades

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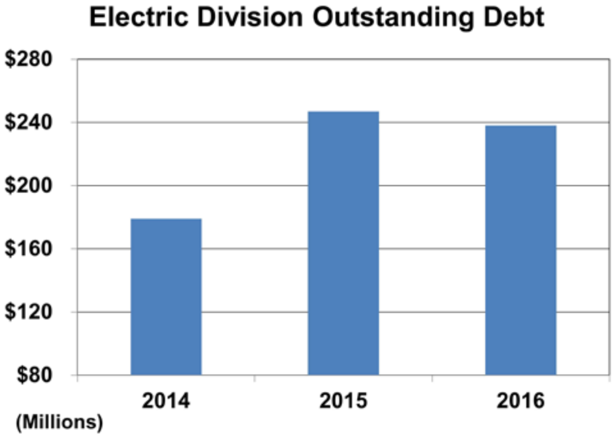
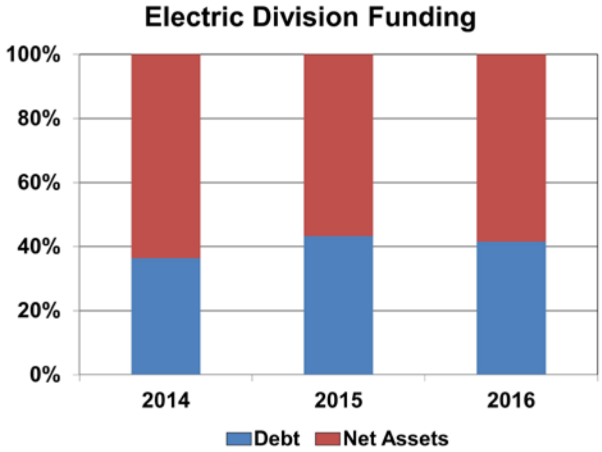
Debt Administration

The Division's outstanding debt was $238 million at June 30, 2016. The bonds are secured solely by revenues of the Electric Division. Debt as a percentage of the Division's capital structure was 41.6 percent in 2016, 43.3 percent in 2015 and 36.4 percent at the end of fiscal year 2014. KUB's Debt Management Policy limits the Division's debt ratio to 60 percent or less.

Outstanding Debt
As of June 30

(in thousands of dollars)	**2016**	**2015**	**2014**
Revenue bonds	$ 237,985	$ 247,055	$ 178,940
Total outstanding debt	$ 237,985	$ 247,055	$ 178,940





The Division will pay $119.2 million in principal payments over the next ten years, representing 50.1 percent of the outstanding bonds. KUB's Debt Management Policy requires that a minimum of 30 percent of electric debt principal be repaid over the next ten years.

Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, the Division had $238 million in outstanding debt (including the current portion of revenue bonds), compared to $247.1 million last year, a decrease of $9.1 million or 3.7 percent. The decrease is attributable to the scheduled repayment of bond debt. The Division's weighted average cost of debt at June 30, 2016 was 3.89 percent.

The Division's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2016, the Division's revenue bonds were rated AA+ by Standard & Poor's and Aa2 by Moody's Investors Service.

Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, the Division had $247.1 million in outstanding debt (including the current portion of revenue bonds), compared to $178.9 million last year, an increase of $68.2 million or 38.1 percent. The Division's weighted average cost of debt at June 30, 2015 was 3.89 percent.

The increase is attributable to the issuance of revenue bonds during the fiscal year of $40 million in August 2014 and $35 million in April 2015. The increase was partially offset by the scheduled repayment of bond debt.

In April 2015, KUB issued $28.6 million of revenue refunding bonds. The refunding of certain bonds at lower interest rates will provide debt service savings of $2.2 million over the life of the bonds.

The Division's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2015, the Division's revenue bonds were rated AA+ by Standard & Poor's and Aa2 by Moody's Investors Service.

Impacts on Future Financial Position

KUB anticipates adding 1,300 additional electric customers in fiscal year 2017.

In June 2014, the KUB Board adopted three years of rate increases for the Electric Division to help fund the ongoing Century II infrastructure programs. The first and second rate increases were effective July 2014 and July 2015. The remaining electric rate increase will be effective July 2016. Each rate increase will provide approximately $5.2 million in additional annual Electric Division revenue.

In April 2016, KUB management presented the fiscal year 2017 budget to the KUB Board of Commissioners that accommodates the projected level of capital investment for the fiscal year. Over the course of the next ten years KUB plans to spend approximately $108 million dollars on Grid Modernization, of which the Division's share is approximately $69.7 million. In July 2016, the four-year deployment of advanced meters began.

KUB sold $40 million in electric system revenue bonds in July 2016 for the purpose of funding electric system capital improvements. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.75 percent.

KUB long-term debt includes $23.9 million of Electric Division 2010 Build America Bonds (BABs). The BABs were sold on a taxable basis with the United States Treasury providing a rebate to KUB for a percentage of the interest cost. The interest rebates were subject to federal sequestration during the fiscal year and were reduced by 6.8 percent. Any future actions by Congress may also affect the anticipated rebates for future fiscal years.

GASB Statement No. 82, *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73* is effective for fiscal years beginning after June 15, 2016. GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* and GASB No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* are effective for periods beginning after June 15, 2017. KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

No other facts, decisions, or conditions are currently known which would have a significant impact on the Division's financial position or results of operations during fiscal year 2016.

Financial Contact

The Division's financial statements are designed to present users (citizens, customers, investors, and creditors) with a general overview of the Division's financial position and results of operations for the fiscal years ending June 30, 2016 and 2015. If you have questions about the statements or need additional financial information, contact KUB's Chief Financial Officer at 445 South Gay Street, Knoxville, Tennessee 37902.

Knoxville Utilities Board Electric Division
Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Assets and Deferred Outflows of Resources		
Current assets:		
Cash and cash equivalents	$ 34,791,786	$ 44,471,851
Short-term contingency fund investments	6,950,668	2,478,572
Other current assets	374,356	1,018,522
Accrued interest receivable	23,575	28,982
Accounts receivable, less allowance of uncollectible accounts of $594,022 in 2016 and $548,492 in 2015	53,968,641	58,078,711
Inventories	8,359,135	6,669,312
Prepaid expenses	684,835	649,770
Total current assets	105,152,996	113,395,720
Restricted assets:		
Electric bond fund	14,739,081	12,976,376
Other funds	10,281	21,071
Unused bond proceeds	-	20,519,850
Total restricted assets	14,749,362	33,517,297
Electric plant in service	859,020,997	789,895,908
Less accumulated depreciation	(394,693,191)	(371,336,117)
	464,327,806	418,559,791
Retirement in progress	1,071,534	568,243
Construction in progress	45,860,796	61,669,625
Net plant in service	511,260,136	480,797,659
Other assets:		
Net pension asset	-	2,890,382
Long-term contingency fund investments	24,934,746	27,725,842
TVA conservation program receivable	8,153,192	10,109,135
Under recovered purchased power cost	1,379,643	-
Other	2,640,401	2,720,927
Total other assets	37,107,982	43,446,286
Total assets	668,270,476	671,156,962
Deferred outflows of resources:		
Pension outflow	4,971,500	1,515,455
Unamortized bond refunding costs	3,572,465	3,895,275
Total deferred outflows of resources	8,543,965	5,410,730
Total assets and deferred outflows of resources	$ 676,814,441	$ 676,567,692

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Electric Division
Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Liabilities, Deferred Inflows, and Net Position		
Current liabilities:		
Current portion of revenue bonds	$ 10,110,000	$ 9,070,000
Sales tax collections payable	881,833	910,574
Accounts payable	40,653,044	42,598,006
Accrued expenses	19,309,494	17,658,067
Customer deposits plus accrued interest	11,735,639	11,084,371
Accrued interest on revenue bonds	4,628,956	3,906,251
Total current liabilities	87,318,966	85,227,269
Other liabilities:		
TVA conservation program	8,412,853	10,336,682
Accrued compensated absences	4,344,437	3,922,730
Customer advances for construction	1,262,889	1,280,962
Net pension liability	2,419,277	-
Over recovered purchased power cost	-	500,522
Other	159,005	220,247
Total other liabilities	16,598,461	16,261,143
Long-term debt:		
Electric revenue bonds	227,875,000	237,985,000
Unamortized premiums/discounts	9,728,282	10,345,326
Total long-term debt	237,603,282	248,330,326
Total liabilities	341,520,709	349,818,738
Deferred inflows of resources:		
Pension inflow	725,888	3,061,589
Total deferred inflows of resources	725,888	3,061,589
Total liabilities and deferred inflows of resources	342,246,597	352,880,327
Net position		
Net investment in capital assets	268,462,479	228,768,196
Restricted for:		
Debt service	10,110,125	9,070,125
Other	10,281	21,070
Unrestricted	55,984,959	85,827,974
Total net position	334,567,844	323,687,365
Total liabilities, deferred inflows, and net position	$ 676,814,441	$ 676,567,692

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Electric Division
Statements of Revenues, Expenses and Changes in Net Position
Years Ended June 30, 2016 and 2015

	2016	2015
Operating revenues	$ 521,369,202	$ 533,205,845
Operating expenses		
Purchased power	402,603,523	419,773,131
Distribution	33,062,072	34,407,647
Customer service	6,589,446	6,546,034
Administrative and general	14,856,340	13,821,576
Provision for depreciation	29,490,370	25,887,777
Taxes and tax equivalents	15,794,474	15,069,402
Total operating expenses	502,396,225	515,505,567
Operating income	18,972,977	17,700,278
Non-operating revenues (expenses)		
Contributions in aid of construction	1,632,730	1,551,247
Interest and dividend income	549,060	322,222
Interest expense	(9,257,913)	(8,548,826)
Amortization of debt costs	143,733	72,445
Write-down of plant for costs recovered through contributions	(1,632,730)	(1,551,247)
Other	294,226	1,512,078
Total non-operating revenues (expenses)	(8,270,894)	(6,642,081)
Change in net position before capital contributions	10,702,083	11,058,197
Capital contributions	178,396	11,611
Change in net position	10,880,479	11,069,808
Net position, beginning of year, as previously reported	323,687,365	312,984,264
Change in method of accounting for pension	-	(366,707)
Net position, beginning of year, as restated	323,687,365	312,617,557
Net position, end of year	$ 334,567,844	$ 323,687,365

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Electric Division
Statements of Cash Flows
Years Ended June 30, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Cash receipts from customers	$ 518,450,827	$ 526,079,765
Cash receipts from other operations	10,049,581	8,687,968
Cash payments to suppliers of goods or services	(439,418,959)	(460,073,403)
Cash payments to employees for services	(24,308,505)	(22,949,363)
Payment in lieu of taxes	(13,900,176)	(13,309,981)
Cash receipts from collections of TVA conservation loan program participants	3,067,056	3,046,131
Cash payments for TVA conservation loan program	(3,034,941)	(3,071,013)
Net cash provided by operating activities	50,904,883	38,410,104
Cash flows from capital and related financing activities:		
Net proceeds from bond issuance	-	77,011,071
Principal paid on revenue bonds and notes payable	(9,070,000)	(7,935,000)
(Increase) decrease in unused bond proceeds	20,519,850	(20,519,850)
Interest paid on revenue bonds and notes payable	(8,535,208)	(7,849,367)
Acquisition and construction of electric plant	(62,417,653)	(63,915,204)
Changes in electric bond fund, restricted	(1,762,705)	(1,392,547)
Customer advances for construction	33,177	525,582
Proceeds received on disposal of plant	241,531	-
Cash received from developers and individuals for capital purposes	1,632,730	1,551,247
Net cash used in capital and related financing activities	(59,358,278)	(22,524,068)
Cash flows from investing activities:		
Changes in deposit and investment accounts:		
Purchase of investment securities	(4,019,405)	(7,518,767)
Maturities of investment securities	2,476,455	4,354,758
Interest received	554,467	304,148
Other property and investments	(238,187)	(26,575)
Net cash provided by (used in) investing activities	(1,226,670)	(2,886,436)
Net increase (decrease) in cash and cash equivalents	(9,680,065)	12,999,600
Cash and cash equivalents, beginning of year	44,471,851	31,472,251
Cash and cash equivalents, end of year	34,791,786	$ 44,471,851
Reconciliation of operating income to net cash provided by operating activities		
Operating income	$ 18,972,977	$ 17,700,278
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	30,602,422	26,978,350
Changes in operating assets and liabilities:		
Accounts receivable	4,191,195	602,185
Inventories	(1,689,822)	853,013
Prepaid expenses	(35,065)	20,329
TVA conservation program receivable	1,874,818	523,680
Other assets	584,979	(1,782,164)
Sales tax collections payable	(28,741)	32,501
Accounts payable and accrued expenses	(353,913)	(2,711,061)
Unrecovered purchased power cost	(1,880,165)	(3,912,247)
TVA conservation program payable	(1,923,829)	(548,563)
Customer deposits plus accrued interest	651,269	558,360
Other liabilities	(61,242)	95,443
Net cash provided by operating activities	$ 50,904,883	$ 38,410,104
Noncash capital activities:		
Acquisition of plant assets through developer contributions	$ 178,396	$ 11,611

The accompanying notes are an integral part of these financial statements.

1. Description of Business

Knoxville Utilities Board (KUB), comprised of the Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions including setting rates. The Electric Division (Division) provides services to certain customers in Knox County and in seven surrounding counties in East Tennessee. The Division's accounts are maintained in conformity with the Uniform Division of Accounts of the Federal Energy Regulatory Commission (FERC) and the Governmental Accounting Standards Board (GASB), as applicable. The financial statements present only the Electric Division and do not purport to, and do not, present fairly the consolidated financial position of Knoxville Utilities Board at June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

2. Summary of Significant Accounting Policies

Basis of Accounting

In conformity with Generally Accepted Accounting Principles (GAAP), KUB follows the provisions of GASB Statement No. 34 (Statement No. 34), *Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* as amended by GASB Statement No. 63 (Statement No. 63), *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position.* Statement No. 34 established standards for external financial reporting for all state and local governmental entities. Under Statement No. 63, financial statements include deferred outflows of resources and deferred inflows of resources, in addition to assets and liabilities, and will report *net position* instead of net assets. In addition, KUB follows GASB Statement No. 62 (Statement No. 62), *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* as it relates to certain items for regulatory accounting. Regulatory accounting allows a regulated utility to defer a cost (a regulatory asset) or recognize an obligation (a regulatory liability) if it is probable that through the rate making process, there will be a corresponding increase or decrease in future revenues. Accordingly, KUB has recognized certain regulatory assets and regulatory liabilities in the accompanying Statements of Net Position.

The financial statements are prepared on the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred. The accounting and financial reporting treatment applied to the Division is determined by measurement focus. The transactions of the Division are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the Statement of Net Position. Net position (i.e., total assets and deferred outflows of resources net of total liabilities and deferred inflows of resources) is segregated into net investment in capital assets, restricted for capital activity and debt service, and unrestricted components.

Recently Adopted New Accounting Pronouncements

In February 2015, the Governmental Accounting Standards Board (GASB) issued Statement No. 72 (Statement No. 72), *Fair Value Measurement and Application.* Statement No. 72 is intended to provide guidance for determining a fair value measurement for financial reporting purposes and for applying fair value to certain investments and disclosures related to all fair value measurements.

In June 2015, the GASB issued GASB Statement No. 73 (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 Provision of GASB Statements 67 and 68.* The requirements of this Statement will improve financial reporting by establishing a single framework for the presentation of information about pensions and enhance comparability.

In June 2015, the GASB issued GASB Statement No. 76 (Statement No. 76), *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to simplify the hierarchy of generally accepted accounting principles (GAAP) used to prepare financial statements of state and local governmental entities. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments,* and amends Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, paragraphs 64, 74, and 82.

In December 2015, the GASB issued GASB Statement No. 79 (Statement No. 79), *Certain External Investment Pools and Pool Participants.* This statement establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes.

Statements No. 72, 73, 76, and 79 are effective for fiscal years beginning after June 15, 2015.

Electric Plant

Electric plant and other property are stated on the basis of original cost. The cost of current repairs and minor replacements is charged to operating expense. The cost of renewals and improvements is capitalized. The original cost of utility plant assets retired or otherwise disposed of and the cost of removal less salvage value is charged to accumulated depreciation. When other property is retired, the related asset and accumulated depreciation are removed from the accounts, and the gain or loss is included in the results of operations.

The provision for depreciation of electric plant in service is based on the estimated useful lives of the assets, which range from three to forty years, and is computed using the straight-line method. Pursuant to FERC, the caption "Provision for depreciation" in the Statements of Revenues, Expenses and Changes in Net Position does not include depreciation for transportation equipment of $1,112,052 in fiscal year 2016 and $1,090,573 in fiscal year 2015. Under regulatory accounting, interest costs are expensed as incurred with construction of plant assets.

Operating Revenue

Operating revenue consists primarily of charges for services provided by the principal operations of the KUB Electric Division. Operating revenue is recorded when the service is rendered, on a cycle basis, and includes an estimate of unbilled revenue. Revenues are reported net of bad debt expense of $1,342,705 in fiscal year 2016 and $1,987,329 in fiscal year 2015.

Non-operating Revenue

Non-operating revenue consists of revenues that are related to financing and investing types of activities and result from non-exchange transactions or ancillary activities.

Expense

When an expense is incurred for purposes for which there are both restricted and unrestricted net assets available, it is KUB’s policy to apply those expenses to restricted net assets to the extent such are available and then to unrestricted net assets.

Net Position

GASB Statement No. 63 requires the classification of net position into three components – net investment in capital assets; net position-restricted; and net position-unrestricted.

These classifications are defined as follows:

- Net investment in capital assets – This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt also should be included in this component of net position. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

- Net position-restricted – This component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported.

- Net position-unrestricted – This component of net position consists of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

Contributions in Aid of Construction and Capital Contributions

Contributions in aid of construction are cash collections from customers or others for a particular purpose, generally the construction of new facilities to serve new customers in excess of the investment KUB is willing to make for a particular incremental revenue source. KUB reduces the plant account balances to which contributions relate by the actual amount of the contribution and recognizes the contributions as non-operating revenue in accordance with Statement No. 62.

Capital contributions represent contributions of utility plant infrastructure constructed by developers and others in industrial parks and other developments, and transferred to KUB upon completion of construction and the initiation of utility service. In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, such contributions are recognized as revenues and capital assets upon receipt.

Inventories

Inventories, consisting of plant materials and operating supplies, are valued at the lower of average cost or replacement value.

Change in Method of Accounting for Pension

In June 2012, the Governmental Accounting Standards Board (GASB) issued Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, which revises existing standards of financial reporting for pensions. In addition, during November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, which requires deferred outflow of resources to be recognized for any contributions made subsequent to the measurement date of the beginning net pension liability. These standards were adopted by KUB in 2015 and resulted in a restatement of 2015 beginning net position of $763,975 (Division's share $366,707).

Pension Plan

KUB's employees are participants in the Knoxville Utilities Board Pension Plan as authorized by the Charter of the City of Knoxville §1107(J) (Note 10). KUB's policy is to fully fund the annual actuarially determined contributions. As required by GASB Statement No. 68, KUB measures net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30, 2016 and 2015 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 are based on a December 31, 2015 and 2014 measurement date, respectively.

Investments

Investments are carried at fair value as determined by quoted market prices at the reporting date.

Self-Insurance

KUB has established self-insurance programs covering portions of workers' compensation, employee health, environmental liability, general liability, property and casualty liability and automobile liability claims. A liability is accrued for claims as they are incurred. When applicable, claims in excess of the self-insured risk are covered by KUB's insurance carrier. Additionally, KUB provides certain lifetime health benefits to eligible retired employees under a self-insurance plan administered by a third party.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates are based on historical experience and various other assumptions that KUB believes are reasonable under the circumstances. However, future events are subject to change and the best estimates and judgments routinely require adjustment. Estimates are used for, but not limited to, inventory valuation, allowance for uncollectible accounts, depreciable lives of plant assets, unbilled revenue volumes, pension trust valuations, OPEB trust valuations, insurance liability reserves, and potential losses from contingencies and litigation. Actual results could differ from those estimates.

Restricted and Designated Assets

Certain assets are restricted by bond resolutions for the construction of utility plant and debt repayment. Certain additional assets are designated by management for contingency purposes and economic development.

Cash Equivalents

For purposes of the Statements of Cash Flows, KUB considers all unrestricted and undesignated highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

Deferred Outflows and Inflows of Resources

Deferred outflows of resources are items previously reported as assets related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. Deferred inflows of resources are items previously reported as liabilities related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. Deferred outflows of resources also include employer pension contributions made subsequent to the measurement date of the net pension liability and before the end of the employer's reporting period in accordance with Statement No. 71. Deferred inflows and deferred outflows also include the net difference between projected and actual earnings on pension plan

investments and differences between expected and actual experience in accordance with Statement No. 68.

Debt Premium/Discount

KUB records unamortized premium and discount on debt as a separate line item in the Long Term Debt section of the Financial Statements. Amortization of these amounts is recorded over the life of the applicable debt and is recorded as amortization expense.

Debt Issuance Costs

In accordance with regulatory accounting, KUB records debt issuance costs as an Other Asset. Amortization of these amounts is recorded over the life of the applicable debt and is recorded as amortization expense.

Deferred Gain/Loss on Refunding of Debt

KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. In accordance with FERC presentation, amortization of these amounts is recorded over the life of the applicable debt and is recorded as amortization expense.

Compensated Absences

KUB accrues a liability for earned but unpaid paid-time off (PTO) days.

TVA Conservation Program

KUB previously served as a fiscal intermediary for TVA whereby loans were made to KUB customers by TVA to be used in connection with TVA's Energy Right Residential Program. While KUB still holds existing loans, no loans were made through this program after October 31, 2015.

Subsequent Events

KUB has evaluated events and transactions through October 27, 2016, the date these financial statements were issued, for items that should potentially be recognized or disclosed. KUB sold $40 million in electric system revenue bonds in July 2016 for the purpose of funding electric system capital improvements in fiscal year 2017. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.75 percent.

Purchased Power Adjustment

In October 2002, the Board adopted a Purchased Power Adjustment (PPA) to address changes in wholesale power costs. The PPA was established in response to an amendment to KUB's power supply contract under which, among other things, TVA relinquished its regulatory authority over KUB retail electric rates. The PPA allows KUB to promptly adjust retail electric rates in response to wholesale rate changes or adjustments, thus ensuring that KUB will recover the costs incurred for purchased power. These changes in electric costs are reflected as adjustments to the base electric rates established by the Board. The rate-setting authority vested in the Board by the City Charter meets the "self-regulated" provisions of Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, and KUB meets the remaining criteria of Statement No. 62.

TVA implemented a fuel cost adjustment in October 2006 applied on a quarterly basis to wholesale power rates. TVA's quarterly fuel cost adjustment became a monthly fuel cost adjustment effective October 2009. KUB flows changes to wholesale power rates from TVA's fuel cost adjustment mechanism directly through to its retail electric rates via the PPA.

In April 2011, TVA modified its wholesale rate structure to demand and energy billing for its distributors. In response, KUB revised its PPA to include a deferred accounting component to ensure appropriate matching of revenue and expense and cost recovery. KUB will adjust its retail rates on an annual basis to flow any over or under recovery of wholesale power costs through to its customers via the PPA.

Under the PPA mechanism, KUB tracks the actual over/(under) recovered amount in the Over/(Under) Recovered Purchased Power Costs accounts. These accounts are rolled into the PPA rate adjustments thereby assuring that any over/(under) recovered amounts are promptly passed on to KUB's electric customers. The amount of over/(under) recovered cost was ($1,379,643) at June 30, 2016 and $500,522 at June 30, 2015.

Recently Issued Accounting Pronouncements

In June 2015, the GASB issued two related Statements that affect accounting and financial reporting by state and local governments for postemployment benefits other than pensions (OPEB). GASB Statement No. 74 (Statement No. 74), *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* addresses reporting by OPEB plans that administer benefits on behalf of governments. GASB Statement No. 75 (Statement No. 75), *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* addresses reporting by governments that provide OPEB to their employees. Statement No. 74 is effective for fiscal years beginning after June 15, 2016, and Statement No. 75 is effective for fiscal years beginning after June 15, 2017.

In March 2016, the GASB issued GASB Statement No. 82 (Statement No. 82), *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to the presentation of payroll-related measures in required supplementary information, the selection of assumptions and treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes and the classification of payments made by employers to satisfy employee contribution obligations. Statement No. 82 is effective for fiscal years beginning after June 15, 2016.

KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

3. Deposits and Investments

KUB follows the provisions of Statement No. 40 of the Governmental Accounting Standards Board, *Deposit and Investment Risk Disclosures an amendment of GASB Statement No. 3*. This Statement establishes and modifies disclosure requirements for state and local governments related to deposit and investment risks. KUB classifies its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*.

KUB's investment policy provides the framework for the administration and investment of cash deposits. The investment policy follows Tennessee State law and defines the parameters under which KUB funds should be invested. State law authorizes KUB to invest in obligations of the United States Treasury, its agencies and instrumentalities; certificates of deposit; repurchase agreements; money market funds; and the State Treasurer's Investment Pool.

Interest Rate Risk. KUB's primary investment objectives are to place investments in a manner to ensure the preservation of capital, remain sufficiently liquid to meet all operating requirements, and maximize yield of return. KUB minimizes its exposure to interest rate risk by adhering to Tennessee State law requirements for the investment of public funds. This includes limiting investments to those types described above and limiting maturity horizons. The maximum maturity is four years from the date of investment. KUB also limits its exposure by holding investments to maturity unless cash flow requirements dictate otherwise.

Credit Risk. KUB's investment policy, as required by state law, is to apply the prudent-person rule: Investments are made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable income to be derived, as well as the probable safety of their capital. KUB's Agency Bond investments are rated Aaa by Moody's Investors Service.

Custodial Credit Risk. KUB's investment policy limits exposure to custodial credit risk by restricting investments to a standard set forth by State law. All deposits in excess of federal depository insurance limits are collateralized with government securities held in KUB's name by a third-party custodian bank(s) acting as KUB's agent(s), or through the State of Tennessee's collateral pool. Financial institutions that participate in the collateral pool are subject to special assessment; therefore, the deposits are considered insured. A portion of KUB's investments are generally held in the State of Tennessee Local Government Investment Pool (LGIP). The LGIP is a part of the State Pooled Investment Fund and is sponsored by the State of Tennessee Treasury Department. Tennessee Code Annotated ¶9-4-701 *et seq.* authorizes local governments to invest in the LGIP. None of KUB's investments are exposed to custodial credit risk.

Classification of deposits and investments per Statement of Net Position:

		2016		**2015**
Current assets				
Cash and cash equivalents	$	34,791,786	$	44,471,851
Short-term contingency fund investments		6,950,668		2,478,572
Other assets				
Long-term contingency fund investments		24,844,482		27,664,712
Restricted assets				
Unused bond proceeds		-		20,519,583
Electric bond fund		14,739,081		12,976,376
Other funds		10,281		21,071
	$	81,336,298	$	108,132,165

The above amounts do not include accrued interest of $90,264 in fiscal year 2016 and $61,397 in fiscal year 2015. Interest income is recorded on an accrual basis.

Investments and maturities of KUB's deposits and investments as held by financial institutions as of June 30, 2016:

	Deposit and Investment Maturities (in Years)					
		Fair Value		**Less Than 1**		**1-5**
Supersweep NOW and Other Deposits	$	42,414,914	$	42,414,914	$	-
State Treasurer's Investment Pool		11,368,956		11,368,956		-
Agency Bonds		38,688,375		6,950,668		31,737,707
Certificates of Deposits		1,490,000		842,500		647,500
	$	93,962,245	$	61,577,038	$	32,385,207

KUB categorizes its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*. The hierarchy is based on the valuation inputs used to measure the fair value of an asset with a maturity at purchase greater than one year. 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.

KUB has the following recurring fair value measurements as of June 30, 2016:

- U.S. Agency bonds of $31,737,707, which have a maturity at purchase of greater than one year, are valued using quoted market prices (Level 1 inputs)
- Certificates of deposits of $647,500, which have a maturity at purchase of greater than one year, are valued at interest rates and yield curves observable at commonly quoted intervals (Level 2 inputs)

KUB measures investments with a maturity at purchase of one year or less at amortized cost, which is considered a fair value equivalent due to their nature. Investments in the State Treasurer's Investment Pool are measured at net asset value (NAV) per share.

4. Accounts Receivable

Accounts receivable consists of the following:

	2016	2015
Wholesale and retail customers		
Billed services	$ 30,849,655	$ 35,223,950
Unbilled services	20,416,060	19,677,853
Other	3,296,948	3,725,400
Allowance for uncollectible accounts	(594,022)	(548,492)
	$ 53,968,641	$ 58,078,711

5. Accounts Payable and Accruals

Accounts payable and accruals were composed of the following:

	2016	2015
Trade accounts	$ 40,653,044	$ 42,598,006
Salaries and wages	1,113,204	802,644
Advances on pole rental	2,135,320	1,147,346
Self-insurance liabilities	843,930	815,352
Other current liabilities	15,217,040	14,892,725
	$ 59,962,538	$ 60,256,073

6. Long-Term Obligations

Long-term debt consists of the following:

	Balance June 30, 2015	Additions	Payments	Defeased	Balance June 30, 2016	Amounts Due Within One Year
W-2005 - 3.0 - 4.5%	$ 31,350,000	$ -	$ 1,870,000	$ -	$ 29,480,000	$ 1,940,000
X-2006 - 4.0 - 5.0%	1,825,000	-	1,825,000	-	-	-
Y-2009 - 2.5 - 5.0%	6,875,000	-	1,600,000	-	5,275,000	1,675,000
Z-2010 - 1.45 - 6.35%	25,205,000	-	1,285,000	-	23,920,000	1,305,000
AA-2012 - 3.0 - 5.0%	34,840,000	-	990,000	-	33,850,000	2,540,000
BB-2012 - 3.0 - 4.0%	33,875,000	-	650,000	-	33,225,000	675,000
CC-2013 - 3.0 - 4.0%	9,535,000	-	50,000	-	9,485,000	450,000
DD-2014 - 2.0 - 4.0%	40,000,000	-	675,000	-	39,325,000	700,000
EE-2015 - 2.0 - 5.0%	28,550,000	-	125,000	-	28,425,000	150,000
FF-2015 - 2.0 - 5.0%	35,000,000	-	-	-	35,000,000	675,000
Total bonds	$ 247,055,000	$ -	$ 9,070,000	$ -	$ 237,985,000	$ 10,110,000
Unamortized Premium	10,345,326	-	617,044	-	9,728,282	-
Total long term debt	$ 257,400,326	$ -	$ 9,687,044	$ -	$ 247,713,282	$ 10,110,000

	Balance June 30, 2014	Additions	Payments	Defeased	Balance June 30, 2015	Amounts Due Within One Year
W-2005 - 3.0 - 4.5%	$ 33,140,000	$ -	$ 1,790,000	$ -	$ 31,350,000	$ 1,870,000
X-2006 - 4.0 - 5.0%	3,550,000	-	1,725,000	-	1,825,000	1,825,000
Y-2009 - 2.5 - 5.0%	35,900,000	-	1,525,000	27,500,000	6,875,000	1,600,000
Z-2010 - 1.45 - 6.35%	26,470,000	-	1,265,000	-	25,205,000	1,285,000
AA-2012 - 3.0 - 5.0%	35,795,000	-	955,000	-	34,840,000	990,000
BB-2012 - 3.0 - 4.0%	34,500,000	-	625,000	-	33,875,000	650,000
CC-2013 - 3.0 - 4.0%	9,585,000	-	50,000	-	9,535,000	50,000
DD-2014 - 2.0 - 4.0%	-	40,000,000	-	-	40,000,000	675,000
EE-2015 - 2.0 - 5.0%	-	28,550,000	-	-	28,550,000	125,000
FF-2015 - 2.0 - 5.0%	-	35,000,000	-	-	35,000,000	-
Total bonds	$ 178,940,000	$ 103,550,000	$ 7,935,000	$ 27,500,000	$ 247,055,000	$ 9,070,000
Unamortized Premium	5,779,555	5,617,592	411,968	639,853	10,345,326	-
Total long term debt	$ 184,719,555	$ 109,167,592	$ 8,346,968	$ 28,139,853	$ 257,400,326	$ 9,070,000

Debt service over remaining term of the debt is as follows:

Fiscal Year	**Principal**	**Total Interest**	**Grand Total**
2017	$ 10,110,000	$ 9,069,156	$ 19,179,156
2018	10,515,000	8,674,203	19,189,203
2019	10,955,000	8,237,917	19,192,917
2020	11,405,000	7,785,808	19,190,808
2021	11,850,000	7,299,291	19,149,291
2022-2026	64,365,000	28,535,403	92,900,403
2027-2031	51,750,000	16,522,440	68,272,440
2032-2036	20,960,000	10,255,208	31,215,208
2037-2041	24,775,000	6,357,063	31,132,063
2042-2046	21,300,000	1,722,875	23,022,875
Total	$ 237,985,000	$ 104,459,364	$ 342,444,364

The Division has pledged sufficient revenue, after deduction of all current operating expenses (exclusive of tax equivalents), to meet the revenue bonds principal and interest payments when due. Such bond requirements are being met through monthly deposits to the Electric Bond Fund as required by the bond covenants. As of June 30, 2016, these requirements had been satisfied.

During fiscal year 2006, KUB’s Electric Division issued Series W 2005 bonds in part to retire certain existing debt and to fund electric system capital improvements. Concurrent with the issuance of these bonds, KUB transferred funds to an irrevocable trust to pay a portion of the Series U 2001 bonds, as such amounts mature.

During fiscal year 2009, KUB’s Electric Division issued Series Y 2009 bonds to fund electric system capital improvements.

During fiscal year 2011, KUB’s Electric Division issued Series Z 2010 bonds to fund electric system capital improvements. The bonds were issued as federally taxable Build America Bonds with a 35 percent interest payment rebate to be received from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8 percent reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change.

During fiscal year 2012, KUB’s Electric Division issued Series AA 2012 bonds to retire a portion of outstanding Series V 2004 bonds.

During fiscal year 2013, KUB’s Electric Division issued Series BB 2012 bonds to fund electric system capital improvements. KUB’s Electric Division also issued Series CC 2013 bonds to retire a portion of outstanding Series X 2006 bonds.

During fiscal year 2015, KUB’s Electric Division issued Series EE 2015 bonds to retire a portion of outstanding Series Y 2009 bonds. KUB’s Electric Division also issued Series DD 2014 and Series FF 2015 to fund electric system capital improvements.

In prior years, certain revenue bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the liability for the defeased bonds, $27.5 million at June 30, 2016, and the trust account assets are not included in the financial statements.

Other liabilities consist of the following:

	Balance June 30, 2015	**Increase**	**Decrease**	**Balance June 30, 2016**
TVA conservation program	$ 10,336,682	$ 1,174,926	$ (3,098,755)	$ 8,412,853
Accrued compensated absences	3,922,730	8,454,477	(8,032,770)	4,344,437
Customer advances for construction	1,280,962	844,669	(862,742)	1,262,889
Other	220,247	96,950	(158,192)	159,005
	$ 15,760,621	$ 10,571,022	$ (12,152,459)	$ 14,179,184

7. Lease Commitments

KUB has non-cancelable operating lease commitments for office equipment, property, and vehicles, summarized for the following fiscal years:

2017	$ 136,464
2018	129,271
2019	75,847
2020	3,931
Total operating minimum lease payments	$ 345,513

8. Capital Assets

Capital asset activity was as follows:

	Balance June 30, 2015	Increase	Decrease	Balance June 30, 2016
Distribution Plant				
Services and Meters	$ 43,187,323	$ 824,211	$ (459,676)	$ 43,551,858
Electric Station Equipment	125,338,097	27,775,476	(880,406)	152,233,167
Poles, Towers and Fixtures	134,306,063	14,897,225	(1,142,671)	148,060,617
Overhead Conductors	128,493,727	9,622,259	(1,341,285)	136,774,701
Line Transformers	92,547,983	5,192,889	(897,720)	96,843,152
Other Accounts	186,274,579	9,899,201	(749,426)	195,424,354
Total Distribution Plant	$ 710,147,772	$ 68,211,261	$ (5,471,184)	$ 772,887,849
General Plant	79,748,136	7,631,550	(1,246,538)	86,133,148
Total Plant Assets	$ 789,895,908	$ 75,842,811	$ (6,717,722)	$ 859,020,997
Less Accumulated Depreciation	(371,336,117)	(30,854,964)	7,497,890	(394,693,191)
Net Plant Assets	$ 418,559,791	$ 44,987,847	$ 780,168	$ 464,327,806
Work In Progress	62,237,868	60,847,411	(76,152,949)	46,932,330
Total Net Plant	$ 480,797,659	$ 105,835,258	$ (75,372,781)	$ 511,260,136

	Balance June 30, 2014	Increase	Decrease	Balance June 30, 2015
Distribution Plant				
Services and Meters	$ 41,235,171	$ 2,176,349	$ (224,197)	$ 43,187,323
Electric Station Equipment	120,964,151	6,556,645	(2,182,699)	125,338,097
Poles, Towers and Fixtures	124,328,627	12,739,496	(2,762,060)	134,306,063
Overhead Conductors	120,168,100	9,163,450	(837,823)	128,493,727
Line Transformers	90,103,801	3,298,379	(854,197)	92,547,983
Other	178,735,315	8,051,035	(511,771)	186,274,579
Total Distribution Plant	$ 675,535,165	$ 41,985,354	$ (7,372,747)	$ 710,147,772
General Plant	75,386,810	5,489,993	(1,128,667)	79,748,136
Total Plant Assets	$ 750,921,975	$ 47,475,347	$ (8,501,414)	$ 789,895,908
Less Accumulated Depreciation	(353,496,822)	(26,741,232)	8,901,937	(371,336,117)
Net Plant Assets	$ 397,425,153	$ 20,734,115	$ 400,523	$ 418,559,791
Work In Progress	48,069,869	62,377,843	(48,209,844)	62,237,868
Total Net Plant	$ 445,495,022	$ 83,111,958	$ (47,809,321)	$ 480,797,659

9. Risk Management

KUB is exposed to various risks of loss related to active and retiree medical claims; injuries to workers; theft of, damage to, and destruction of assets; environmental damages; and natural disasters. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported.

These liabilities are included in accrued expenses in the Statement of Net Position. The liability is KUB's best estimate based on available information. At June 30, 2016 and June 30, 2015, the amount of these liabilities was $843,930 and $815,352, respectively, resulting from the following changes:

	2016	2015
Balance, beginning of year	$ 815,352	$ 738,983
Current year claims and changes in estimates	6,744,214	6,885,119
Claims payments	(6,715,636)	(6,808,750)
Balance, end of year	$ 843,930	$ 815,352

10. Pension Plan

Description of Plan

The Knoxville Utilities Board Pension Plan (the Plan) is a governmental plan as defined by the Employee Retirement Income Security Act of 1974 ("ERISA" or the "Act"), is not subject to any of the provisions of the Act, and was revised January 1, 2014 to include all prior approved amendments. The Plan is a single-employer contributory, defined benefit pension plan established by Knoxville Utilities Board ("KUB") Resolution No. 980 dated February 18, 1999, effective July 1, 1999, as authorized by the Charter of the City of Knoxville §1107(J). The Plan is designed to provide retirement, disability and death benefits to KUB employees. KUB administers the Plan through an Administrative Committee consisting of seven KUB employees that are appointed by KUB's President and CEO. Any amendments to the Plan involving costs not approved in the operating budget must be adopted by KUB's Board of Commissioners, upon recommendation by KUB's President and CEO. All other amendments to the Plan may be approved by KUB's President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The Plan issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017. For purposes of this disclosure, presentation is on a consolidated basis unless division's share is specified.

Effective January 1, 2011, KUB closed the Plan such that persons employed or re-employed by KUB on or after January 1, 2011, are not eligible to participate, but that eligible employees hired prior to January 1, 2011, who have not separated from service, shall continue as Participants and to accrue benefits under the Plan.

Participants in the Plan consisted of the following as of December 31:

	2015	**2014**
Inactive plan members:		
Terminated vested participants	39	40
Retirees and beneficiaries	628	627
Active plan members	692	725
Total	1,359	1,392

Retirement Benefits

The Plan provides three benefit arrangements for KUB participants, retirees, and beneficiaries.

The Plan provides pension benefits through the Career Equity Program ("CEP") for eligible employees hired on or after January 1, 1999, and for eligible former "City System Plan A" participants who elected CEP coverage as of July 1, 1999. The guaranteed pension benefit payable to a participant who has completed five or more years of service (or reached the normal retirement date, if earlier) upon termination of KUB employment shall be a lump sum equal to the participant's average compensation times their benefit percentage, as defined in the Plan document, or an annuity may be chosen by the participant.

In addition, the Plan provided retirement benefits through "Plan A" for former City System Plan A participants who elected not to participate in the CEP. Plan A is a closed plan and is not available to KUB employees hired after July 1, 1999. Plan A provides for early retirement benefits with 25 years of service and normal retirement benefits at age 62 or later. Benefits provided to Plan A participants include several different forms of monthly annuity payments.

The Plan also provides retirement benefits through "Plan B" for former "City System Plan B" participants. Plan B is a closed plan providing benefits to participants not covered by Social Security. Benefits provided to Plan B participants include several different forms of monthly annuity payments available to participants.

Effective January 1, 2012, KUB began to provide for additional monthly supplements, which will not be subject to cost of living adjustments, to certain former employees and surviving dependents of former employees who are eligible for and have elected coverage under the KUB retiree medical plan and are eligible for Medicare. This was done to address the loss of drug coverage under the KUB retiree medical plan and to assist such individuals in obtaining prescription drug coverage under Medicare Part D.

Contributions

Participation in Plan A requires employee contributions of 3 percent of the first $4,800 of annual earnings and 5 percent of annual earnings in excess of $4,800. Plan B participants may not make contributions to the Plan. KUB contributions are determined by the enrolled actuary of the Plan and equal the amount necessary to provide the benefits under the Plan determined by the application of accepted actuarial methods and assumptions. The method of funding shall be consistent with Plan objectives.

Plan Funding

KUB maintains a Funding Policy for the Plan in accordance with Tennessee State Law. The primary goal of the Policy is to document the method KUB has adopted to provide assurance that future KUB and employee contributions and current Plan assets will be sufficient to fund all benefits expected to be paid to current active, inactive and retired Plan participants and their beneficiaries. Per the Funding Policy, KUB fully funds its annual Actuarially Determined Contribution.

Investments

The Plan's investments are held by State Street Bank and Trust Company (the "Trustee"). The Plan's policy in regard to the allocation of invested assets is established by the Investment Committee and approved by the KUB Board of Commissioners and may only be amended by the KUB Board of Commissioners. It is the policy of the Investment Committee to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes. The following was the Plan's adopted asset allocation policy as of December 31, 2015:

Asset Class	Target Allocation
Domestic equity – large cap	20% - 50%
Domestic equity – mid cap	0% - 15%
Domestic equity – small cap	0% - 15%
Domestic equity - convertible securities	0% - 10%
Non-U.S. equity	0% - 20%
Real estate equity	0% - 10%
Fixed income – aggregate bonds	5% - 25%
Fixed income – long-term bonds	10% - 25%
Cash and deposits	0% - 5%

Contributions of $5,669,380 and $6,314,399 for 2014 and 2013, respectively, were made during KUB's fiscal years ending June 30, 2016 and 2015, respectively. Of these amounts, $2,721,302 and $3,030,911 are attributable to the Electric Division. The contribution was determined as part of the January 1, 2014 valuation using the Individual Entry Age Normal funding method. The objective under this method is to fund each participant's benefits under the Plan as payments which are level as a percentage of salary, starting on the original participation date (employment date) and continuing until the assumed retirement, termination, disability or death. The actuarial valuation for the Plan year ending December 31, 2015 resulted in an actuarially determined contribution of $4,816,913 for the fiscal year ending June 30, 2017, based on the Plan's current funding policy. The Electric Division's portion of this contribution is $2,312,118.

Subsequent to June 30, 2016, the actuarial valuation for the Plan year ending December 31, 2016 was completed. The actuarial valuation resulted in an actuarially determined contribution of $3,756,283 for the fiscal year ending June 30, 2018, based on the Plan's current funding policy. The Electric Division's portion of this contribution is $1,803,016. For the Plan year ending December 31, 2016, the Plan's actuarial funded ratio was 103.04 percent.

The actuarial valuations for the Plan years ending December 31, 2015 and 2016, which determine the actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Implementation of GASB 68

In fiscal year 2015, KUB adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*("GASB 68"), which requires measurement of the net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 will be based on the December 31, 2015 and 2014 measurement date, respectively. The Division's share of the net pension liability at June 30, 2016 is $2,419,277 and net pension asset at June 30, 2015 is $2,890,382.

GASB 68 requires certain disclosures related to the net pension liability of the Plan as disclosed below:

		2015		**2014**
Total pension liability	$	204,502,350	$	202,773,764
Plan fiduciary net position		199,462,190		(208,795,394)
Plan's net pension liability (asset)	$	5,040,160	$	(6,021,630)
Plan fiduciary net position as a percentage of the total pension liability		97.54%		102.97%

Changes in Net Pension Liability are as follows:

		Total Pension Liability (a)		Increase (Decrease) Plan Fiduciary Net Position (b)		Net Pension Liability (a) - (b)
Balances at December 31, 2014	$	202,773,764	$	208,795,394	$	(6,021,630)
Changes for the year:						
Service cost		4,157,062		-		4,157,062
Interest		14,812,784		-		14,812,784
Differences between Expected and Actual Experience		(1,890,334)		-		(1,890,334)
Changes of Assumptions		-		-		-
Contributions - employer		-		5,991,887		(5,991,887)
Contributions - rollovers		-		482,060		(482,060)
Contributions - member		-		5,486		(5,486)
Net investment income		-		(64,551)		64,551
Benefit payments		(15,350,926)		(15,350,926)		-
Administrative expense		-		(397,160)		397,160
Net changes		1,728,586		(9,333,204)		11,061,790
Balances at December 31, 2015	$	204,502,350	$	199,462,190	$	5,040,160

Actuarial Assumptions

The total pension liability was determined by an actuarial valuation as of December 31, 2015 and 2014, using the following actuarial assumptions, applied to all periods included in the measurement:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.80% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the January 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation
Inflation	2.8 percent

The actuarial assumptions used in the December 31, 2015 valuation were based on the results of an actuarial experience study for the period January 1, 2009 through December 31, 2013.

The long-term expected rate of return on Plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of Plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the Plan's target asset allocation as of December 31, 2015 and 2014 are summarized in the following table. The real rate of return reported for fixed income is for aggregate fixed income. The Plan has both aggregate and long duration fixed income.

	Long Term Expected Real Rate of Return	
Asset Class	**2015**	**2014**
Domestic equity	7.2%	6.0%
Non-U.S. equity	7.4%	7.0%
Real estate equity	6.5%	5.7%
Fixed income	3.7%	1.8%
Cash and deposits	2.6%	0.5%

Discount rate
The discount rate used to measure the total pension liability was 7.5 percent as of January 1, 2015 and 2014. The projection of cash flows used to determine the discount rate assumed that participant contributions will be made at the current contribution rate and that KUB contributions will be made at rates equal to the actuarially determined contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the net pension liability to changes in the discount rate
The following presents the net pension liability of the Plan as of December 31, 2015, calculated using the discount rate of 7.5 percent, as well as what the Plan's net pension liability would be if it were calculated using a discount rate that is one percent lower (6.5 percent) or one percent higher (8.5 percent) than the current rate:

	1% Decrease (6.5%)	**Current Discount Rate (7.5%)**	**1% Increase (8.5%)**
Plan's net pension liability	$ 17,128,897	$ 5,040,160	$ (5,963,331)

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

For the year ended June 30, 2015, KUB recognized pension expense of $2,749,905 (Division's share $1,319,954).

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in expense over the average expected remaining service life of all active and inactive members. As of the measurement date, this recognition period was 3.72 years. However, there were no experience gains or losses, and there were no assumption changes during the measurement year.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment gain of $7,972,887. $1,594,577 of that gain was recognized in the current year and an identical amount will be recognized in each of the next four years, resulting in a deferred inflow of resources of $6,378,310 (Division's share $3,061,589). The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over the next five years. In addition, KUB recorded a deferred outflow of resources of $3,157,199 (Division's share $1,515,455) at June 30, 2015 for employer contributions made between December 31, 2014 and June 30, 2015.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ -
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	-	6,378,310
Contributions subsequent to measurement date	3,157,199	-
Total	$ 3,157,199	$ 6,378,310

For the year ended June 30, 2016, KUB recognized pension expense of $4,665,035 (Division's share $2,239,217).

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in the pension expense over the average expected remaining service life of all active and inactive members, determined as of the beginning of the measurement period. As of December 31, 2014, this average was 5.00 years. During the measurement year, there were no assumption or benefit changes. There was an experience gain of $1,890,334 with $378,067 of that recognized in the current year and in each of the next four years.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment loss of $15,382,915. $3,076,583 of that loss was recognized in the current year and an identical amount will be recognized in each of the next four years. Unrecognized investment gains from prior periods were $6,378,310 of which $1,594,577 was recognized as a reduction in pension expense in the current year.

Experience gains this year created a deferred inflow of resources of $1,512,267 (Division's share $725,888). The combination of unrecognized investment losses this year along with unrecognized net investment gains from prior periods results in a deferred outflow of resources as of December 31, 2015 of $7,522,599 (Division's share $3,610,848). The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over future years. In addition, KUB recorded a deferred outflow of resources of $2,834,692 (Division's share $1,360,652) at June 30, 2016 for employer contributions made between December 31, 2015 and June 30, 2016.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ 1,512,267
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	7,522,599	-
Contributions subsequent to measurement date	2,834,692	-
Total	$ 10,357,291	$ 1,512,267

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

Year ended June 30:	
2017	$ 3,938,630
2018	1,103,939
2019	1,103,938
2020	2,698,517
Thereafter	-

11. Defined Contribution Plan

The KUB Asset Accumulation 401(k) Plan (the "401(k) Plan") is a defined contribution 401(k) employee retirement savings plan covering eligible KUB employees established by the KUB Board of Commissioners in accordance with the Charter of the City of Knoxville, Tennessee. The 401(k) Plan's assets are held in trust under an agreement between KUB and Fidelity Management Trust Company. Employees hired prior to January 1, 2011 may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. Employees hired on or after January 1, 2011 have an enhanced 401(k) due to the closure of the Defined Benefit Pension Plan. They may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. They also receive a nonelective KUB contribution of from 3 percent to 6 percent, depending on years of service, whether they contribute or not.

Matching contributions were previously remitted to the KUB Pension Plan (a separate defined benefit plan) in the name of the participant for employees hired prior to January 1, 2011. As of December 9, 2015, these Pension match assets moved from the KUB Pension Plan to the 401(k) Plan. Effective December 9, 2015, all matching contributions are remitted to the 401(k) Plan. The match and nonelective contributions for employees hired on or after January 1, 2011 are paid directly by KUB. KUB funded 401(k) matching contributions and nonelective contributions of $1,739,057 (Division's share $834,747) and $1,593,350 (Division's share $764,808), respectively, for the years ended June 30, 2016 and 2015.

12. Other Post-Employment Benefits (OPEB)

The Governmental Accounting Standards Board (GASB) established standards for the measurement, recognition, and reporting of other post-employment benefits (OPEB). OPEB includes post-employment benefits other than pension, which, for KUB, is presently limited to post-employment health care. GASB Statement No. 45 (Statement No. 45) requires the recognition of the accrued OPEB liability for the respective year, plus the disclosure of the total unfunded liability.

KUB currently provides post-employment health care benefits to 585 former employees and 593 covered dependents. The cost of coverage is shared with retirees and beneficiaries. KUB recognizes its share of the cost of post-employment health care benefits as an expense as claims are paid.

KUB amended its Group Health Plan in 1999, eliminating post-employment health care benefits for all employees hired on or after July 1, 1999. As of June 30, 2016, 356 active employees were eligible for individual and dependent coverage at separation. To qualify, the employee must meet the Rule of 80 (age plus years of service) with a minimum of 20 years of service, and be enrolled in medical coverage on their last day.

In May 2006, the State of Tennessee adopted Tennessee Code Annotated, Title 8, Chapter 50, Part 12 authorizing governmental entities to establish Trusts for the purpose of pre-funding their respective OPEB liabilities.

Although Statement No. 45 does not require pre-funding of the liability, KUB has determined that it is in the long-term economic interest of KUB and its ratepayers to establish a Trust to pre-fund KUB’s OPEB liability.

Knoxville Utilities Board Other Post-Employment Benefits Trust (the “Trust”) is a single-employer Other Post-Employment Benefits Plan established by the Knoxville Utilities Board (KUB) Board of Commissioners through Resolution No. 1168, as amended, dated October 18, 2007. The applicable documentation was submitted to the State Funding Board and, in December 2007, the State Funding Board approved the Trust. The Trust was also approved by the Internal Revenue Service in June 2008. KUB administers the Trust through a Board of Trustees consisting of seven KUB employees that are appointed by KUB’s President and CEO. Any amendments to the Trust involving costs not approved in the operating budget must be approved by KUB’s Board of Commissioners, upon recommendation by KUB’s President and CEO. All other amendments to the Trust may be approved by KUB’s President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The investment of all deposits to the Trust is governed by an Investment Policy, which was adopted by the KUB Board and approved by the State Funding Board.

KUB makes annual contributions to the Trust at an actuarially determined rate. Based on the date of retirement, certain retired plan members are required to contribute specified amounts monthly to maintain health insurance. Those who retired prior to July 1983 have no required monthly premiums for themselves or dependents. The retirees, or their surviving dependents, who retired between August 1983 and January 1998 are required to pay $250 per month for pre-Medicare family health insurance. For individuals who retired after January 1998, the required monthly premium for pre-Medicare health insurance is $250 for single coverage and $500 for family coverage. There is currently no premium for Medicare eligible retirees or dependents.

An actuarial valuation of KUB's Postretirement Benefit Plan was performed for the Trust as of January 1, 2014 for fiscal year June 30, 2015 and January 1, 2015 for fiscal year June 30, 2016. The following table presents the OPEB cost for the year, the amount contributed to the Trust, and changes in the net OPEB obligation for fiscal year ending June 30:

	2016	**2015**
a) Net OPEB Obligation/(Asset) at beginning of fiscal year	$ (174,410)	$ (177,322)
b) Annual Required Contribution (ARC)	953,221	3,497,372
c) Interest on Net OPEB Obligation/(Asset)	(13,081)	(14,186)
d) Adjustment to ARC	(16,427)	(17,098)
e) Annual OPEB Cost **(b+c-d)**	956,567	3,500,284
f) Employer Contributions	953,221	3,497,372
g) Net OPEB Obligation/(Asset) at end of fiscal year **(a+e-f)**	$ (171,064)	$ (174,410)

KUB's annual OPEB cost, the percentage of annual OPEB cost contributed to the Trust, and the net OPEB obligation for fiscal year 2016 and the two preceding years were as follows:

Schedule of Employer Contributions

Actuarial Valuation Date	**Employer Fiscal Year**	**Annual Required Contribution**	**Fiscal Year Actual Contribution**	**Percentage Contributed**	**Net OPEB Obligation**
1/1/2012	6/30/2014	3,327,412	4,057,091	121.93%	(177,322)
1/1/2013	6/30/2015	3,497,372	3,497,372	100.00%	(174,410)
1/1/2014	6/30/2016	953,221	953,221	100.00%	(171,064)

Total contributions to the OPEB Trust for the fiscal year ended June 30, 2016 were $953,221 (Division's share $457,546). The contribution to the Trust was consistent with the annual required contribution, as determined by the Postretirement Benefit Plan's actuarial valuation as of January 1, 2014, which was $953,221 (Division's share $457,546). As of June 30, 2016, the employer's OPEB obligation has been exceeded by $171,064 (Division's share $82,111).

The annual required contribution for the fiscal year ending June 30, 2017, as determined by the Plan's actuarial valuation as of January 1, 2015 is $620,015 (Division's share $297,607).

The actuarial valuation for the Plan as of January 1, 2016 has been completed. The valuation determined that the Plan's actuarial accrued liability was $45,118,624 (Division's share $21,656,940). The actuarial value of the Plan's assets was $48,510,796 (Division's share $23,285,182). As a result, the Plan's unfunded actuarial accrued liability was ($3,392,172) (Division's share ($1,628,243)). The Plan's actuarial funded ratio was 108 percent. Due to the future implementation of GASB 75, the contributions made for fiscal year ending June 30, 2018 will be the actuarially determined contribution instead of the annual required contribution and the actuarial cost method used to determine the contributions will change from the projected unit credit cost method to the entry age normal cost method. The actuarially determined contribution for fiscal year ending June 30, 2018 will be zero. See Required Supplementary Information for OPEB Schedule of Funding Progress.

The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution and actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

The required schedule of funding progress immediately following the notes to the financial statements presents multi-year trend information about whether the actuarial value of Trust assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point.

Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

Identification of actuarial methods and significant assumptions used to determine the annual required contribution for the fiscal year ending June 30, 2016:

I. Actuarial cost method	Projected unit credit cost method
II. Actuarial value of assets	Smoothed market value with phase-in method using a smoothing period of 5 years
III. Investment return	7.5%, based on the expected portfolio return
Projected salary increases	N/A
Healthcare cost Trend:	
Medicare	2014 - 2030+, ranging from 4.5% to 7.45%
Non-Medicare	2014 - 2030+, ranging from 4.5% to 8.75%
IV. Amortization method	Level dollar closed (30-year)
Remaining amortization period	22 years

The Trust issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement Division, P.O. Box 59017, Knoxville, TN 37950-9017.

13. Related Party Transactions

The Division, in the normal course of operations, is involved in transactions with the City of Knoxville and with other divisions of KUB. Such transactions for the years ended June 30, 2016 and 2015 are summarized as follows:

	2016	**2015**
City of Knoxville		
Amounts billed by the Division for utilities and related services	$ 8,675,231	$ 8,591,649
Payments by the Division in lieu of property tax	6,979,195	6,764,881
Payments by the Division for services provided	14,497	75,417
Other divisions of KUB		
Amounts billed to other divisions for utilities and related services provided	5,255,288	5,530,344
Interdivisional rental expense	-	-
Interdivisional rental income	769,151	786,190
Amounts billed to the Division by other divisions for utilities services provided	197,577	212,051

With respect to these transactions, accounts receivable from the City of Knoxville included in the balance sheet at year end were:

	2016	**2015**
Accounts receivable	$ 541,608	$ 539,053

14. Other Commitments and Contingencies

In the normal course of business, there are various lawsuits pending against KUB. Management has reviewed these lawsuits with counsel, who is vigorously defending KUB's position and is of the opinion that the ultimate disposition of these matters will not have a material adverse effect on KUB's financial position, results of operations or cash flows.

Knoxville Utilities Board Electric Division
Required Supplementary Information – Schedule of Funding Progress
June 30, 2016
(Unaudited)

Other Post-Employment Benefits (OPEB)

	Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a)/(b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b)-(a)]/(c)
	January 1, 2008	$ -	$ 108,329,141	$ 108,329,141	0%	$ 31,234,509	346.8%
	January 1, 2009	14,593,487	100,726,738	86,133,251	14%	31,846,091	270.5%
	January 1, 2010	21,275,643	58,475,364	37,199,721	36%	30,069,028	123.7%
	January 1, 2011	40,749,815	64,289,254	23,539,439	63%	28,878,791	81.5%
	January 1, 2012	37,907,357	61,603,466	23,696,109	62%	28,269,123	83.8%
	January 1, 2013	38,571,803	63,341,531	24,769,728	61%	27,566,340	89.9%
	January 1, 2014	43,409,955	46,889,808	3,479,853	93%	26,724,154	13.0%
*	January 1, 2015	47,705,478	47,745,640	40,162	100%	25,816,884	0.2%
*	January 1, 2016	48,510,796	45,118,624	(3,392,172)	108%	25,243,127	(13.4%)

***** The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Knoxville Utilities Board Electric Division
Required Supplementary Information – Schedule of Changes in Net Pension Liability and Related Ratios
June 30, 2016
(Unaudited)

	Year ended December 31	
	2015	**2014**
Total pension liability		
Service cost	$ 4,157,062	$ 4,092,808
Interest	14,812,784	14,698,657
Differences between expected and actual experience	(1,890,334)	-
Benefit payments, including refunds of member contributions	(15,350,926)	(15,533,167)
Net change in total pension liability	1,728,586	3,258,298
Total pension liability - beginning	202,773,764	199,515,466
Total pension liability - ending (a)	$ 204,502,350	$ 202,773,764
Plan fiduciary net position		
Contributions - employer	$ 5,991,887	$ 5,908,541
Contributions - participants	487,546	475,854
Net investment income	(95,430)	22,292,369
Other additions	30,879	29,733
Benefit payments, including refunds of member contributions	(15,274,926)	(15,405,167)
Administrative expense	(397,160)	(378,085)
Death benefits	(76,000)	(128,000)
Net change in plan fiduciary net position**	(9,333,204)	12,795,245
Plan fiduciary net position - beginning**	208,795,394	196,000,149
Plan fiduciary net position - ending (b)**	$ 199,462,190	$ 208,795,394
Plan's net pension liability - ending (a) - (b)	$ 5,040,160	$ (6,021,630)
Plan fiduciary net position as a percentage of the total pension liability	97.54%	102.97%
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Plan's net pension liability as a percentage of covered-employee payroll	9.95%	(11.98%)

Notes to Schedule:

* Information not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented in 2014.

** Excludes amounts related to 401(k) matching contributions.

Knoxville Utilities Board Electric Division
Required Supplementary Information – Schedule of Employer Pension Contributions
June 30, 2016
(Unaudited)

	Year ended December 31 2015	 2014
Annual required contribution	$ 5,991,887	$ 5,908,541
Contribution in relation to the annual required contribution	5,991,887	5,908,541
Contribution deficiency	$ -	$ -
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Contributions as a percentage of covered-employee payroll	11.82%	11.76%

Notes to Schedule:

Valuation Dates:	January 1, 2013 and January 1, 2014
Timing:	Actuarially determined contributions for a plan year are based upon 50% of the amounts determined at the actuarial valuations for each of the two prior plan years.

Key methods and assumptions used to determine contribution rates:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014.
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.8% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the Janaury 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation.
Inflation:	2.8 percent

* Schedule of Employer Contribution information is not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented 2014.

Knoxville Utilities Board Electric Division

Supplemental Information –

Schedule of Expenditures of Federal Awards and State Financial Assistance

June 30, 2016 Schedule 1

KUB was awarded a grant from Tennessee Emergency Management Agency (as a flow through from FEMA) for reimbursement for costs related to storms in 2015. The schedule below shows the expenditures for the current fiscal year.

Program Name	Federal/State Agency	CFDA Number	Contract Number	Expenditures
U.S. Department of Homeland Security	Tennessee Emergency Management	97.036	34101-06616	$ 1,325,524
		Total Program 97.036		$ 1,325,524
		Total Federal Awards		$ 1,325,524

NOTE 1 - BASIS OF PRESENTATION

The Schedule of Expenditures of Federal Awards and State Financial Assistance includes the federal award related grant activity of Knoxville Utilities Board and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Knoxville Utilities Board Electric Division
Supplemental Information – Schedule of Findings and Questioned Costs
June 30, 2016 Schedule 2

Section I -- Summary of Auditors' Results

Financial Statements

Type of auditors' report issued:	Unmodified
Internal control over financial reporting: Material weakness(es) identified?	None reported
Significant deficiency(s) identified not considered to be material weaknesses?	None reported
Noncompliance material to financial statements:	None reported

Federal Awards

Internal control over major programs: Material weakness(es) identified?	None reported
Significant deficiency(s) identified not considered to be material weaknesses?	None reported
Type of auditors' report issued on compliance for major programs:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with Title 2 U.S. Code of Federal Regulations Part 200?	None reported

Identification of major programs:

CFDA	Name of Program
97.036	Tennessee Emergency Management

Dollar threshold used to distinguish between Type A and Type B programs:	$750,000
Auditee qualified as low-risk auditee?	No

Section II -- Financial Statement Findings

None reported.

Section III -- Federal Award Findings and Questioned Costs

None reported.

Section IV – Summary Schedule of Prior Year Audit Findings

Not applicable as there were no prior year findings reported.

Section V – Corrective Action Plan

Not applicable as there were no current year findings reported.

Knoxville Utilities Board Electric Division
Supplemental Information - Schedule of Insurance in Force
June 30, 2016
(Unaudited) Schedule 3

Insurance coverage is for KUB as a consolidated entity.

Crime
Covers losses resulting from employee dishonesty, robbery, burglary, and computer fraud. Limits of coverage - $5,000,000; $250,000 retention.

Directors' and Officers' Liability Insurance
Covers KUB personnel appropriately authorized to make decisions on behalf of KUB (including but not limited to Commissioners, President and CEO, Senior Vice Presidents, Vice Presidents, and Directors) for wrongful acts. Limits of coverage - $20,000,000; $1,000,000 corporate deductible, $0 individual deductible.

Employment Practices Liability
Coverage for costs related to actual or alleged employment practices violations for amounts exceeding specified amount ($500,000). Limits of coverage - $10,000,000.

Fiduciary
Covers losses resulting from wrongful acts related to KUB's Pension, 401(k), and OPEB Trust funds. Limits of coverage - $10,000,000; $150,000 deductible.

Pollution Legal Liability
New conditions coverage for losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - $20,000,000.

Property Insurance
This coverage provides protection of KUB's property for fire, extended coverage, vandalism and malicious mischief, and coverage on boilers and machinery. Also included are flood and earthquake damage and mechanical failure. Limits of coverage - $250,000,000 per occurrence (subject to certain sublimits); $2,500,000 deductible per occurrence.

Travel Accident
Covers losses related to employees' business travel. Limits of coverage - $1,500,000 aggregate.

Excess Insurance for General Liability
As a government entity, KUB's liability is limited under the Tennessee Governmental Tort Liability Act (TCA §29-20-403). KUB is self-insured for up to the first $700,000 of any accident and has insurance of $1,000,000 above this retention.

Excess Insurance for Workers' Compensation
Covers all losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - Statutory; stop loss coverage applies for aggregate losses over $5,000,000.

Employee Health Plan Stop Loss Coverage
KUB's employee health plan is self-funded. KUB has purchased stop loss insurance, which covers KUB's exposure to annual expenses in excess of $400,000 per individual participant.

Knoxville Utilities Board Electric Division

Supplemental Information - Schedule of Debt Maturities by Fiscal Year

June 30, 2016

(Unaudited)

Schedule 4

Continued on Next Page

	W-2005		Y-2009		Z-2010			AA-2012	
FY	Principal	Interest	Principal	Interest	Principal	Interest	Rebate*	Principal	Interest
16-17	1,940,000	1,218,606	1,675,000	151,625	1,305,000	1,225,919	429,072	2,540,000	1,353,963
17-18	2,015,000	1,139,506	1,750,000	100,250	1,330,000	1,180,440	413,154	2,670,000	1,223,713
18-19	2,095,000	1,057,306	1,850,000	37,000	1,355,000	1,128,729	395,055	2,805,000	1,086,838
19-20	2,185,000	970,341			1,390,000	1,070,710	374,749	2,955,000	942,838
20-21	2,275,000	878,354			1,425,000	1,007,355	352,575	3,100,000	791,463
21-22	2,370,000	781,069			1,470,000	939,300	328,756	3,270,000	632,213
22-23	2,470,000	678,219			1,515,000	866,145	303,151	3,415,000	482,163
23-24	2,580,000	569,294			1,560,000	787,710	275,698	3,540,000	360,763
24-25	2,695,000	453,903			1,615,000	703,545	246,241	3,640,000	253,063
25-26	2,820,000	333,263			1,670,000	613,180	214,614	1,105,000	180,506
26-27	2,950,000	205,201			1,725,000	516,395	180,739	1,140,000	144,025
27-28	3,085,000	69,413			1,785,000	413,266	144,643	1,180,000	106,325
28-29					1,850,000	303,738	106,308	1,225,000	65,713
29-30					1,925,000	187,156	65,505	1,265,000	22,138
30-31					2,000,000	63,500	22,225		
31-32									
32-33									
33-34									
34-35									
35-36									
36-37									
37-38									
38-39									
39-40									
40-41									
41-42									
42-43									
43-44									
44-45									
45-46									
Total	$ 29,480,000	$ 8,354,475	$ 5,275,000	$ 288,875	$ 23,920,000	$ 11,007,088	$ 3,852,485	$ 33,850,000	$ 7,645,724

*Series Z-2010 bonds were issued as federally taxable Build America Bonds. KUB is scheduled to receive a 35 percent interest rebate payment from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8% reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change.

Knoxville Utilities Board Electric Division

Supplemental Information - Schedule of Debt Maturities by Fiscal Year

June 30, 2016

(Unaudited)

Schedule 4

Continued from Previous Page

	BB-2012		CC-2013		DD-2014		EE-2015		FF-2015		Total		Grand Total (P + I)
FY	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	
16-17	675,000	1,017,625	450,000	305,099	700,000	1,354,369	150,000	977,450	675,000	1,464,500	10,110,000	9,069,156	19,179,156
17-18	700,000	997,000	475,000	286,600	725,000	1,332,994	150,000	969,950	700,000	1,443,750	10,515,000	8,674,203	19,189,203
18-19	725,000	972,000	475,000	267,600	775,000	1,314,369	150,000	962,450	725,000	1,411,625	10,955,000	8,237,917	19,192,917
19-20	750,000	942,500	500,000	248,100	800,000	1,298,619	2,075,000	937,950	750,000	1,374,750	11,405,000	7,785,808	19,190,808
20-21	800,000	911,500	515,000	227,800	825,000	1,282,369	2,135,000	863,825	775,000	1,336,625	11,850,000	7,299,291	19,149,291
21-22	825,000	879,000	540,000	206,700	875,000	1,256,619	2,235,000	788,100	800,000	1,297,250	12,385,000	6,780,251	19,165,251
22-23	875,000	849,375	560,000	187,497	900,000	1,221,119	2,300,000	708,250	825,000	1,256,625	12,860,000	6,249,393	19,109,393
23-24	900,000	822,750	575,000	170,475	950,000	1,184,119	2,415,000	590,375	850,000	1,214,750	13,370,000	5,700,236	19,070,236
24-25	950,000	795,000	590,000	153,000	975,000	1,145,619	2,555,000	478,900	900,000	1,171,000	13,920,000	5,154,030	19,074,030
25-26	975,000	766,125	640,000	134,550	1,025,000	1,110,744	2,670,000	387,750	925,000	1,125,375	11,830,000	4,651,493	16,481,493
26-27	1,025,000	736,125	650,000	115,200	1,075,000	1,079,244	2,735,000	306,675	950,000	1,078,500	12,250,000	4,181,365	16,431,365
27-28	1,075,000	704,625	670,000	95,400	1,125,000	1,046,244	2,850,000	222,900	975,000	1,030,375	12,745,000	3,688,548	16,433,548
28-29	1,125,000	671,625	675,000	75,225	1,175,000	1,011,744	2,955,000	135,825	1,025,000	985,500	10,030,000	3,249,370	13,279,370
29-30	1,175,000	637,125	710,000	54,450	1,225,000	975,744	3,050,000	45,750	1,050,000	944,000	10,400,000	2,866,363	13,266,363
30-31	1,225,000	601,125	725,000	32,925	1,275,000	938,244			1,100,000	901,000	6,325,000	2,536,794	8,861,794
31-32	1,275,000	563,625	735,000	11,023	1,325,000	897,919			1,125,000	856,500	4,460,000	2,329,067	6,789,067
32-33	1,325,000	524,625			1,375,000	854,375			1,175,000	810,500	3,875,000	2,189,500	6,064,500
33-34	1,375,000	484,125			1,450,000	808,469			1,225,000	762,500	4,050,000	2,055,094	6,105,094
34-35	1,450,000	441,750			1,500,000	759,594			1,250,000	713,000	4,200,000	1,914,344	6,114,344
35-36	1,500,000	397,500			1,575,000	707,703			1,300,000	662,000	4,375,000	1,767,203	6,142,203
36-37	1,575,000	351,375			1,650,000	652,250			1,350,000	609,000	4,575,000	1,612,625	6,187,625
37-38	1,625,000	303,375			1,725,000	593,188			1,400,000	554,000	4,750,000	1,450,563	6,200,563
38-39	1,700,000	253,500			1,800,000	531,500			1,450,000	497,000	4,950,000	1,282,000	6,232,000
39-40	1,775,000	201,375			1,875,000	462,500			1,500,000	438,000	5,150,000	1,101,875	6,251,875
40-41	1,850,000	147,000			1,950,000	386,000			1,550,000	377,000	5,350,000	910,000	6,260,000
41-42	1,950,000	90,000			2,025,000	306,500			1,600,000	314,000	5,575,000	710,500	6,285,500
42-43	2,025,000	30,375			2,125,000	223,500			1,675,000	248,500	5,825,000	502,375	6,327,375
43-44					2,225,000	136,500			1,725,000	180,500	3,950,000	317,000	4,267,000
44-45					2,300,000	46,000			1,800,000	110,000	4,100,000	156,000	4,256,000
45-46									1,850,000	37,000	1,850,000	37,000	1,887,000
Total	$ 33,225,000	$ 16,092,125	$ 9,485,000	$ 2,571,644	$ 39,325,000	$ 24,918,158	$ 28,425,000	$ 8,376,150	$ 35,000,000	$ 25,205,125	$ 237,985,000	$ 104,459,364	$ 342,444,364

Knoxville Utilities Board Electric Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)

Schedule 5

Rate Class		Base Charge			Number of Customers
Residential		Customer Charge:	$16.60 per month, less Hydro Allocation Credit: $1.60 per month.		179,100
		Energy Charge:	Summer Period	8.688 cents per kWh per month.	
			Winter Period	8.647 cents per kWh per month.	
			Transition Period	8.647 cents per kWh per month.	
Commercial/ Industrial	**A. 1.**	If (a) the higher of (i) the customer's currently effective contract demand, if any, or (ii) its highest billing demand during the latest 12-month period is not more than 50 kWh, and (b) customer's monthly energy takings for any month during such period do not exceed 15,000 kWh:			19,454
		Customer Charge:	$22.00 per delivery point per month.		
		Energy Charge:	Summer Period	10.112 cents per kWh.	
			Winter Period	10.071 cents per kWh.	
			Transition Period	10.071 cents per kWh.	
	2.	If (a) the higher of (i) the customer's currently effective contract demand or (ii) its highest billing demand during the latest 12-month period is greater than 50 kW but not more than 1,000 kW, or (b) if the customer's billing demand is less than 50 kW and its energy takings for any month during such period exceed 15,000 kWh:			2,799
		Customer Charge:	$60.00 per delivery point per month.		
		Demand Charge:	First 50 kW of billing demand per month, no demand charge.		
			Excess over 50 kW of billing demand per month, at		
			Summer Period	$13.92 per kW.	
			Winter Period	$13.13 per kW.	
			Transition Period	$13.13 per kW.	
		Energy Charge:	Summer Period	First 15,000 kWh per month at 11.487 cents per kWh Additional kWh per month at 5.713 cents per kWh.	
			Winter Period	First 15,000 kWh per month at 11.446 cents per kWh Additional kWh per month at 5.713 cents per kWh.	
			Transition Period	First 15,000 kWh per month at 11.446 cents per kWh Additional kWh per month at 5.713 cents per kWh.	

Knoxville Utilities Board Electric Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)
Schedule 5

Rate Class			Number of Customers
3. If (a) the higher of the customer's currently effective contract demand or (b) its highest billing demand during the latest 12-month period is greater than 1,000 kW:			51
Customer Charge:	$160.00 per delivery point per month.		
Demand Charge:	Summer Period	First 1,000 kW of billing demand per month, at $14.23 per kW. Excess over 1,000 kW of billing demand per month, at $15.13 per kW, plus an additional $15.13 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds the higher of 2,500 kW or its contract demand.	
	Winter Period	First 1,000 kW of billing demand per month, at $13.47 per kW. Excess over 1,000 kW of billing demand per month, at $14.37 per kW, plus an additional $14.37 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds the higher of 2,500 kW or its contract demand.	
	Transition Period	First 1,000 kW of billing demand per month, at $13.47 per kW. Excess over 1,000 kW of billing demand per month, at $14.37 per kW, plus an additional $14.37 per kW per month for each kW, if any, of the amount by which the customer's billing demand exceeds the higher of 2,500 kW or its contract demand.	
Energy Charge:	Summer Period	6.175 cents per kWh.	
	Winter Period	6.175 cents per kWh.	
	Transition Period	6.175 cents per kWh.	

Knoxville Utilities Board Electric Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)

Schedule 5

Rate Class		Base Charge	Number of Customers
Commercial/ Industrial	**B.**	This rate shall apply to the firm electric power requirements where a customer's currently effective contract demand is greater than 5,000 kW but not more than 15,000 kW:	4

Customer Charge:	$1,500 per delivery point per month.	
Administrative Charge:	$700 per delivery point per month.	
Demand Charge:		
Summer Period	Onpeak Demand	$10.15 per kW per month of the customer's onpeak billing demand, plus
	Maximum Demand	$5.56 per kW per month of the customer's maximum billing demand, plus
	Excess Demand	$15.71 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.
Winter Period	Onpeak Demand	$9.25 per kW per month of the customer's onpeak billing demand, plus
	Maximum Demand	$5.56 per kW per month of the customer's maximum billing demand plus
	Excess Demand	$14.81 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.
Transition Period	Onpeak Demand	$9.25 per kW per month of the customer's onpeak billing demand, plus
	Maximum Demand	$5.56 per kW per month of the customer's maximum billing demand plus
	Excess Demand	$14.81 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.

Knoxville Utilities Board Electric Division
Supplemental Information - Schedule of Current Rates in Force
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(Unaudited)

Schedule 5

Energy Charge:

Summer Period	Onpeak	9.158 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.827 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.493 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.175 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Winter Period	Onpeak	8.094 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	7.034 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.493 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.175 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Transition Period	Onpeak	6.798 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.798 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.493 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.175 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.

For the Summer Period, Winter Period, and Transition Period, Offpeak Block 1 energy rates less fuel rat of 1.733 cents per kWh per month shall be applied to the portion, if any, of the minimum offpeak energy takings amount that is greater than the metered energy.

Rate Class		Base Charge			Number of Customers
Commercial/ Industrial	**C.**	This rate shall apply to the firm electric power requirements where a customer's currently effective contract demand is greater than 15,000 kW but not more than 25,000 kW:			1
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:			
		Summer Period	Onpeak Demand	$10.15 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.27 per kW per month of the customer's maximum billing demand, plus	
			Excess Demand	$15.42 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Winter Period	Onpeak Demand	$9.25 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.27 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$14.52 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Transition Period	Onpeak Demand	$9.25 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.27 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$14.52 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	

Energy Charge:		
Summer Period	Onpeak	9.158 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.827 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.493 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.175 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Winter Period	Onpeak	8.094 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	7.034 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.493 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.175 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Transition Period	Onpeak	6.798 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.798 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.493 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.175 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.

For the Summer Period, Winter Period, and Transition Period, Offpeak Block 1 energy rates less fuel rate of 1.733 cents per kWh per month shall be applied to the portion, if any, of the minimum offpeak energy takings amount that is greater than the metered energy.

Knoxville Utilities Board Electric Division

Supplemental Information - Schedule of Current Rates in Force

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(Unaudited)

Schedule 5

Rate Class		**Base Charge**			**Number of Customers**
Commercial/ Industrial	**D.**	This rate shall apply to the firm electric power requirements where a customer's currently effective contract demand is greater than 25,000 kW:			1
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:			
		Summer Period	Onpeak Demand	$10.15 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.32 per kW per month of the customer's maximum billing demand, plus	
			Excess Demand	$15.47 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Winter Period	Onpeak Demand	$9.25 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.32 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$14.57 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Transition Period	Onpeak Demand	$9.25 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.32 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$14.57 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	

Energy Charge:

Summer Period	Onpeak	9.183 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.852 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.412 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.200 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Winter Period	Onpeak	8.119 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	7.059 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.412 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.200 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Transition Period	Onpeak	6.823 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.823 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.412 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.200 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.

For the Summer Period, Winter Period, and Transition Period, Offpeak Block 1 energy rates less fuel rate of 1.733 cents per kWh per month shall be applied to the portion, if any, of the minimum offpeak energy takings amount that is greater than the metered energy.

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Rate Class		Base Charge			Number of Customers
Commercial/ Industrial Time of Use	**A.**	This rate shall apply to the firm electric power requirements where a customer's currently effective contract demand is greater than 1,000 kW but not more than 5,000 kW:			3
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:			
		Summer Period	Onpeak Demand	$10.21 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.56 per kW per month of the customer's maximum billing demand, plus	
			Excess Demand	$15.77 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Winter Period	Onpeak Demand	$9.31 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.56 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$14.87 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Transition Period	Onpeak Demand	$9.31 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$5.56 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$14.87 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	

Energy Charge:

Summer Period	Onpeak	9.474 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.349 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.388 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.104 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Winter Period	Onpeak	8.047 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.626 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.388 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.104 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Transition Period	Onpeak	6.737 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	6.737 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.388 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.104 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.

For the Summer Period, Winter Period, and Transition Period, Offpeak Block 1 energy rates less fuel rate of 1.733 cents per kWh per month shall be applied to the portion, if any, of the minimum offpeak energy takings amount that is greater than the metered energy.

Rate Class		Base Charge			Number of Customers
Seasonal	**B.**	This rate shall apply to the firm electric power requirements where a customer's currently effective contract demand is greater than 5,000 kW but not more than 15,000 kW:			-
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:	Summer Period	$20.18 per kW per month of the customer's billing demand, plus $20.18 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Winter Period	$17.09 per kW per month of the customer's billing demand, plus $17.09 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Transition Period	$14.01 per kW per month of the customer's billing demand, plus $14.01 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
		Energy Charge:	Summer Period	4.930 cents per kWh per month.	
			Winter Period	4.487 cents per kWh per month.	
			Transition Period	4.386 cents per kWh per month.	

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Rate Class		Base Charge			Number of Customers
Seasonal	**C.**	This rate shall apply to the firm electric power requirements where a customer's currently effective contract demand is greater than 15,000 kW but not more than 25,000 kW:			-
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:	Summer Period	$19.89 per kW per month of the customer's billing demand, plus $19.89 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Winter Period	$16.80 per kW per month of the customer's billing demand, plus $16.80 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Transition Period	$13.72 per kW per month of the customer's billing demand, plus $13.72 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
		Energy Charge:	Summer Period	4.872 cents per kWh per month.	
			Winter Period	4.418 cents per kWh per month.	
			Transition Period	4.322 cents per kWh per month.	

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Rate Class		Base Charge			Number of Customers
Seasonal	**D.**	This rate shall apply to the firm electric power requirements where a customer's currently effective contract demand is greater than 25,000 kW:			-
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:	Summer Period	$19.94 per kW per month of the customer's billing demand, plus $19.94 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Winter Period	$16.85 per kW per month of the customer's billing demand, plus $16.85 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Transition Period	$13.77 per kW per month of the customer's billing demand, plus $13.77 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
		Energy Charge:	Summer Period	4.666 cents per kWh per month.	
			Winter Period	4.271 cents per kWh per month.	
			Transition Period	4.183 cents per kWh per month.	

Rate Class		Base Charge			Number of Customers
Manufacturing	**B.**	This rate shall apply to the firm electric power requirements where (a) a customer's currently effective contract demand is greater than 5,000 kW but not more than 15,000 kW and (b) the major use of electricity is for activities conducted at the delivery point serving that customer which are classified with a 2-digit Standard Industrial Classification Code between 20 and 39, inclusive, or classified with 2002 North American Industry Classification System (NAICS) code 5181, or 2007 NAICS codes 5182, 522320, and 541214.			1
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:			
		Summer Period	Onpeak Demand	$9.55 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$2.74 per kW per month of the customer's maximum billing demand, plus	
			Excess Demand	$12.29 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Winter Period	Onpeak Demand	$8.65 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$2.74 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$11.39 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Transition Period	Onpeak Demand	$8.65 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$2.74 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$11.39 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	

Energy Charge:		
Summer Period	Onpeak	7.334 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	5.002 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.232 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	1.994 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Winter Period	Onpeak	6.270 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	5.210 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.232 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	1.994 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Transition Period	Onpeak	5.292 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	5.292 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.232 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	1.994 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.

For the Summer Period, Winter Period, and Transition Period, Offpeak Block 1 energy rates less fuel rate of 1.733 cents per kWh per month shall be applied to the portion, if any, of the minimum offpeak energy takings amount that is greater than the metered energy.

Rate Class		Base Charge	Number of Customers
Manufacturing	**C.**	This rate shall apply to the firm electric power requirements where (a) a customer's currently effective contract demand is greater than 15,000 kW but not more than 25,000 kW and (b) the major use of electricity is for activities conducted at the delivery point serving that customer which are classified with a 2-digit Standard Industrial Classification Code between 20 and 39, inclusive, or classified with 2002 North American Industry Classification System (NAICS) code 5181, or 2007 NAICS codes 5182, 522320, and 541214.	2

Customer Charge:	$1,500 per delivery point per month.	
Administrative Charge:	$700 per delivery point per month.	
Demand Charge:		
Summer Period	Onpeak Demand	$9.55 per kW per month of the customer's onpeak billing demand, plus
	Maximum Demand	$2.49 per kW per month of the customer's maximum billing demand, plus
	Excess Demand	$12.04 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.
Winter Period	Onpeak Demand	$8.65 per kW per month of the customer's onpeak billing demand, plus
	Maximum Demand	$2.49 per kW per month of the customer's maximum billing demand plus
	Excess Demand	$11.14 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.
Transition Period	Onpeak Demand	$8.65 per kW per month of the customer's onpeak billing demand, plus
	Maximum Demand	$2.49 per kW per month of the customer's maximum billing demand plus
	Excess Demand	$11.14 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.

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Energy Charge:

Summer Period	Onpeak	7.229 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	4.897 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.365 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.365 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Winter Period	Onpeak	6.165 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	5.105 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.365 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.365 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Transition Period	Onpeak	5.186 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	5.186 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.365 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.365 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.

For the Summer Period, Winter Period, and Transition Period, Offpeak Block 1 energy rates less fuel rate of 1.733 cents per kWh per month shall be applied to the portion, if any, of the minimum offpeak energy takings amount that is greater than the metered energy.

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Rate Class		Base Charge			Number of Customers
Manufacturing	**D.**	This rate shall apply to the firm electric power requirements where (a) a customer's currently effective contract demand is greater than 25,000 kW and (b) the major use of electricity is for activities conducted at the delivery point serving that customer which are classified with a 2-digit Standard Industrial Classification Code between 20 and 39, inclusive, or classified with 2002 North American Industry Classification System (NAICS) code 5181, or 2007 NAICS codes 5182, 522320, and 541214.			1
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:			
		Summer Period	Onpeak Demand	$9.55 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$2.54 per kW per month of the customer's maximum billing demand, plus	
			Excess Demand	$12.09 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Winter Period	Onpeak Demand	$8.65 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$2.54 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$11.19 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Transition Period	Onpeak Demand	$8.65 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$2.54 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$11.19 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	

Energy Charge:		
Summer Period	Onpeak	7.042 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	4.710 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.231 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.178 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Winter Period	Onpeak	5.978 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	4.918 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.231 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.178 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Transition Period	Onpeak	4.999 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	4.999 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.231 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	2.178 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.

For the Summer Period, Winter Period, and Transition Period, Offpeak Block 1 energy rates less fuel rate of 1.733 cents per kWh per month shall be applied to the portion, if any, of the minimum offpeak energy takings amount that is greater than the metered energy.

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Rate Class		Base Charge			Number of Customers
Manufacturing Time of Use	**A.**	This rate shall apply to the firm electric power requirements where (a) a customer's currently effective contract demand is greater than 1,000 kW but not more than 5,000 kW and (b) the major use of electricity is for activities conducted at the delivery point serving that customer which are classified with a 2-digit Standard Industrial Classification Code between 20 and 39, inclusive, or classified with 2002 North American Industry Classification System (NAICS) code 5181, or 2007 NAICS codes 5182, 522320, and 541214.			1
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:			
		Summer Period	Onpeak Demand	$9.55 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$3.97 per kW per month of the customer's maximum billing demand, plus	
			Excess Demand	$13.52 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Winter Period	Onpeak Demand	$8.65 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$3.97 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$12.62 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	
		Transition Period	Onpeak Demand	$8.65 per kW per month of the customer's onpeak billing demand, plus	
			Maximum Demand	$3.97 per kW per month of the customer's maximum billing demand plus	
			Excess Demand	$12.62 per kW per month for each kW of the amount, if any, by which (1) the customer's onpeak billing demand exceeds its onpeak contract demand or (2) the customer's offpeak billing demand exceeds its offpeak contract demand, whichever is higher.	

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Energy Charge:

Summer Period	Onpeak	7.122 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	4.790 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.232 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	1.994 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Winter Period	Onpeak	6.058 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	4.998 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.232 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	1.994 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.
Transition Period	Onpeak	5.080 cents per kWh per month for all metered onpeak kWh, plus
	Offpeak: Block 1	5.080 cents per kWh per month for the first 200 hours use of onpeak metered demand multiplied by the ratio of offpeak energy to toal energy, plus
	Block 2	2.232 cents per kWh per month for the next 200 hours use of onpeak metered demand multiplied by the ratio of offpeak enegy to total energy, plus
	Block 3	1.994 cents per kWh per month for the hours use of onpeak metered demand in excess of 400 hours multiplied by the ratio of offpeak energy to total energy.

For the Summer Period, Winter Period, and Transition Period, Offpeak Block 1 energy rates less fuel rate of 1.733 cents per kWh per month shall be applied to the portion, if any, of the minimum offpeak energy takings amount that is greater than the metered energy.

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Manufacturing			**Number of Customers**
Seasonal	**B.**	This rate shall apply to the firm electric power requirements where (a) a customer's currently effective contract demand is greater than 5,000 kW but not more than 15,000 kW and (b) the major use of electricity is for activities conducted at the delivery point serving that customer which are classified with a 2-digit Standard Industrial Classification Code between 20 and 39, inclusive, or classified with 2002 North American Industry Classification System (NAICS) code 5181, or 2007 NAICS codes 5182, 522320, and 541214.	-

Customer Charge:	$1,500 per delivery point per month.	
Administrative Charge:	$700 per delivery point per month.	
Demand Charge:	Summer Period	$17.00 per kW per month of the customer's billing demand, plus $17.00 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.
	Winter Period	$13.91 per kW per month of the customer's billing demand, plus $13.91 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.
	Transition Period	$10.83 per kW per month of the customer's billing demand, plus $10.83 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.
Energy Charge:	Summer Period	4.025 cents per kWh per month.
	Winter Period	3.524 cents per kWh per month.
	Transition Period	3.406 cents per kWh per month.

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					Number of Customers
Seasonal	**C.**	This rate shall apply to the firm electric power requirements where (a) a customer's currently effective contract demand is greater than 15,000 kW but not more than 25,000 kW and (b) the major use of electricity is for activities conducted at the delivery point serving that customer which are classified with a 2-digit Standard Industrial Classification Code between 20 and 39, inclusive, or classified with 2002 North American Industry Classification System (NAICS) code 5181, or 2007 NAICS codes 5182, 522320, and 541214.			-
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:	Summer Period	$16.75 per kW per month of the customer's billing demand, plus $16.75 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Winter Period	$13.66 per kW per month of the customer's billing demand, plus $13.66 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Transition Period	$10.58 per kW per month of the customer's billing demand, plus $10.58 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
		Energy Charge:	Summer Period	3.940 cents per kWh per month.	
			Winter Period	3.470 cents per kWh per month.	
			Transition Period	3.357 cents per kWh per month.	

Manufacturing					**Number of Customers**
Seasonal	**D.**	This rate shall apply to the firm electric power requirements where (a) a customer's currently effective contract demand is greater than 25,000 kW; and (b) the major use of electricity is for activities conducted at the delivery point serving that customer which are classified with a 2-digit Standard Industrial Classification Code between 20 and 39, inclusive, or classified with 2002 North American Industry Classification System (NAICS) code 5181, or 2007 NAICS codes 5182, 522320, and 541214.			-
		Customer Charge:	$1,500 per delivery point per month.		
		Administrative Charge:	$700 per delivery point per month.		
		Demand Charge:	Summer Period	$19.94 per kW per month of the customer's billing demand, plus $19.94 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Winter Period	$16.85 per kW per month of the customer's billing demand, plus $16.85 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
			Transition Period	$13.77 per kW per month of the customer's billing demand, plus $13.77 per kW per month for each kW of the amount, if any, by which the customer's billing demand exceeds its contract demand.	
		Energy Charge:	Summer Period	3.194 cents per kWh per month.	
			Winter Period	2.818 cents per kWh per month.	
			Transition Period	2.726 cents per kWh per month.	

Knoxville Utilities Board Electric Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)
Schedule 5

Rate Class	Base Charge	Number of Customers
Outdoor Lighting		
	Part A - Charges for Street and Park Lighting Systems, Traffic Signal Systems, and Athletic Field Lighting Installations	51

Energy Charge:	Summer Period	7.173 cents per kWh per month.
	Winter Period	7.173 cents per kWh per month.
	Transition Period	7.173 cents per kWh per month.

Facility Charge: The annual facility charge shall be 14.64 percent of the installed cost to KUB's electric system of the facilities devoted to street and park lighting service specified in this Part A. Such installed cost shall be recomputed on July 1 of each year, or more often if substantial changes in the facilities are made. Each month, one-twelfth of the then total annual facility charge shall be billed to the customer. If any part of the facilities has not been provided at the electric system's expense, or if the installed cost of any portion thereof is reflected on the books of another municipality or agency or department, the annual facility charge shall be adjusted to reflect properly the remaining cost to be borne by the electric system.

Customer Charge: $2.50.

Part B - Charges for Outdoor Lighting for Individual Customers 1374

Charges Per Fixture Per Month

a.	**Type of Fixture**	**(Watts)**	**(Lumens)**	**Rated kWh**	**Facility Charge**	**Total Lamp Charge**
	Mercury Vapor or Incandescent*	175	7,650	70	$ 4.58	$ 9.60
		400	19,100	155	6.39	17.51
		1000**	47,500	378	10.22	37.33
	High Pressure Sodium	100	8,550	42	4.58	7.59
		250	23,000	105	5.43	12.96
		400	45,000	165	6.39	18.23
		1000**	126,000	385	10.22	37.84
	Decorative	100	8,550	42	5.21	8.22

* Mercury Vapor and Incandescent fixtures not offered for new service.

** 1,000 watt fixtures not offered for new service.

b. Energy Charge: For each lamp size under **a.** above, 7.173 cents per rated kWh per month.

Additional pole charge: $3.00 per pole.

Rate Class	Base Charge	Number of Customers
LED Pilot Program	Service under the LED Pilot Program shall only be available for select outdoor (security) lighting facilities of governmental entities located in the KUB electric system service territory. Participation in the LED Pilot Program shall be on a voluntary basis.	
	Pilot Program Charges - No Capital Contribution	-

The following charges are applicable to those customers participating in the LED Pilot Program, for whom the installed cost of facilities for providing service under the program has been borne by the electric system. The following charges are per LED fixture per month.

LED Fixture Type	Facility Charge	Rated kWh	Energy Charge Per kWh	Total Charge
LED - 150WE - Rectangular Head	$ 12.27	38	$ 0.07173	$ 15.00
LED - 150WE - Cobra Head	11.19	38	0.07173	13.92
LED - 250WE - Rectangular Head	$ 14.75	57	$ 0.07173	$ 18.84
LED - 250WE - Cobra Head	13.44	57	0.07173	17.53

		Number of Customers
	Pilot Program Charges - Capital Contribution	-

The following charges are applicable to those customers participating in the LED Pilot Program, for whom the installed cost of facilities providing service under the program has been borne by the customer. The following charges are per LED fixture per month.

LED Fixture Type	Facility Charge	Rated kWh	Energy Charge Per kWh	Total Charge
LED - 150WE - Rectangular Head	$ 5.29	38	$ 0.07173	$ 8.02
LED - 150WE - Cobra Head	5.16	38	0.07173	7.89
LED - 250WE - Rectangular Head	$ 6.15	57	$ 0.07173	$ 10.24
LED - 250WE - Cobra Head	5.98	57	0.07173	10.07

Additional pole charge: $3.00 per pole.

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

Board of Commissioners
Electric Division of the Knoxville Utilities Board
Knoxville, Tennessee

Report on the Financial Statements

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Electric Division (the Division) of the Knoxville Utilities Board, a component unit of the City of Knoxville, Tennessee, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements, and have issued our report thereon dated October 27, 2016.

Internal Control over Financial Reporting

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

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

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

Board of Commissioners
Electric Division of the Knoxville Utilities Board
Knoxville, Tennessee

Compliance and Other Matters

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

Purpose of Report

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

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

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Report of Independent Auditors on Compliance for Each Major Program and on Internal Control over Compliance Required by the Uniform Guidance

Board of Commissioners
Electric Division of the Knoxville Utilities Board
Knoxville, Tennessee

Report on Compliance for the Major Federal Program

We have audited the Electric Division (the Division) of the Knoxville Utilities Board's, a component unit of the City of Knoxville, Tennessee, compliance with the types of compliance requirements described in the OMB Compliance Supplement that could have a direct and material effect on the Division's major federal program for the year ended June 30, 2016. The Division's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the Division's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Division's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the Division's compliance.

Board of Commissioners
Electric Division of the Knoxville Utilities Board
Knoxville, Tennessee

Opinion on the Major Federal Program

In our opinion, the Division complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2016.

Report on Internal Control over Compliance

Management of the Division is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Division's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Division's internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

Knoxville Utilities Board

Gas Division

Financial Statements and Supplemental Information
June 30, 2016 and 2015

KUB Board of Commissioners

Management

Mintha Roach
President and
Chief Executive Officer

Bill Elmore
Executive Vice President and
Chief Operating Officer

Mark Walker
Senior Vice President and
Chief Financial Officer

Susan Edwards
Senior Vice President and
Chief Administrative Officer

Eddie Black
Senior Vice President

Mike Bolin
Vice President

Julie Childers
Vice President

Derwin Hagood
Vice President

Dawn Mosteit
Vice President

Paul Randolph
Vice President

Dennis Upton
Vice President

Knoxville Utilities Board Gas Division
Index
June 30, 2016 and 2015

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Report of Independent Auditors

Board of Commissioners
Gas Division of the Knoxville Utilities Board
Knoxville, Tennessee

We have audited the accompanying financial statements of the Gas Division (the Division) of the Knoxville Utilities Board, a component unit of the City of Knoxville, Tennessee, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements as listed in the index.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Division'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 Division'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 the Gas Division of the Knoxville Utilities Board as of June 30, 2016 and 2015, and the changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Commissioners
Gas Division of the Knoxville Utilities Board
Knoxville, Tennessee

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 23 and the required supplementary information on pages 52 through 54 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Division's basic financial statements. The supplemental information is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplemental information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 27, 2016, on our consideration of the Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

Knoxville Utilities Board Gas Division
Management's Discussion and Analysis
June 30, 2016 and 2015

Knoxville Utilities Board (KUB), comprised of Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions. The Gas Division (Division) provides services to certain customers in Knox County and portions of Anderson and Loudon counties. The Division's accounts are maintained in conformity with the Uniform System of Accounts of the Federal Energy Regulatory Commission and the Governmental Accounting Standards Board, as applicable. The financial statements present only the Gas Division and do not purport to, and do not, present fairly the consolidated financial position of Knoxville Utilities Board at June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Division's discussion and analysis is designed to (a) assist the reader in focusing on significant financial issues, (b) provide an overview of the Division's financial activity, (c) identify major changes in the Division's financial position, and (d) identify any financial concerns.

The Division's Management Discussion and Analysis (MD&A) focuses on the fiscal year ending June 30, 2016 activities, resulting changes and current known facts, and should be read in conjunction with the Division's financial statements.

Gas Division Highlights

System Highlights

KUB's natural gas system serves 99,808 customers, and its service territory covers 284 square miles. KUB maintains 2,316 miles of service mains to provide 11.4 million dekatherms of natural gas to its customers annually.

KUB's natural gas system service territory experienced the second mildest winter in the last forty years. As a result, natural gas sales were 10.2 percent less than the previous fiscal year. Gas Division margin (operating revenue less purchased gas cost) was $3.2 million lower in fiscal year 2016, reflecting a decrease in sales volumes from a mild winter and additional revenue from gas system rate increases which were effective in October 2014 and October 2015.

The natural gas system's peak demand occurred February 2015 at 136,356 dekatherms. The previous natural gas system peak was 133,366 dekatherms in January 2014.

The typical residential gas customer's average monthly gas bill was $52.51 for the twelve months ending June 30, 2016, representing a decrease of $4.64 compared to last year based on normalized sales.

The natural gas system has added approximately 1,583 customers over the past three years representing annual growth of less than one percent.

Century II Infrastructure Program

Century II is KUB's proactive long-range program to improve and maintain the electric, natural gas, water and wastewater systems for its customers. It includes maintenance and asset replacement strategies for each system and establishes sustainable replacement cycles. Century II moves KUB into its second century of service by improving each system through sound planning, resource allocation, and continued, but accelerated, investment.

In 2013, the Board extended the funding approach for Century II to include the natural gas system. The Board formally endorsed by resolution, a ten year funding plan for the Gas Division, which includes a combination of rate increases and debt issues to fully fund the natural gas system's Century II program.

In April 2014, KUB management provided the Board an updated assessment of the overall condition of each utility system, including a recommendation for annual rate increases for each division for the next three fiscal years.

In June 2014, the Board approved the proposed three annual rate increases for the Gas Division. Each gas rate increase will generate $1.8 million in additional annual Gas Division revenue.

In fiscal year 2015, KUB concluded the smart grid pilot project, of which a portion of the project was funded by a United States Department of Energy Smart Grid Investment Grant (SGIG). This grant was received by KUB in 2009 as part of the American Reinvestment and Recovery Act (ARRA). Based upon the success of that pilot, KUB formed a plan to move forward with a Century II Grid Modernization initiative, which includes advanced metering for all KUB customers, a telecommunication system linking critical KUB infrastructure, and an increased investment in automation technology to help operate KUB's energy and water distribution systems.

KUB replaced 4.2 miles of cast iron/ductile iron gas main during fiscal year 2016, which was less than originally forecast due to a shift in focus to other gas system improvements.

The South Loop project that included a new 8 mile transmission main in the southwest portion of KUB's service territory was completed in October 2015. The South Loop provides additional system capacity to meet the increased natural gas demands of the University of Tennessee, in addition to other potential growth opportunities in that portion of KUB's gas service territory.

Financial Highlights

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division's net position increased $7.6 million in fiscal year 2016. This increase was $4.5 million less than the prior year's change in net position. A restatement to the fiscal year 2014's net position based on a change in method of accounting for the pension reduced the total net position by $0.1 million during fiscal year 2015.

Operating revenue decreased $25.7 million or 22.5 percent. The decrease is attributable to a decrease of 10.2 percent in billed sales volumes and lower wholesale gas costs, which were directly flowed through to KUB's natural gas rates through the Purchased Gas Adjustment mechanism. Purchased gas expense was $22.5 million or 35.3 percent lower due to reduced customer demand from the mild winter and lower natural gas commodity prices. Margin on gas sales (operating revenue less purchased gas expense) decreased $3.2 million or 6.4 percent, reflecting the decrease in gas sales volumes partially offset by additional revenue from the rate increases.

Operating expenses (excluding purchased gas expense) increased $1.8 million or 5.4 percent. Taxes and tax equivalents increased $0.7 million and depreciation expense was $0.6 million higher than the prior year. Operating and maintenance (O&M) expenses were $0.5 million more than the prior fiscal year.

Wholesale purchased gas expense represented forty seven percent of natural gas sales revenue for the fiscal year ended June 30, 2016.

Interest income was consistent with the prior fiscal year. Interest expense decreased $0.5 million, the result of lower interest costs from the refinancing of certain outstanding bonds in April 2015.

Total plant assets (net) increased $15.5 million or 6.2 percent reflecting capital investment associated with the replacement of key gas system assets and other major system projects, including the South Loop.

Long-term debt represented 34.5 percent of the Division's capital structure as of June 30, 2016, as compared to 36.6 percent last year. Capital structure equals long-term debt (which includes the current and long-term portion of revenue bonds and notes) plus net position.

The Division's bond covenants require a debt service coverage ratio of at least 1.2 times the maximum principal and interest payments over the life of the Division's outstanding bonds. Current year debt coverage for the fiscal year was 3.13. Maximum debt service coverage was 3.16.

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division's net position increased $12.1 million in fiscal year 2015. This increase was $1.5 million greater than the prior year's change in net position. A restatement to the prior fiscal year's net position based on a change in method of accounting for the pension reduced the total net position by $0.1 million during fiscal year 2015. This change resulted in a net increase of $12 million or 6.9 percent in the Division's net position.

Operating revenue decreased $3 million or 2.5 percent. A modest increase of approximately one percent in sales volumes was offset by lower wholesale gas costs, which were directly flowed through to KUB's natural gas rates through the Purchased Gas Adjustment mechanism. Purchased gas expense was $5.6 million or 8.1 percent lower due to reduced natural gas commodity prices. Margin on gas sales (operating revenue less purchased gas expense) increased $2.6 million or 5.5 percent, reflecting the modest increase in gas sales volumes and additional revenue from the rate increases.

Operating expenses (excluding purchased gas expense) increased $1.3 million or 3.9 percent. Depreciation expense was $1.2 million higher than the prior year. Operating and maintenance (O&M) expenses were $0.2 million less than the prior fiscal year while taxes and tax equivalents increased $0.3 million.

Wholesale purchased gas expense represented 57 percent of natural gas sales revenue for the fiscal year ended June 30, 2015.

Interest income was consistent with the prior fiscal year. Interest expense decreased $0.1 million, the result of lower interest costs from the refinancing of certain outstanding bonds in April 2015.

Total plant assets (net) increased $26.7 million or 12 percent over the end of the last fiscal year reflecting capital investment associated with the replacement of key gas system assets and other major system projects, including the South Loop.

Long-term debt represented 36.6 percent of the Division's capital structure as of June 30, 2015, as compared to 39.2 percent last year. Capital structure equals long-term debt (which includes the current and long-term portion of revenue bonds and notes) plus net position.

The Division's bond covenants require a debt service coverage ratio of at least 1.2 times the maximum principal and interest payments over the life of the Division's outstanding bonds. Current year debt coverage for the fiscal year was 3.52. Maximum debt service coverage was 3.53.

Knoxville Utilities Board Gas Division - Financial Statements

The Division's financial performance is reported under three basic financial statements: the Statement of Net Position; the Statement of Revenues, Expenses and Changes in Net Position; and the Statement of Cash Flows.

Statement of Net Position

The Division reports its assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position in the Statement of Net Position. Assets are classified as current, restricted, gas plant in service, or other assets.

Liabilities are classified as current, other, or long-term debt. Net position is classified as net investment in capital assets; restricted; or unrestricted. Net position represents what was previously reported as accumulated or retained earnings. Net position tells the user what the Division has done with its accumulated earnings not just the balance.

Net investment in capital assets is the net book value of all capital assets less the outstanding balances of debt used to acquire, construct, or improve those assets.

Restricted net position includes assets that have been limited to specific uses by the Division's bond covenants or through resolutions passed by the KUB Board.

Unrestricted net position is a residual classification; the amount remaining after reporting net position as either invested in capital or restricted is reported there.

Statement of Revenues, Expenses and Changes in Net Position

The Division reports its revenues and expenses (both operating and non-operating) on the Statement of Revenues, Expenses and Changes in Net Position. In addition, any contributions in aid of construction (funds received via grants, developers, etc. to fund capital projects) and associated write-downs of plant assets are reported on this statement.

Total revenue less total expense equals the change in net position for the reporting. Net position at the beginning of the period are increased or decreased, as applicable, by the change in net position for the reporting period.

The change in net position for the reporting period is added to the net position segment of the Statement of Net Position.

Statement of Cash Flows

The Divisions reports its cash flows from operating activities, capital and related financing activities, and investing activities on its Statement of Cash Flows. This statement tells the user the Division's sources and uses of cash during the reporting period.

The statement indicates the Division's beginning cash balance and ending cash balance and how it was either increased or decreased during the reporting period.

The statement also reconciles cash flow back to operating income as it appears on the Statement of Revenues, Expenses and Changes in Net Position.

Condensed Financial Statements

Statement of Net Position

The following table reflects the condensed Statement of Net Position for the Gas Division compared to the prior year and the year preceding the prior year.

Statements of Net Position
As of June 30

(in thousands of dollars)	2016	2015	2014
Current, restricted and other assets	$ 47,676	$ 63,520	$ 85,266
Capital assets, net	263,531	248,032	221,372
Deferred outflows of resources	3,005	1,925	512
Total assets and deferred outflows of resources	314,212	313,477	307,150
Current and other liabilities	19,875	20,070	22,182
Long-term debt outstanding	100,164	105,919	110,650
Deferred inflows of resources	257	1,148	-
Total liabilities and deferred inflows of resources	120,296	127,137	132,832
Net position			
Net investment in capital assets	159,696	138,973	107,234
Restricted	1,820	1,801	1,725
Unrestricted	32,400	45,566	65,359
Total net position	$ 193,916	$ 186,340	$ 174,318

Normal Impacts on Statement of Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Net Position presentation.

- Change in net position (from Statement of Revenues, Expenses and Changes in Net Position): impacts (increase/decrease) current and other assets and/or capital assets and unrestricted net position.

- Issuing debt for capital: increases deferred outflows of resources and long-term debt.

- Spending debt proceeds on new capital: reduces current assets and increases capital assets.

- Spending of non-debt related current assets on new capital: (a) reduces current assets and increases capital assets and (b) reduces unrestricted net position and increases net investment in capital assets.

- Principal payment on debt: (a) reduces current and other assets and reduces long-term debt and (b) reduces unrestricted net position and increases net investment in capital assets.

- Reduction of capital assets through depreciation: reduces capital assets and net investment in capital assets.

Impacts and Analysis

Current, Restricted and Other Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Current, restricted and other assets decreased $15.8 million or 24.9 percent. General fund cash and investments decreased $15.2 million primarily to fund capital expenditures. Operating contingency reserves increased $1.2 million. Accounts receivable decreased $1.5 million compared to June 2015.

KUB under recovered its wholesale gas costs by $2.2 million in fiscal year 2016 compared to a $1.1 million over recovery in fiscal year 2015. The under recovery of costs will be collected from customers next fiscal year through adjustments to rates via the Purchased Gas Adjustment. Gas storage decreased $1.4 million, reflecting lower commodity prices for natural gas for slightly higher storage volumes compared to the prior fiscal year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current, restricted and other assets decreased $21.7 million or 25.5 percent. General fund cash and investments decreased $17.8 million in order to fund capital expenditures. Operating contingency reserves increased $1 million. Accounts receivable decreased $2.3 million compared to June 2014. Gas storage decreased $0.8 million, reflecting lower commodity prices for natural gas which offset the impact of higher storage volumes.

Capital Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Capital assets increased $15.5 million or 6.2 percent. Major capital expenditures during the year included $15.1 million for the construction of mains and service extensions, $3.9 million for gas main replacement, $2.5 million for the replacement and relocation of gas system assets to accommodate Tennessee Department of Transportation (TDOT) highway improvement projects, and $1.4 million for upgrades to various information systems.

Fiscal Year 2015 Compared to Fiscal Year 2014

Capital assets increased $26.7 million or 12 percent. Major capital expenditures during the year included $24.2 million for the construction of mains and service extensions and $6 million for gas main replacement. The Division also retired $1.8 million of assets during the year.

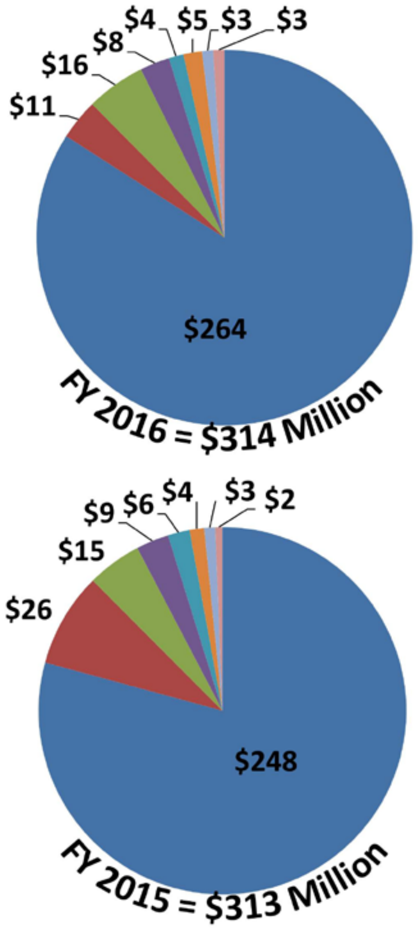
Deferred Outflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred outflows of resources increased $1.1 million compared to the prior fiscal year. This increase is attributable to a $1.2 million increase in pension outflow and a $0.1 million decrease in unamortized bond refunding costs.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred outflows of resources increased $1.4 million compared to the prior fiscal year. This increase is attributable to a $0.8 million increase in unamortized bond refunding costs and a $0.6 million increase in pension outflow.



Gas Division Total Assets and Deferred Outflows of Resources (in Millions)

		FY16	FY15
■	Plant	84%	79%
■	General Fund	4%	8%
■	Contingency Fund	5%	5%
■	Gas Storage	3%	3%
■	Accounts Receivable	1%	2%
■	Other Assets	1%	1%
■	Restricted Assets	1%	1%
■	Deferred Outflows of Resources	1%	1%

Current and Other Liabilities

Fiscal Year 2016 Compared to Fiscal Year 2015

Current and other liabilities decreased $0.2 million or 1 percent. Accounts payable decreased $0.4 million compared to the prior fiscal year. This was offset by an actuarially determined net pension obligation of $0.9 million recognized during fiscal year 2016.

KUB over recovered $1.1 million in wholesale gas costs of from its customers in fiscal year 2015 as compared to a $2.2 million under recovery in fiscal year 2016. The over recovery of costs was flowed back to KUB's gas customers during fiscal year 2016 through adjustments to rates via the Purchased Gas Adjustment.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current and other liabilities decreased $2.1 million or 9.5 percent. The Division over recovered $1.1 million in wholesale gas costs from its customers in fiscal year 2015, as compared to $1.3 million over recovered in fiscal year 2014. This over recovery of costs will be flowed back to KUB's gas customers next fiscal year through adjustments to rates via the Purchased Gas Adjustment. Accounts payable decreased $1 million compared to the prior fiscal year. Current payables for bond debt increased $0.3 million and accrued interest on bonds decreased $0.1 million.

Long-Term Debt

Fiscal Year 2016 Compared to Fiscal Year 2015

Long-term debt was $5.8 million or 5.4 percent lower than the prior year, primarily due to $5.5 million of long-term bond debt that shifted to current liabilities as payable within the next year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Long-term debt was $4.7 million or 4.3 percent lower than the prior year, primarily the result of the scheduled repayment of bond debt during the fiscal year.

Deferred Inflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred inflows of resources decreased $0.9 million compared to the prior fiscal year due to differences in pension inflows.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred inflows of resources increased $1.1 million due to the addition of pension inflow.

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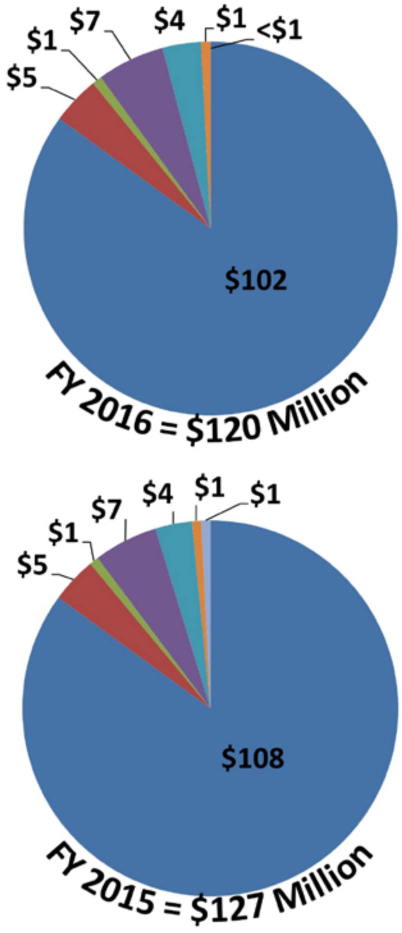

Gas Division Total Liabilities and Deferred Inflows of Resources (in Millions)

	FY16	FY15
🟦 Bond Debt	85%	84%
🟥 Payables	4%	4%
🟩 Misc Current	1%	1%
🟪 Other Liabilities	6%	6%
🟦 Customer Deposits	3%	3%
🟧 Interest Accrued	1%	1%
🟦 Deferred Inflows of Resources	<1%	1%

Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

Net investment in capital assets, net of debt increased $20.7 million or 14.9 percent, primarily from an increase in net plant in service of $15.5 million and a decrease of $5.8 million in long term debt. Restricted net position was consistent with the prior fiscal year. Unrestricted net position decreased $13.2 million primarily due to a $15.2 million decrease in general fund cash compared to June of the prior year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Net investment in capital assets, net of debt increased $31.7 million or 29.6 percent, primarily from an increase in net plant in service of $26.7 million offset by a decrease of $4.7 million in long term debt. Restricted net position increased $0.1 million compared to the prior fiscal year. Unrestricted net position decreased $19.8 million primarily due to a $17.8 million decrease in general fund cash compared to June of the prior year.

Statement of Revenues, Expenses and Changes in Net Position

The following table reflects the condensed Statement of Revenues, Expenses and Changes in Net Position for the Gas Division compared to the prior year and the year preceding the prior year.

Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended June 30

(in thousands of dollars)	2016	2015	2014
Operating revenues	$ 88,441	$ 114,169	$ 117,146
Less: Purchased gas expense	41,212	63,735	69,351
Margin from sales	47,229	50,434	47,795
Operating expenses			
Distribution	8,305	7,922	7,617
Customer service	2,676	2,688	2,626
Administrative and general	5,984	5,843	6,460
Depreciation	11,481	10,895	9,675
Taxes and tax equivalents	7,391	6,657	6,336
Total operating expenses	35,837	34,005	32,714
Operating income	11,392	16,429	15,081
Interest income	183	159	144
Interest expense	(4,033)	(4,537)	(4,772)
Other income/(expense)	34	105	175
Change in net position before capital contributions	7,576	12,156	10,628
Capital contributions	-	4	-
Change in net position	$ 7,576	$ 12,160	$ 10,628

Normal Impacts on Statement of Revenues, Expenses and Changes in Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Revenues, Expenses and Changes in Net Position presentation.

- Operating revenue is largely determined by volume of natural gas sales for the fiscal year. Any change (increase/decrease) in retail gas rates would also be a cause of change in operating revenue. The Division utilizes a Purchased Gas Adjustment (PGA) mechanism in setting its monthly retail gas rates. Through the PGA, the Division adjusts its retail rates each month based on current wholesale gas prices. If wholesale gas prices increase/decrease, the Division increases/decreases its retail gas rates accordingly.

- Volumes of gas purchased from the Division's wholesale gas suppliers for resale to customers impact purchased gas expense. The Division purchases gas for resale to its customers from a variety of wholesale suppliers. Changes (increase/decrease) in wholesale gas prices would also result in a change in purchased gas expense.

- Operating expenses (distribution, customer service, administrative and general) are normally impacted by changes in areas including, but not limited to, labor costs (staffing, wage rates), active employee and retiree medical costs, and gas distribution system maintenance.

- Depreciation expense is impacted by plant additions and retirements during the fiscal year.

- Taxes and tax equivalents are impacted by plant additions/retirements, changes in property tax rates, and margin (operating revenue less purchased gas expense) levels.

- Interest income is impacted by the level of interest rates and investments.

- Interest expense on debt is impacted by the level of outstanding debt and the interest rates on the outstanding debt.

- Other income/(expense) is impacted by miscellaneous non-operating revenues and expenses.

Impacts and Analysis

Change in Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division’s net position increased $7.6 million. This increase was $4.5 million lower than the prior year’s change in net position. A restatement to fiscal year 2014’s net position based on a change in method of accounting for the pension reduced the total net position by $0.1 million during fiscal year 2015. Lower earnings were primarily attributable to decreased margin on gas sales.

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division’s net position increased $12.1 million. This increase was $1.5 million greater than the prior year’s change in net position. A restatement to the prior fiscal year’s net position based on a change in method of accounting for the pension reduced the total net position by $0.1 million during fiscal year 2015. This change resulted in a net increase of $12 million or 6.9 percent in the Division’s net position. Higher earnings were primarily attributable to increased margin on gas sales.

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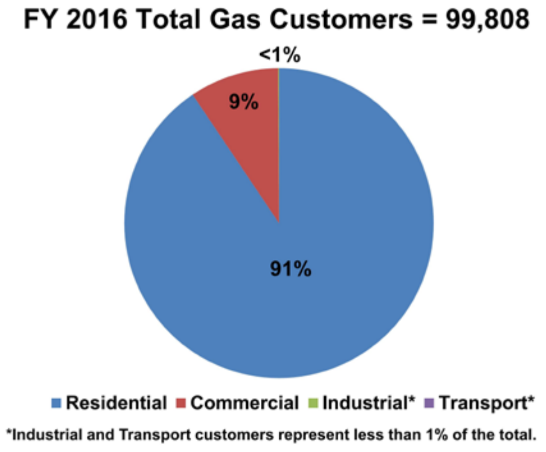
Margin from Sales

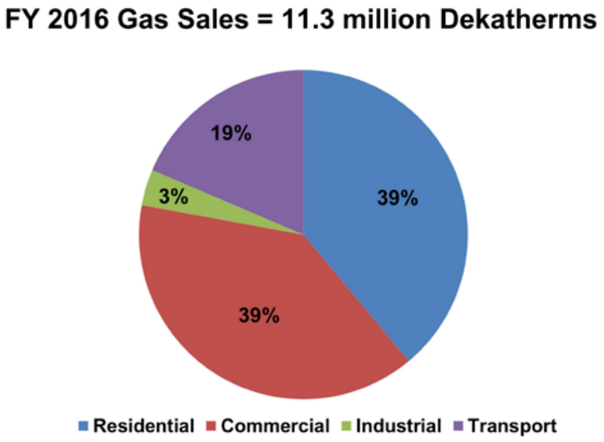
Fiscal Year 2016 Compared to Fiscal Year 2015

Margin on gas sales (operating revenue less purchased gas expense) decreased $3.2 million or 6.4 percent due to a 10.2 percent decrease in billed sales volumes offset by revenue from rate increases that were effective October 2014 and October 2015.

Operating revenue decreased $25.7 million or 22.5 percent for the fiscal year ending June 30, 2016. The gas system service territory experienced the second mildest winter in the last forty years. Billed sales were down 10.2 percent due to the warmer winter, and purchased gas commodity prices flowed through to customer rates were lower. However, additional revenue was generated from the rate increases.

Purchased gas expense decreased $22.5 million or 35.3 percent, due to lower customer demand and reduced commodity prices for natural gas during the fiscal year. KUB purchased 15.5 percent less gas from its suppliers during the fiscal year to meet customer demand and maintain gas storage levels. The net result was a 14.6 percent decrease in total volumes delivered to KUB's gas distribution system. The Division's weighted average cost of gas purchased for fiscal year 2016 was $2.49 per dekatherm, as compared to $3.62 per dekatherm last year.





Residential customers, whose natural gas is primarily used as a heat source during winter months, accounted for 91 percent of customers billed and 39 percent of total volumes sold during the year.

Commercial and industrial sales volumes (including transportation customers) increased 3.3 percent. KUB's ten largest gas customers accounted for 28.1 percent of KUB's billed gas volumes. Those ten customers represent five industrial and five commercial customers, including one governmental customer.

KUB also has 18 transport customers who purchase gas directly from a supplier other than KUB. KUB provides transportation service on its gas distribution system to those customers.

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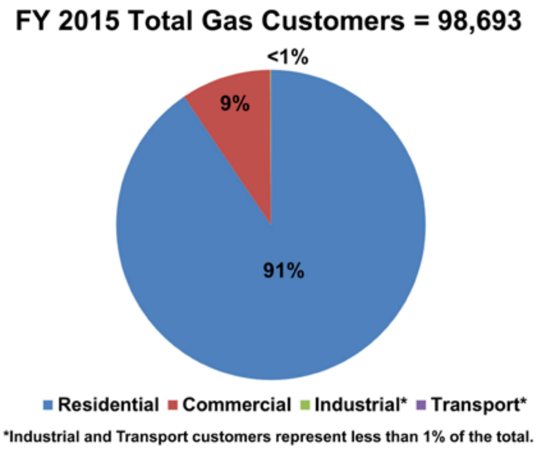
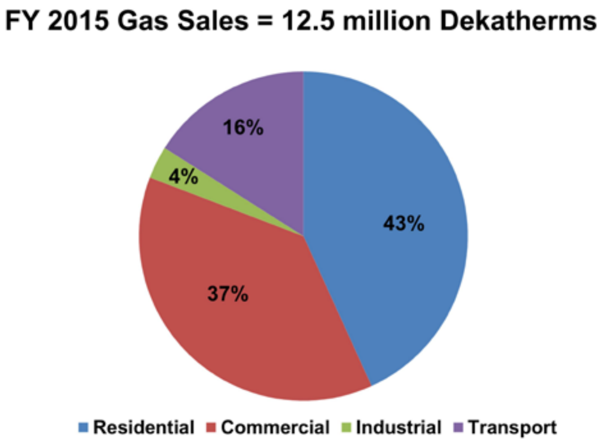
Fiscal Year 2015 Compared to Fiscal Year 2014

Margin on gas sales (operating revenue less purchased gas expense) increased $2.6 million or 5.5 percent due to a 0.7 percent increase in billed sales volumes as well as revenue from rate increases that were effective October 2013 and October 2014.

Operating revenue decreased $3 million or 2.5 percent for the fiscal year ending June 30, 2015, the net result of lower purchased gas commodity prices flowed through to customer rates and additional revenue from the rate increases.

Purchased gas expense decreased $5.6 million or 8.1 percent, due to reduced commodity prices for natural gas during the fiscal year. KUB purchased 2.3 percent more gas from its suppliers during the fiscal year to meet a modest increase in customer demand and maintain gas storage levels. The net result was a 0.9 percent increase in total volumes delivered to KUB's gas distribution system. The Division's weighted average cost of gas purchased for fiscal year 2015 was $3.62 per dekatherm, as compared to $4.08 per dekatherm last year.





Residential customers, whose natural gas is primarily used as a heat source during winter months, accounted for 91 percent of customers billed and 43 percent of total volumes sold during the year.

Commercial and industrial sales volumes (including transportation customers) decreased 2.9 percent. KUB's ten largest gas customers accounted for 23.3 percent of KUB's billed gas volumes. Those ten customers represent five industrial and five commercial customers, including one governmental customer. KUB also has 14 transport customers who purchase gas directly from a supplier other than KUB. KUB provides transportation service on its gas distribution system to those customers.

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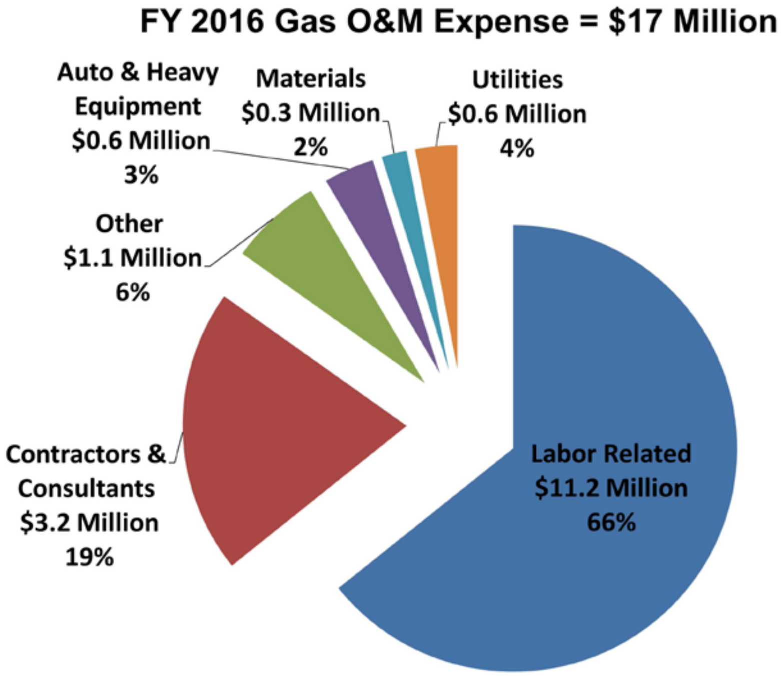
Operating Expenses

Fiscal Year 2016 Compared to Fiscal Year 2015

Operating expenses (excluding purchased gas expense) increased $1.8 million or 5.4 percent compared to fiscal year 2015. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as distribution, customer service and administrative and general.

- Distribution system O&M expenses were $0.4 million higher than the prior fiscal year, due to an increase in labor related expenses.
- Customer service expenses were consistent with the prior fiscal year.
- Administrative and general expenses increased $0.1 million or 2.4 percent.

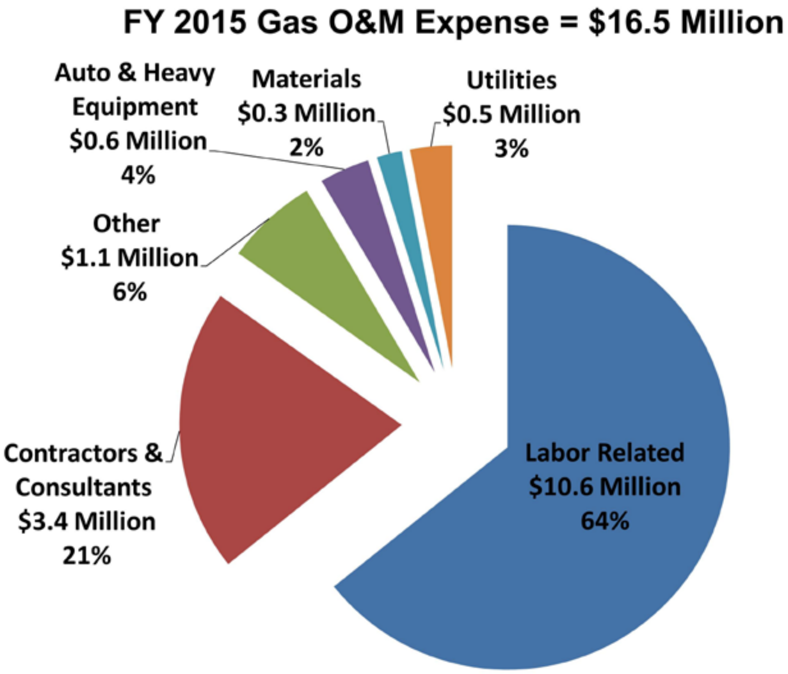


- Depreciation expense was $0.6 million higher than the prior year, primarily due to the increased depreciation on mains due to Century II replacement programs and the completion of the South Loop project.
- Taxes and tax equivalents were $0.7 million higher than the prior fiscal year due increased plant in service levels.

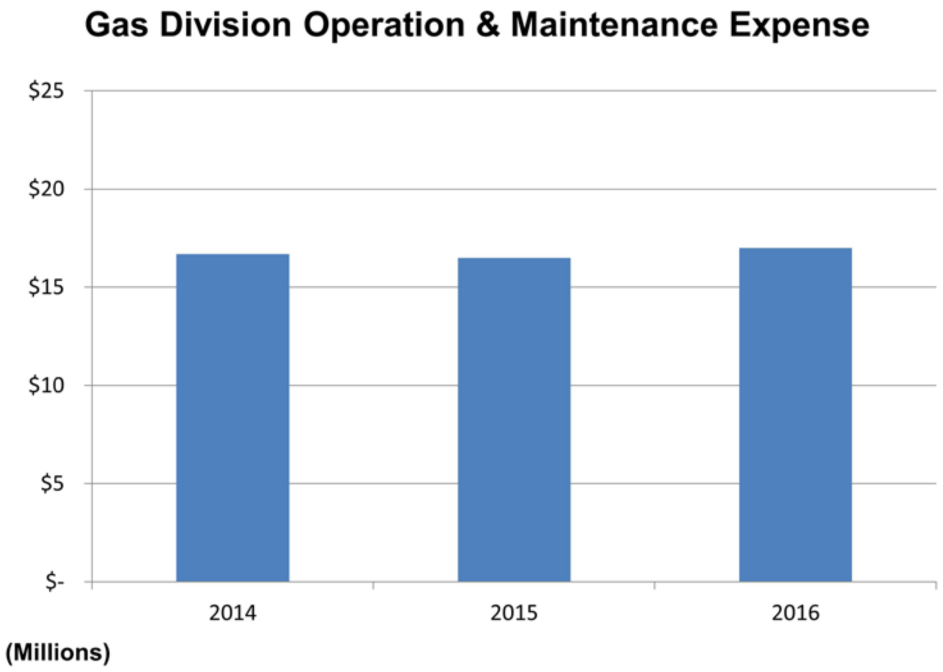
Fiscal Year 2015 Compared to Fiscal Year 2014

Operating expenses (excluding purchased gas expense) increased $1.3 million or 3.9 percent compared to fiscal year 2014. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as distribution, customer service and administrative and general.

- Distribution system operating and maintenance expenses were $0.3 million higher than the prior fiscal year, due to an increase in labor related expenses.
- Customer service expenses increased $0.1 million compared to last fiscal year.
- Administrative and general expenses decreased $0.6 million or 9.6 percent primarily due to a decrease in pension expense.



- Depreciation expense was $1.2 million higher than the prior year, the result of a full year of depreciation for $23.4 million of assets added to plant in service in fiscal year 2014 and a partial year of depreciation for $17.6 million of assets added to plant in service in fiscal year 2015. In addition, $1.8 million in assets were retired during the fiscal year.
- Taxes and tax equivalents were $0.3 million higher than the prior fiscal year due to an increase in tax equivalent payments to the City of Knoxville, Knox County, and other taxing jurisdictions. The City of Knoxville's property tax rate increased this year and higher plant in service levels contributed to the growth in tax equivalent payments.



Other Income and Expense

Fiscal Year 2016 Compared to Fiscal Year 2015

Contributions in aid of construction increased $6.6 million compared to the prior fiscal year. This was primarily due to a $4 million contribution from the University of Tennessee, representing the remaining portion of the University's contribution for the South Loop project.

Interest income was consistent with the prior fiscal year.

Interest expense decreased $0.5 million compared with the prior year, reflecting interest savings from the bond refunding in April 2015.

Other income (net) was down $0.1 million from the prior fiscal year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Contributions in aid of construction decreased $3.9 million. This was due to a $3.9 million contribution from the University of Tennessee during fiscal year 2014, representing a portion of the University's contribution for the South Loop project.

Interest income was consistent with the prior fiscal year.

Interest expense decreased $0.1 million compared with the prior year, reflecting interest savings from the bond refunding in April 2015 in addition to previous bond refundings.

Other income (net) was consistent with the prior fiscal year.

Capital Assets

Capital Assets
As of June 30
(Net of Depreciation)

(in thousands of dollars)

	2016	2015	2014
Distribution Plant			
Mains	$ 176,253	149,720	144,218
Services and Meters/Regulators	57,053	52,580	50,238
Other Accounts	845	766	901
Total Distribution Plant	234,151	$ 203,066	$ 195,357
Total General Plant	$ 8,549	7,688	8,551
Total Plant Assets	242,700	$ 210,754	$ 203,908
Work In Progress	20,831	37,278	17,464
Total Net Plant	$ 263,531	$ 248,032	$ 221,372

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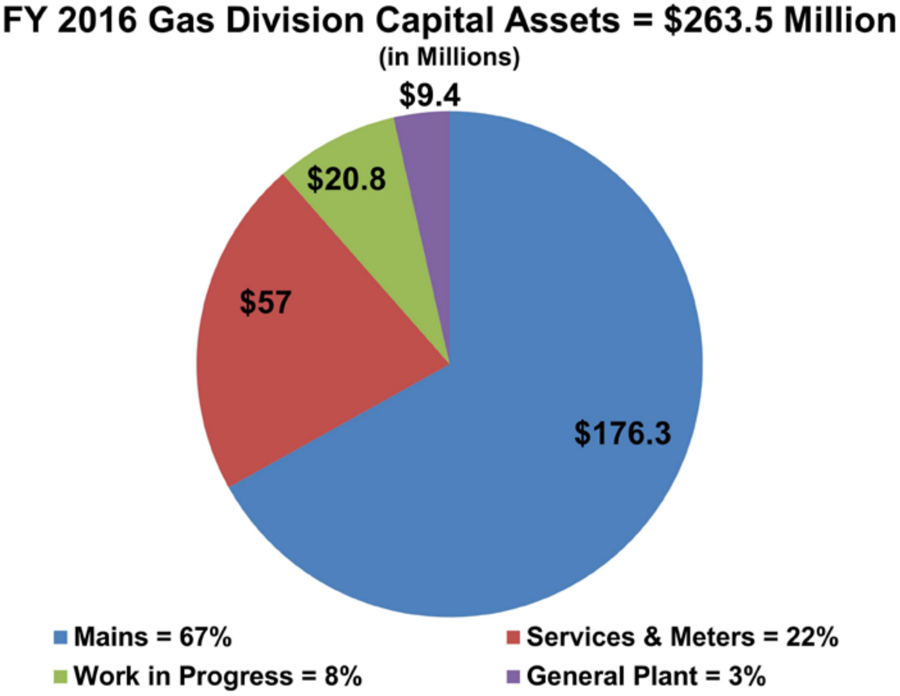
Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, the Division had $263.5 million invested in a variety of capital assets, as reflected in the schedule of capital assets, which represents a net increase (including additions, retirements, and depreciation) of $15.5 million or 6.2 percent over the end of last fiscal year.



Major capital asset expenditures during the year were as follows:

- $15.1 million for installation of new main and service extensions
    - $7.6 million for the South Loop project
- $3.9 million for main replacement
- $2.5 million for replacement and relocation of gas system assets to accommodate TDOT highway improvement projects
- $1.4 million for upgrades to various information systems

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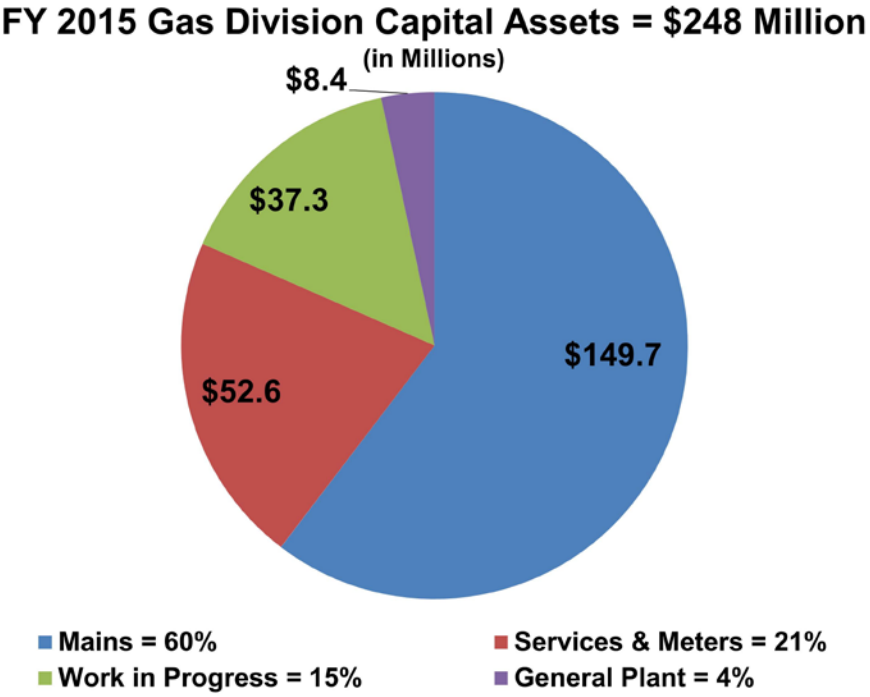
Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, the Division had $248 million invested in a variety of capital assets, as reflected in the schedule of capital assets, which represents a net increase (including additions, retirements, and depreciation) of $26.7 million or 12 percent over the end of last fiscal year.



Major capital asset expenditures during the year were as follows:

- $24.2 million for installation of new main and service extensions
- $6 million for main replacement
- $1.5 million for information systems upgrades

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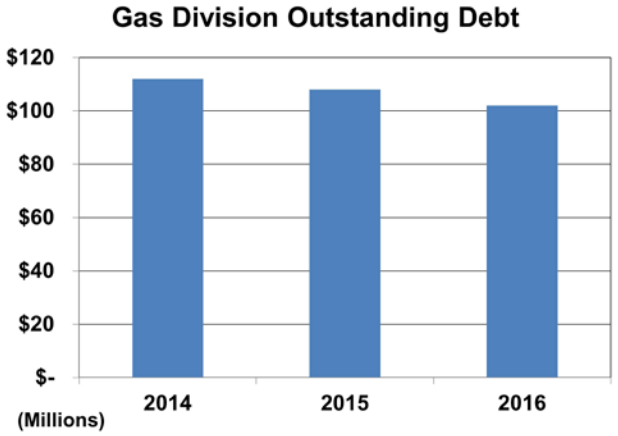
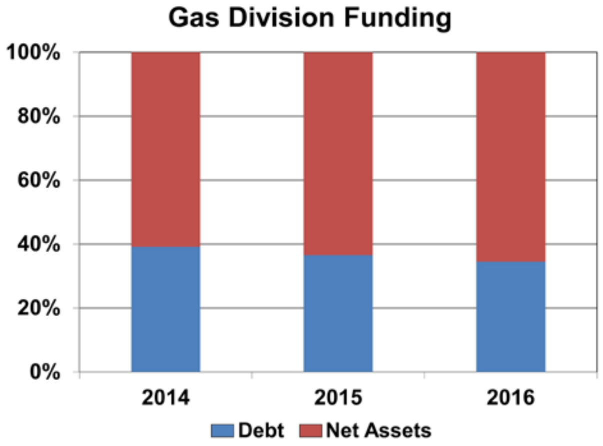
Debt Administration

As of June 30, 2016 the Gas Division had $102.1 million in outstanding gas system bonds. The bonds are secured solely by revenues of the Gas Division. Debt as a percentage of the Division’s capital structure represented 34.5 percent in 2016, 36.6 percent in 2015, and 39.2 percent at the end of fiscal year 2014. KUB’s Debt Management Policy limits the Division’s debt ratio to 60 percent or less.

Outstanding Debt
As of June 30

(in thousands of dollars)	2016	2015	2014
Revenue bonds	$ 102,125	$ 107,545	$ 112,365
Total outstanding debt	$ 102,125	$ 107,545	$ 112,365





The Division will pay $61.9 million in principal payments over the next ten years, representing 60.6 percent of the outstanding bonds. KUB’s Debt Management Policy requires a minimum of 30 percent of gas debt principal be repaid over the next ten years.

Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, the Division had $102.1 million in outstanding debt (including current portions of revenue bonds), compared to $107.5 million last year, representing a decrease of $5.4 million or 5 percent. The decrease is attributable to the scheduled repayment of bond debt. The Division’s weighted average cost of debt as of June 30, 2016 was 3.9 percent.

The Division’s outstanding debt is rated by Standard & Poor’s and Moody’s Investors Service. As of June 30, 2016, the Division’s revenue bonds were rated AA by Standard & Poor’s and Aa2 by Moody’s Investors Service.

Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, the Division had $107.5 million in outstanding debt (including current portions of revenue bonds), compared to $112.4 million last year, representing a decrease of $4.9 million or 4.3 percent. The Division’s weighted average cost of debt as of June 30, 2015 was 3.86 percent.

In April 2015, the Division issued $11.8 million in gas system revenue refunding bonds to refinance certain outstanding bonds at lower interest rates. The refunding of certain bonds at lower interest rates will provide debt service savings of $1.2 million over the life of the bonds.

The Division's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2015, the Division's revenue bonds were rated AA by Standard & Poor's and Aa2 by Moody's Investors Service.

Impacts on Future Financial Position

KUB expects to add 900 new gas customers during the course of the next fiscal year.

In June 2014, the KUB Board adopted three years of rate increases for all four Divisions to help fund the ongoing Century II infrastructure programs for each system. The first and second of three rate increases were effective October 2014 and October 2015. The remaining natural gas rate increase will be effective October 2016. Each rate increase will result in $1.8 million in additional annual gas system revenue.

KUB sold $12 million in natural gas system revenue bonds in July 2016 for the purpose of funding natural gas system capital improvements. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.78 percent.

KUB long-term debt includes $12 million of Gas Division 2010 Build America Bonds (BABs). The BABs were sold on a taxable basis with the United States Treasury providing a rebate to KUB for a percentage of the interest cost. The interest rebates were subject to federal sequestration during the fiscal year and were reduced by 6.8 percent. Any future actions by Congress may also affect the anticipated rebates for future fiscal years.

In April 2016, KUB management presented the fiscal year 2017 budget to the KUB Board of Commissioners that accommodates the projected level of capital investment for the fiscal year. Over the course of the next ten years KUB plans to spend approximately $108 million dollars on Grid Modernization, of which the Division's share is $14.2 million. In July 2016, the four-year deployment of advanced meters began.

GASB Statement No. 82, *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73* is effective for fiscal years beginning after June 15, 2016. GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* and GASB No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* are effective for periods beginning after June 15, 2017. KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

No other facts, decisions, or conditions are currently known which would have a significant impact on the Division's financial position or results of operations during fiscal year 2016.

Financial Contact

The Division's financial statements are designed to present users (citizens, customers, investors, and creditors) with a general overview of the Division's financial position and results of operations for the fiscal years ending June 30, 2016 and 2015. If you have questions about the statements or need additional financial information, contact KUB's Chief Financial Officer at 445 South Gay Street, Knoxville, Tennessee 37902.

Knoxville Utilities Board Gas Division
Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Assets and Deferred Outflows of Resources		
Current assets:		
Cash and cash equivalents	$ 11,036,149	$ 26,262,919
Short-term contingency fund investments	3,597,830	2,950,146
Other current assets	240,425	375,832
Accrued interest receivable	2,595	1,108
Accounts receivable, less allowance of uncollectible accounts of $46,630 in 2016 and $34,907 in 2015	4,440,145	5,930,278
Inventories	630,535	465,596
Gas storage	8,010,091	9,447,403
Prepaid expenses	66,013	55,502
Total current assets	28,023,783	45,488,784
Restricted assets:		
Gas bond fund	3,145,854	3,111,502
Other funds	3,641	7,901
Total restricted assets	3,149,495	3,119,403
Gas plant in service	364,632,055	324,150,132
Less accumulated depreciation	(121,932,008)	(113,395,656)
	242,700,047	210,754,476
Retirement in progress	54,370	89,960
Construction in progress	20,777,003	37,187,771
Net plant in service	263,531,420	248,032,207
Other assets:		
Net pension asset	-	1,083,893
Long-term contingency fund investments	12,754,872	12,186,218
Under recovered purchased gas costs	2,178,653	-
Other	1,569,632	1,641,273
Total other assets	16,503,157	14,911,384
Total assets	311,207,855	311,551,778
Deferred outflows of resources:		
Pension outflow	1,760,739	568,296
Unamortized bond refunding costs	1,243,933	1,357,050
Total deferred outflows of resources	3,004,672	1,925,346
Total assets and deferred outflows of resources	$ 314,212,527	$ 313,477,124

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Gas Division
Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Liabilities, Deferred Inflows, and Net Position		
Current liabilities:		
Current portion of revenue bonds	$ 5,450,000	$ 5,420,000
Sales tax collections payable	72,463	74,674
Accounts payable	4,930,035	5,321,481
Accrued expenses	1,004,924	1,005,599
Customer deposits plus accrued interest	3,677,724	3,576,615
Accrued interest on revenue bonds	1,329,087	1,318,069
Total current liabilities	16,464,233	16,716,438
Other liabilities:		
Accrued compensated absences	1,531,331	1,507,803
Customer advances for construction	984,710	718,096
Net pension liability	856,827	-
Over recovered purchased gas costs	-	1,063,761
Other	37,751	63,182
Total other liabilities	3,410,619	3,352,842
Long-term debt:		
Gas revenue bonds	96,675,000	102,125,000
Unamortized premiums/discounts	3,488,853	3,794,404
Total long-term debt	100,163,853	105,919,404
Total liabilities	120,038,705	125,988,684
Deferred inflows of resources:		
Pension inflow	257,085	1,148,096
Total deferred inflows of resources	257,085	1,148,096
Total liabilities and deferred inflows of resources	120,295,790	127,136,780
Net position		
Net investment in capital assets	159,696,458	138,973,111
Restricted for:		
Debt service	1,816,767	1,793,433
Other	3,641	7,901
Unrestricted	32,399,871	45,565,899
Total net position	193,916,737	186,340,344
Total liabilities, deferred inflows, and net position	$ 314,212,527	$ 313,477,124

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Gas Division
Statements of Revenues, Expenses and Changes in Net Position
Years Ended June 30, 2016 and 2015

	2016	2015
Operating revenues	$ 88,441,144	$ 114,168,784
Operating expenses		
Purchased gas	41,212,470	63,735,433
Distribution	8,304,516	7,922,463
Customer service	2,676,224	2,687,961
Administrative and general	5,983,853	5,842,471
Provision for depreciation	11,481,432	10,894,826
Taxes and tax equivalents	7,390,744	6,657,038
Total operating expenses	77,049,239	97,740,192
Operating income	11,391,905	16,428,592
Non-operating revenues (expenses)		
Contributions in aid of construction	7,078,153	450,281
Interest and dividend income	183,418	158,779
Interest expense	(4,104,192)	(4,642,526)
Amortization of debt costs	70,748	106,159
Write-down of plant for costs recovered through contributions	(7,078,153)	(450,281)
Other	34,514	104,921
Total non-operating revenues (expenses)	(3,815,512)	(4,272,667)
Change in net position before capital contributions	7,576,393	12,155,925
Capital contributions	-	4,353
Change in net position	7,576,393	12,160,278
Net position, beginning of year, as previously reported	186,340,344	174,317,582
Change in method of accounting for pension	-	(137,516)
Net position, beginning of year, as restated	186,340,344	174,180,066
Net position, end of year	$ 193,916,737	$ 186,340,344

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Gas Division
Statements of Cash Flows
June 30, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Cash receipts from customers	$ 89,485,188	$ 115,921,501
Cash (payments to) receipts from other operations	999,976	1,047,805
Cash payments to suppliers of goods or services	(52,432,985)	(73,855,383)
Cash payments to employees for services	(8,871,606)	(8,047,999)
Payment in lieu of taxes	(6,737,649)	(6,081,256)
Net cash provided by operating activities	22,442,924	28,984,668
Cash flows from capital and related financing activities:		
Principal paid on revenue bonds and notes payable	(5,420,000)	(5,150,000)
(Increase) decrease in unused bond proceeds	-	1,055,410
Interest paid on revenue bonds and notes payable	(4,093,173)	(4,435,230)
Acquisition and construction of gas plant	(34,428,703)	(38,191,918)
Changes in gas bond fund, restricted	(34,352)	69,391
Customer advances for construction	267,894	178,113
Proceeds received on disposal of plant	1,028	-
Cash received from developers and individuals for capital purposes	7,078,153	450,281
Net cash used in capital and related financing activities	(36,629,153)	(46,023,953)
Cash flows from investing activities:		
Changes in deposit and investment accounts:		
Purchase of investment securities	(4,099,811)	(3,282,494)
Maturities of investment securities	2,949,225	2,277,167
Interest received	181,931	159,691
Other property and investments	(71,886)	133,629
Net cash provided by (used in) investing activities	(1,040,541)	(712,007)
Net increase (decrease) in cash and cash equivalents	(15,226,770)	(17,751,292)
Cash and cash equivalents, beginning of year	26,262,919	44,014,211
Cash and cash equivalents, end of year	$ 11,036,149	$ 26,262,919
Reconciliation of operating income to net cash provided by operating activities		
Operating income	$ 11,391,905	$ 16,428,592
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	11,709,804	11,083,056
Changes in operating assets and liabilities:		
Accounts receivable	1,490,134	2,315,045
Inventories	(164,939)	(90,138)
Prepaid expenses	1,426,802	844,387
Other assets	89,621	(145,258)
Sales tax collections payable	(2,211)	(8,986)
Accounts payable and accrued expenses	(331,456)	(1,396,187)
Underrecovered gas costs	(3,242,414)	(214,383)
Customer deposits plus accrued interest	101,109	120,482
Other liabilities	(25,431)	48,058
Net cash provided by operating activities	$ 22,442,924	$ 28,984,668
Noncash capital activities:		
Acquisition of plant assets through developer contributions	$ -	$ 4,353

The accompanying notes are an integral part of these financial statements.

1. Description of Business

Knoxville Utilities Board (KUB), comprised of Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions including setting rates. The Gas Division (Division) provides services to certain customers in Knox County and in two surrounding counties in East Tennessee. The Division's accounts are maintained in conformity with the Uniform System of Accounts of the Federal Energy Regulatory Commission (FERC) and the Governmental Accounting Standards Board (GASB), as applicable. The financial statements present only the Gas Division and do not purport to, and do not, present fairly the consolidated financial position of Knoxville Utilities Board at June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

2. Significant Accounting Policies

Basis of Accounting

In conformity with Generally Accepted Accounting Principles (GAAP), KUB follows the provisions of GASB Statement No. 34 (Statement No. 34), *Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* as amended by GASB Statement No. 63 (Statement No. 63), *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position.* Statement No. 34 established standards for external financial reporting for all state and local governmental entities. Under Statement No. 63, financial statements include deferred outflows of resources and deferred inflows of resources, in addition to assets and liabilities, and will report *net position* instead of net assets. In addition, KUB follows GASB Statement No. 62 (Statement No. 62), *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* as it relates to certain items for regulatory accounting. Regulatory accounting allows a regulated utility to defer a cost (a regulatory asset) or recognize an obligation (a regulatory liability) if it is probable that through the rate making process, there will be a corresponding increase or decrease in future revenues. Accordingly, KUB has recognized certain regulatory assets and regulatory liabilities in the accompanying Statements of Net Position.

The financial statements are prepared on the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred. The accounting and financial reporting treatment applied to the Division is determined by measurement focus. The transactions of the Division are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the Statement of Net Position. Net position (i.e., total assets and deferred outflows of resources net of total liabilities and deferred inflows of resources) is segregated into net investment in capital assets, restricted for capital activity and debt service, and unrestricted components.

Recently Adopted New Accounting Pronouncements

In February 2015, the Governmental Accounting Standards Board (GASB) issued Statement No. 72 (Statement No. 72), *Fair Value Measurement and Application.* Statement No. 72 is intended to provide guidance for determining a fair value measurement for financial reporting purposes and for applying fair value to certain investments and disclosures related to all fair value measurements.

In June 2015, the GASB issued GASB Statement No. 73 (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 Provision of GASB Statements 67 and 68.* The requirements of this Statement will improve financial reporting by establishing a single framework for the presentation of information about pensions and enhance comparability.

In June 2015, the GASB issued GASB Statement No. 76 (Statement No. 76), *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to simplify the hierarchy of generally accepted accounting principles (GAAP) used to prepare financial statements of state and local governmental entities. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments,* and amends Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, paragraphs 64, 74, and 82.

In December 2015, the GASB issued GASB Statement No. 79 (Statement No. 79), *Certain External Investment Pools and Pool Participants.* This statement establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes.

Statements No. 72, 73, 76, and 79 are effective for fiscal years beginning after June 15, 2015.

Gas Plant

Gas plant and other property are stated on the basis of original cost. The cost of current repairs and minor replacements is charged to operating expense. The cost of renewals and improvements is capitalized. The original cost of utility plant assets retired or otherwise disposed of and the cost of removal less salvage value is charged to accumulated depreciation. When other property is retired, the related asset and accumulated depreciation are removed from the accounts, and the gain or loss is included in the results of operations.

The provision for depreciation of gas plant in service is based on the estimated useful lives of the assets, which range from three to thirty-three years, and is computed using the straight-line method. Pursuant to FERC, the caption "Provision for depreciation" in the Statements of Revenues, Expenses and Changes in Net Position does not include depreciation for transportation equipment of $228,372 in fiscal year 2016 and $188,229 in fiscal year 2015. Under regulatory accounting, interest costs are expensed as incurred with construction of plant assets.

Operating Revenue

Operating revenue consists primarily of charges for services provided by the principal operations of the KUB Gas Division. Operating revenue is recorded when the service is rendered, on a cycle basis, and includes an estimate of unbilled revenue. Revenues are reported net of bad debt expense of $87,712 in fiscal year 2016 and $134,460 in fiscal year 2015.

Non-operating Revenue

Non-operating revenue consists of revenues that are related to financing and investing types of activities and result from non-exchange transactions or ancillary activities.

Expense

When an expense is incurred for purposes for which there are both restricted and unrestricted net assets available, it is KUB's policy to apply those expenses to restricted net assets to the extent such are available and then to unrestricted net assets.

Net Position

GASB Statement No. 63 requires the classification of net position into three components – net investment in capital assets; net position-restricted; and net position-unrestricted.

These classifications are defined as follows:

- Net investment in capital assets – This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt also should be included in this component of net position. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

- Net position-restricted – This component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported.

- Net position-unrestricted – This component of net position consists of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

Contributions in Aid of Construction and Capital Contributions

Contributions in aid of construction are cash collections from customers or others for a particular purpose, generally the construction of new facilities to serve new customers in excess of the investment KUB is willing to make for a particular incremental revenue source. KUB reduces the plant account balances to which contributions relate by the actual amount of the contribution and recognizes the contributions as non-operating revenue in accordance with Statement No. 62.

Capital contributions represent contributions of utility plant infrastructure constructed by developers and others in industrial parks and other developments, and transferred to KUB upon completion of construction and the initiation of utility service. In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, such contributions are recognized as revenues and capital assets upon receipt.

Inventories

Inventories, consisting of plant materials and operating supplies, are valued at the lower of average cost or replacement value.

Change in Method of Accounting for Pension

In June 2012, the Governmental Accounting Standards Board (GASB) issued Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, which revises existing standards of financial reporting for pensions. In addition, during November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, which requires deferred outflow of resources to be recognized for any contributions made subsequent to the measurement date of the beginning net pension liability. These standards were adopted by KUB in 2015 and resulted in a restatement of 2015 beginning net position of $763,975 (Division's share $137,516).

Pension Plan

KUB's employees are participants in the Knoxville Utilities Board Pension Plan as authorized by the Charter of the City of Knoxville §1107(J) (Note 10). KUB's policy is to fully fund the annual actuarially determined contributions. As required by GASB Statement No. 68, KUB measures net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30, 2016 and 2015 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 are based on a December 31, 2015 and 2014 measurement date, respectively.

Investments

Investments are carried at fair value as determined by quoted market prices at the reporting date.

Self-Insurance

KUB has established self-insurance programs covering portions of workers' compensation, employee health, environmental liability, general liability, property and casualty liability, and automobile liability claims. A liability is accrued for claims as they are incurred. When applicable, claims in excess of the self-insured risk are covered by KUB's insurance carrier. Additionally, KUB provides certain lifetime health benefits to eligible retired employees under a self-insurance plan administered by a third party.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates are based on historical experience and various other assumptions that KUB believes are reasonable under the circumstances. However, future events are subject to change and the best estimates and judgments routinely require adjustment. Estimates are used for, but not limited to, inventory valuation, allowance for uncollectible accounts, depreciable lives of plant assets, unbilled revenue volumes, pension trust valuations, OPEB trust valuations, insurance liability reserves, and potential losses from contingencies and litigation. Actual results could differ from those estimates.

Restricted and Designated Assets

Certain assets are restricted by bond resolutions for the construction of utility plant and debt repayment. Certain additional assets are designated by management for contingency purposes and economic development.

Cash Equivalents

For purposes of the Statements of Cash Flows, KUB considers all unrestricted and undesignated highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

Deferred Outflows and Inflows of Resources

Deferred outflows of resources are items previously reported as assets related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. Deferred inflows of resources are items previously reported as liabilities related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. Deferred outflows of resources also include employer pension contributions made subsequent to the measurement date of the net pension liability and before the end of the employer's reporting period in accordance with Statement No. 71. Deferred inflows and deferred outflows also include the net difference between projected and actual earnings on pension plan

investments and differences between expected and actual experience in accordance with Statement No. 68.

Debt Premium/Discount

KUB records unamortized premium and discount on debt as a separate line item in the Long Term Debt section of the Financial Statements. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Debt Issuance Costs

In accordance with regulatory accounting, KUB records debt issuance costs as an Other Asset. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Deferred Gain/Loss on Refunding of Debt

KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. In accordance with FERC presentation, amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Compensated Absences

KUB accrues a liability for earned but unpaid paid-time off (PTO) days.

Subsequent Events

KUB has evaluated events and transactions through October 27, 2016, the date these financial statements were issued, for items that should potentially be recognized or disclosed. KUB sold $12 million in natural gas system revenue bonds in July 2016 for the purpose of funding natural gas system capital improvements in fiscal year 2017. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.78 percent.

Purchased Gas Adjustment

In November 1990, the Board implemented a deferred Purchased Gas (Cost) Adjustment (PGA) mechanism, which allows KUB to flow changes in purchased gas costs through to its customers. These changes in gas costs are reflected as adjustments to the base gas rates established by the Board. The rate-setting authority vested in the Board by the City Charter meets the “self-regulated” provisions of GASB Statement No. 62 (Statement No. 62), *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*.

The PGA is intended to assure that KUB recovers the total cost of natural gas purchased, transported and/or reserved for delivery to its sales and transportation customers on an equitable basis. The PGA is also intended to assure that no excess or deficient cost recovery from KUB’s customers occurs.

Under the PGA mechanism, KUB tracks the actual over/(under) recovered amount in the Over/(Under) Recovered Purchased Gas Costs accounts. These accounts are rolled into the PGA rate adjustment on June 30 of each year thereby assuring that any over/(under) recovered amounts are passed on to KUB’s gas system customers. The amount of over/(under) recovered cost was ($2,178,653) at June 30, 2016 and $1,063,761 at June 30, 2015.

Recently Issued Accounting Pronouncements

In June 2015, the GASB issued two related Statements that affect accounting and financial reporting by state and local governments for postemployment benefits other than pensions (OPEB). GASB Statement No. 74 (Statement No. 74), *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* addresses reporting by OPEB plans that administer benefits on behalf of governments. GASB Statement No. 75 (Statement No. 75), *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* addresses reporting by governments that provide OPEB to their employees. Statement No. 74 is effective for fiscal years beginning after June 15, 2016, and Statement No. 75 is effective for fiscal years beginning after June 15, 2017.

In March 2016, the GASB issued GASB Statement No. 82 (Statement No. 82), *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to the presentation of payroll-related measures in required supplementary information, the selection of assumptions and treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes and the classification of payments made by employers to satisfy employee contribution obligations. Statement No. 82 is effective for fiscal years beginning after June 15, 2016.

KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

3. Deposits and Investments

KUB follows the provisions of Statement No. 40 of the Governmental Accounting Standards Board, *Deposit and Investment Risk Disclosures an amendment of GASB Statement No. 3*. This Statement establishes and modifies disclosure requirements for state and local governments related to deposit and investment risks. KUB classifies its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*.

KUB’s investment policy provides the framework for the administration and investment of cash deposits. The investment policy follows Tennessee State law and defines the parameters under which KUB funds should be invested. State law authorizes KUB to invest in obligations of the United States Treasury, its agencies and instrumentalities; certificates of deposit; repurchase agreements; money market funds; and the State Treasurer's Investment Pool.

Interest Rate Risk. KUB’s primary investment objectives are to place investments in a manner to ensure the preservation of capital, remain sufficiently liquid to meet all operating requirements, and maximize yield of return. KUB minimizes its exposure to interest rate risk by adhering to Tennessee State law requirements for the investment of public funds. This includes limiting investments to those types described above and limiting maturity horizons. The maximum maturity is four years from the date of investment. KUB also limits its exposure by holding investments to maturity unless cash flow requirements dictate otherwise.

Credit Risk. KUB’s investment policy, as required by state law, is to apply the prudent-person rule: Investments are made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable income to be derived, as well as the probable safety of their capital. KUB’s Agency Bond investments are rated Aaa by Moody’s Investors Service.

Custodial Credit Risk. KUB’s investment policy limits exposure to custodial credit risk by restricting investments to a standard set forth by State law. All deposits in excess of federal depository insurance limits are collateralized with government securities held in KUB's name by a third-party custodian bank(s) acting as KUB's agent(s), or through the State of Tennessee's collateral pool. Financial institutions that participate in the collateral pool are subject to special assessment; therefore, the deposits are considered insured. A portion of KUB’s investments are generally held in the State of Tennessee Local Government Investment Pool (LGIP). The LGIP is a part of the

State Pooled Investment Fund and is sponsored by the State of Tennessee Treasury Department. Tennessee Code Annotated ¶9-4-701 *et seq*. authorizes local governments to invest in the LGIP. None of KUB's investments are exposed to custodial credit risk.

Classification of deposits and investments per Statement of Net Position:

	2016	**2015**
Current assets		
Cash and cash equivalents	$ 11,036,149	$ 26,262,919
Short-term contingency fund investments	3,597,830	2,950,146
Other assets		
Long-term contingency fund investments	12,712,792	12,150,457
Restricted assets		
Gas bond fund	3,145,854	3,111,502
Other funds	3,641	7,901
	$ 30,496,266	$ 44,482,925

The above amounts do not include accrued interest of $42,080 in fiscal year 2016 and $35,761 in fiscal year 2015. Interest income is recorded on an accrual basis.

Investments and maturities of KUB's deposits and investments as held by financial institutions as of June 30, 2016:

	Deposit and Investment Maturities (in Years)		
	Fair Value	**Less Than 1**	**1-5**
Supersweep NOW and Other Deposits	$ 17,314,876	$ 17,314,876	$ -
State Treasurer's Investment Pool	1,118,710	1,118,710	-
Agency Bonds	15,863,747	3,597,830	12,265,917
Certificates of Deposits	2,473,919	2,027,044	446,875
	$ 36,771,252	$ 24,058,460	$ 12,712,792

KUB categorizes its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*. The hierarchy is based on the valuation inputs used to measure the fair value of an asset with a maturity at purchase greater than one year. 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.

KUB has the following recurring fair value measurements as of June 30, 2016:

- U.S. Agency bonds of $12,265,917, which have a maturity at purchase of greater than one year, are valued using quoted market prices (Level 1 inputs)
- Certificates of deposits of $446,875, which have a maturity at purchase of greater than one year, are valued at interest rates and yield curves observable at commonly quoted intervals (Level 2 inputs)

KUB measures investments with a maturity at purchase of one year or less at amortized cost, which is considered a fair value equivalent due to their nature. Investments in the State Treasurer's Investment Pool are measured at net asset value (NAV) per share.

4. Accounts Receivable

Accounts receivable consists of the following:

	2016	2015
Wholesale and retail customers		
Billed services	$ 3,122,483	$ 4,610,243
Unbilled services	1,113,275	1,121,876
Other	251,017	233,066
Allowance for uncollectible accounts	(46,630)	(34,907)
	$ 4,440,145	$ 5,930,278

5. Accounts Payable and Accruals

Accounts payable and accruals were composed of the following:

	2016	2015
Trade accounts	$ 4,930,035	$ 5,321,481
Salaries and wages	334,914	219,134
Self-insurance liabilities	300,161	306,714
Other current liabilities	369,849	479,751
	$ 5,934,959	$ 6,327,080

6. Long-Term Obligations

Long-term debt consists of the following:

	Balance June 30, 2015	Additions	Payments	Defeased	Balance June 30, 2016	Amounts Due Within One Year
L-2005 - 3.0 - 4.75%	$ 10,715,000	$ -	$ 695,000	$ -	$ 10,020,000	$ 725,000
N-2007 - 4.0 - 5.0%	550,000	-	-	-	550,000	550,000
O-2010 - 2.0 - 3.0%	3,475,000	-	3,475,000	-	-	-
P-2010 - 3.3 - 6.2%	12,000,000	-	-	-	12,000,000	540,000
Q-2012 - 2.0 - 4.0%	23,345,000	-	700,000	-	22,645,000	2,065,000
R-2012 - 2.0 - 4.0%	9,600,000	-	200,000	-	9,400,000	400,000
S-2013 - 2.0 - 4.0%	11,480,000	-	50,000	-	11,430,000	570,000
T-2013 - 2.0 - 4.6%	24,600,000	-	200,000	-	24,400,000	500,000
U-2015 - 2.0 - 3.5%	11,780,000	-	100,000	-	11,680,000	100,000
Total bonds	$ 107,545,000	$ -	$ 5,420,000	$ -	$ 102,125,000	$ 5,450,000
Unamortized Premium	3,794,404	-	305,551	-	3,488,853	-
Total long term debt	$ 111,339,404	$ -	$ 5,725,551	$ -	$ 105,613,853	$ 5,450,000

	Balance June 30, 2014	Additions	Payments	Defeased	Balance June 30, 2015	Amounts Due Within One Year
L-2005 - 3.0 - 4.75%	$ 11,380,000	$ -	$ 665,000	$ -	$ 10,715,000	$ 695,000
N-2007 - 4.0 - 5.0%	12,000,000	-	-	11,450,000	550,000	-
O-2010 - 2.0 - 3.0%	6,825,000	-	3,350,000	-	3,475,000	3,475,000
P-2010 - 3.3 - 6.2%	12,000,000	-	-	-	12,000,000	-
Q-2012 - 2.0 - 4.0%	24,030,000	-	685,000	-	23,345,000	700,000
R-2012 - 2.0 - 4.0%	9,800,000	-	200,000	-	9,600,000	200,000
S-2013 - 2.0 - 4.0%	11,530,000	-	50,000	-	11,480,000	50,000
T-2013 - 2.0 - 4.6%	24,800,000	-	200,000	-	24,600,000	200,000
U-2015 - 2.0 - 3.5%	-	11,780,000	-	-	11,780,000	100,000
Total bonds	$ 112,365,000	$ 11,780,000	$ 5,150,000	$ 11,450,000	$ 107,545,000	$ 5,420,000
Unamortized Premium	3,434,514	701,501	296,934	44,677	3,794,404	-
Total long term debt	$ 115,799,514	$ 12,481,501	$ 5,446,934	$ 11,494,677	$ 111,339,404	$ 5,420,000

Debt service over remaining term of the debt is as follows:

Fiscal Year	**Principal**	**Total Interest**	**Grand Total**
2017	$ 5,450,000	$ 3,987,262	$ 9,437,262
2018	5,590,000	3,793,753	9,383,753
2019	5,780,000	3,599,143	9,379,143
2020	5,985,000	3,390,981	9,375,981
2021	6,240,000	3,137,531	9,377,531
2022 - 2026	32,840,000	11,816,353	44,656,353
2027 - 2031	29,565,000	5,769,511	35,334,511
2032 - 2036	10,675,000	1,074,950	11,749,950
Total	$ 102,125,000	$ 36,569,484	$ 138,694,484

The Division has pledged sufficient revenue, after deduction of all current operating expenses (exclusive of tax equivalents), to meet bond principal and interest payments when due. The requirements for the bonds are being met through monthly deposits to the Gas Bond Fund, as required by the bond covenants. As of June 30, 2016, these bond covenant requirements had been satisfied.

During fiscal year 2006, KUB's Gas Division issued Series L 2005 bonds to retire certain existing debt and fund gas system capital improvements. Concurrent with the issuance of these bonds, KUB transferred funds to an irrevocable trust to pay a portion of the Series J 2001 bonds, as such amounts mature.

During fiscal year 2008, KUB's Gas Division issued Series N 2007 bonds to fund gas system capital improvements.

During fiscal year 2011, KUB's Gas Division issued Series P 2010 bonds to fund gas system capital improvements. These bonds were issued as federally taxable Build America Bonds with a 35 percent interest payment rebate to be received from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8 percent reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change.

During fiscal year 2012, KUB's Gas Division issued Series Q 2012 bonds to retire Series K 2004 bonds.

During fiscal year 2013, KUB's Gas Division issued Series R 2012 bonds to fund gas system capital improvements. KUB's Gas Division also issued Series S 2013 bonds to retire Series M 2006 outstanding bonds.

During fiscal year 2014, KUB's Gas Division issued Series T 2013 to fund gas system capital improvements.

During fiscal year 2015, KUB's Gas Division issued Series U 2015 bonds to retire a portion of Series N 2007 outstanding bonds.

In prior years, certain revenue bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the liability for the defeased bonds, $11.5 million at June 30, 2016, and the trust account assets are not included in the financial statements.

Other liabilities consist of the following:

	Balance June 30, 2015	**Increase**	**Decrease**	**Balance June 30, 2016**
Accrued compensated absences	$ 1,507,803	$ 2,799,906	$ (2,776,378)	$ 1,531,331
Customer advances for construction	718,096	655,313	(388,699)	984,710
Other	63,182	53,012	(78,443)	37,751
	$ 2,289,081	$ 3,508,231	$ (3,243,520)	$ 2,553,792

7. Lease Commitments

KUB has non-cancelable operating lease commitments for office equipment, property, and vehicles, summarized for the following fiscal years:

2017	$ 52,460
2018	49,913
2019	29,271
2020	1,392
Total operating minimum lease payments	$ 133,036

8. Capital Assets

Capital asset activity was as follows:

	Balance June 30, 2015	**Increase**	**Decrease**	**Balance June 30, 2016**
Production Plant	$ 14,640	$ -	$ -	$ 14,640
Distribution Plant				
Mains	215,234,641	33,590,164	(922,731)	247,902,074
Services and Meters/Regulators	82,397,049	6,978,966	(1,893,978)	87,482,037
Other Accounts	1,330,905	103,742	(6,000)	1,428,647
Total Distribution Plant	$ 298,962,595	$ 40,672,872	$ (2,822,709)	$ 336,812,758
Total General Plant	25,172,897	2,899,368	(267,608)	27,804,657
Total Plant Assets	$ 324,150,132	$ 43,572,240	$ (3,090,317)	$ 364,632,055
Less Accumulated Depreciation	(113,395,656)	(11,798,907)	3,262,555	(121,932,008)
Net Plant Assets	$ 210,754,476	$ 31,773,333	$ 172,238	$ 242,700,047
Work In Progress	37,277,731	29,759,691	(46,206,049)	20,831,373
Total Net Plant	$ 248,032,207	$ 61,533,024	$ (46,033,811)	$ 263,531,420

	Balance June 30, 2014	Increase	Decrease	Balance June 30, 2015
Production Plant	$ 14,640	$ -	$ -	$ 14,640
Distribution Plant				
Mains	203,808,024	11,750,358	(323,741)	215,234,641
Services and Meters/Regulators	79,129,896	4,351,598	(1,084,445)	82,397,049
Other	1,493,396	2,585	(165,076)	1,330,905
Total Distribution Plant	$ 284,431,316	$ 16,104,541	$ (1,573,262)	$ 298,962,595
Total General Plant	23,929,959	1,450,671	(207,733)	25,172,897
Total Plant Assets	$ 308,375,915	$ 17,555,212	$ (1,780,995)	$ 324,150,132
Less Accumulated Depreciation	(104,468,506)	(11,064,683)	2,137,533	(113,395,656)
Net Plant Assets	$ 203,907,409	$ 6,490,529	$ 356,538	$ 210,754,476
Work In Progress	17,464,141	36,852,089	(17,038,499)	37,277,731
Total Net Plant	$ 221,371,550	$ 43,342,618	$ (16,681,961)	$ 248,032,207

9. Risk Management

KUB is exposed to various risks of loss related to active and retiree medical claims; injuries to workers; theft of, damage to, and destruction of assets; environmental damages; and natural disasters. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported.

These liabilities are included in accrued expenses in the Statement of Net Position. The liability is KUB's best estimate based on available information. At June 30, 2016 and 2015, the amount of these liabilities was $300,161 and $306,714, respectively, resulting from the following changes:

	2016	2015
Balance, beginning of year	$ 306,714	$ 298,833
Current year claims and changes in estimates	2,369,808	2,525,126
Claims payments	(2,376,361)	(2,517,245)
Balance, end of year	$ 300,161	$ 306,714

10. Pension Plan

Description of Plan

The Knoxville Utilities Board Pension Plan (the Plan) is a governmental plan as defined by the Employee Retirement Income Security Act of 1974 ("ERISA" or the "Act"), is not subject to any of the provisions of the Act, and was revised January 1, 2014 to include all prior approved amendments. The Plan is a single-employer contributory, defined benefit pension plan established by Knoxville Utilities Board ("KUB") Resolution No. 980 dated February 18, 1999, effective July 1, 1999, as authorized by the Charter of the City of Knoxville §1107(J). The Plan is designed to provide retirement, disability and death benefits to KUB employees. KUB administers the Plan through an Administrative Committee consisting of seven KUB employees that are appointed by KUB's President and CEO. Any amendments to the Plan involving costs not approved in the operating budget must be adopted by KUB's Board of Commissioners, upon recommendation by KUB's President and CEO. All other amendments to the Plan may be approved by KUB's President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The Plan issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017. For purposes of this disclosure, presentation is on a consolidated basis unless division's share is specified.

Effective January 1, 2011, KUB closed the Plan such that persons employed or re-employed by KUB on or after January 1, 2011, are not eligible to participate, but that eligible employees hired prior to January 1, 2011, who have not separated from service, shall continue as Participants and to accrue benefits under the Plan.

Participants in the Plan consisted of the following as of December 31:

	2015	**2014**
Inactive plan members:		
Terminated vested participants	39	40
Retirees and beneficiaries	628	627
Active plan members	692	725
Total	1,359	1,392

Retirement Benefits

The Plan provides three benefit arrangements for KUB participants, retirees, and beneficiaries.

The Plan provides pension benefits through the Career Equity Program ("CEP") for eligible employees hired on or after January 1, 1999, and for eligible former "City System Plan A" participants who elected CEP coverage as of July 1, 1999. The guaranteed pension benefit payable to a participant who has completed five or more years of service (or reached the normal retirement date, if earlier) upon termination of KUB employment shall be a lump sum equal to the participant's average compensation times their benefit percentage, as defined in the Plan document, or an annuity may be chosen by the participant.

In addition, the Plan provided retirement benefits through "Plan A" for former City System Plan A participants who elected not to participate in the CEP. Plan A is a closed plan and is not available to KUB employees hired after July 1, 1999. Plan A provides for early retirement benefits with 25 years of service and normal retirement benefits at age 62 or later. Benefits provided to Plan A participants include several different forms of monthly annuity payments.

The Plan also provides retirement benefits through “Plan B” for former “City System Plan B” participants. Plan B is a closed plan providing benefits to participants not covered by Social Security. Benefits provided to Plan B participants include several different forms of monthly annuity payments available to participants.

Effective January 1, 2012, KUB began to provide for additional monthly supplements, which will not be subject to cost of living adjustments, to certain former employees and surviving dependents of former employees who are eligible for and have elected coverage under the KUB retiree medical plan and are eligible for Medicare. This was done to address the loss of drug coverage under the KUB retiree medical plan and to assist such individuals in obtaining prescription drug coverage under Medicare Part D.

Contributions

Participation in Plan A requires employee contributions of 3 percent of the first $4,800 of annual earnings and 5 percent of annual earnings in excess of $4,800. Plan B participants may not make contributions to the Plan. KUB contributions are determined by the enrolled actuary of the Plan and equal the amount necessary to provide the benefits under the Plan determined by the application of accepted actuarial methods and assumptions. The method of funding shall be consistent with Plan objectives.

Plan Funding

KUB maintains a Funding Policy for the Plan in accordance with Tennessee State Law. The primary goal of the Policy is to document the method KUB has adopted to provide assurance that future KUB and employee contributions and current Plan assets will be sufficient to fund all benefits expected to be paid to current active, inactive and retired Plan participants and their beneficiaries. Per the Funding Policy, KUB fully funds its annual Actuarially Determined Contribution.

Investments

The Plan’s investments are held by State Street Bank and Trust Company (the “Trustee”). The Plan's policy in regard to the allocation of invested assets is established by the Investment Committee and approved by the KUB Board of Commissioners and may only be amended by the KUB Board of Commissioners. It is the policy of the Investment Committee to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes. The following was the Plan's adopted asset allocation policy as of December 31, 2015:

Asset Class	Target Allocation
Domestic equity – large cap	20% - 50%
Domestic equity – mid cap	0% - 15%
Domestic equity – small cap	0% - 15%
Domestic equity - convertible securities	0% - 10%
Non-U.S. equity	0% - 20%
Real estate equity	0% - 10%
Fixed income – aggregate bonds	5% - 25%
Fixed income – long-term bonds	10% - 25%
Cash and deposits	0% - 5%

Contributions of $5,669,380 and $6,314,399 for 2014 and 2013, respectively, were made during KUB’s fiscal years ending June 30, 2016 and 2015, respectively. Of these amounts, $963,795 and $1,136,592 are attributable to the Gas Division. The contribution was determined as part of the January 1, 2014 valuation using the Individual Entry Age Normal funding method. The objective under this method is to fund each participant's benefits under the Plan as payments which are level as a percentage of salary, starting on the original participation date (employment date) and continuing until the assumed retirement, termination, disability or death. The actuarial valuation for the Plan year ending December 31, 2015 resulted in an actuarially determined contribution of $4,816,913 for the fiscal year ending June 30, 2017, based on the Plan's current funding policy. The Gas Division's portion of this contribution is $818,875.

Subsequent to June 30, 2016, the actuarial valuation for the Plan year ending December 31, 2016 was completed. The actuarial valuation resulted in an actuarially determined contribution of $3,756,283 for the fiscal year ending June 30, 2018, based on the Plan's current funding policy. The Gas Division's portion of this contribution is $638,568. For the Plan year ending December 31, 2016, the Plan's actuarial funded ratio was 103.04 percent.

The actuarial valuations for the Plan years ending December 31, 2015 and 2016, which determine the actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Implementation of GASB 68

In fiscal year 2015, KUB adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27* ("GASB 68"), which requires measurement of the net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 will be based on the December 31, 2015 and 2014 measurement date, respectively. The Division's share of the net pension liability at June 30, 2016 is $856,827 and the net pension asset at June 30, 2015 is $1,083,893.

GASB 68 requires certain disclosures related to the net pension liability of the Plan as disclosed below:

	2015	**2014**
Total pension liability	$ 204,502,350	$ 202,773,764
Plan fiduciary net position	199,462,190	(208,795,394)
Plan's net pension liability (asset)	$ 5,040,160	$ (6,021,630)
Plan fiduciary net position as a percentage of the total pension liability	97.54%	102.97%

Changes in Net Pension Liability are as follows:

	Total Pension Liability (a)	Increase (Decrease) Plan Fiduciary Net Position (b)	Net Pension Liability (a) - (b)
Balances at December 31, 2014	$ 202,773,764	$ 208,795,394	$ (6,021,630)
Changes for the year:			
Service cost	4,157,062	-	4,157,062
Interest	14,812,784	-	14,812,784
Differences between Expected and Actual Experience	(1,890,334)	-	(1,890,334)
Changes of Assumptions	-	-	-
Contributions - employer	-	5,991,887	(5,991,887)
Contributions - rollovers	-	482,060	(482,060)
Contributions - member	-	5,486	(5,486)
Net investment income	-	(64,551)	64,551
Benefit payments	(15,350,926)	(15,350,926)	-
Administrative expense	-	(397,160)	397,160
Net changes	1,728,586	(9,333,204)	11,061,790
Balances at December 31, 2015	$ 204,502,350	$ 199,462,190	$ 5,040,160

Actuarial Assumptions

The total pension liability was determined by an actuarial valuation as of December 31, 2015 and 2014, using the following actuarial assumptions, applied to all periods included in the measurement:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.80% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the January 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation
Inflation	2.8 percent

The actuarial assumptions used in the December 31, 2015 valuation were based on the results of an actuarial experience study for the period January 1, 2009 through December 31, 2013.

The long-term expected rate of return on Plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of Plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the Plan's target asset allocation as of December 31, 2015 and 2015 are summarized in the following table. The real rate of return reported for fixed income is for aggregate fixed income. The Plan has both aggregate and long duration fixed income.

	Long Term Expected Real Rate of Return	
Asset Class	**2015**	**2014**
Domestic equity	7.2%	6.0%
Non-U.S. equity	7.4%	7.0%
Real estate equity	6.5%	5.7%
Fixed income	3.7%	1.8%
Cash and deposits	2.6%	0.5%

Discount rate

The discount rate used to measure the total pension liability was 7.5 percent as of January 1, 2015 and 2014. The projection of cash flows used to determine the discount rate assumed that participant contributions will be made at the current contribution rate and that KUB contributions will be made at rates equal to the actuarially determined contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the net pension liability to changes in the discount rate

The following presents the net pension liability of the Plan as of December 31, 2015, calculated using the discount rate of 7.5 percent, as well as what the Plan's net pension liability would be if it were calculated using a discount rate that is one percent lower (6.5 percent) or one percent higher (8.5 percent) than the current rate:

	1% Decrease (6.5%)	**Current Discount Rate (7.5%)**	**1% Increase (8.5%)**
Plan's net pension liability	$ 17,128,897	$ 5,040,160	$ (5,963,331)

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

For the year ended June 30, 2015, KUB recognized pension expense of $2,749,905 (Division's share $494,983).

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in expense over the average expected remaining service life of all active and inactive members. As of the measurement date, this recognition period was 3.72 years. However, there were no experience gains or losses, and there were no assumption changes during the measurement year.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment gain of $7,972,887. $1,594,577 of that gain was recognized in the current year and an identical amount will be recognized in each of the next four years, resulting in a deferred inflow of resources of $6,378,310 (Division's share $1,148,096). The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over the next five years. In addition, KUB recorded a deferred outflow of resources of $3,157,199 (Division's share $568,296) at June 30, 2015 for employer contributions made between December 31, 2014 and June 30, 2015.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ -
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	-	6,378,310
Contributions subsequent to measurement date	3,157,199	-
Total	$ 3,157,199	$ 6,378,310

For the year ended June 30, 2016, KUB recognized pension expense of $4,665,035 (Division's share $793,056).

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in the pension expense over the average expected remaining service life of all active and inactive members, determined as of the beginning of the measurement period. As of December 31, 2014, this average was 5.00 years. During the measurement year, there were no assumption or benefit changes. There was an experience gain of $1,890,334 with $378,067 of that recognized in the current year and in each of the next four years.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment loss of $15,382,915. $3,076,583 of that loss was recognized in the current year and an identical amount will be recognized in each of the next four years. Unrecognized investment gains from prior periods were $6,378,310 of which $1,594,577 was recognized as a reduction in pension expense in the current year.

Experience gains this year created a deferred inflow of resources of $1,512,267 (Division's share $257,085). The combination of unrecognized investment losses this year along with unrecognized net investment gains from prior periods results in a deferred outflow of resources as of December 31, 2015 of $7,522,599 (Division's share $1,278,842). The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over future years. In addition, KUB recorded a deferred outflow of resources of $2,834,692 (Division's share $481,897) at June 30, 2016 for employer contributions made between December 31, 2015 and June 30, 2016.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ 1,512,267
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	7,522,599	-
Contributions subsequent to measurement date	2,834,692	-
Total	$ 10,357,291	$ 1,512,267

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

Year ended June 30:	
2017	$ 3,938,630
2018	1,103,939
2019	1,103,938
2020	2,698,517
Thereafter	-

11. Defined Contribution Plan

The KUB Asset Accumulation 401(k) Plan (the “401(k) Plan”) is a defined contribution 401(k) employee retirement savings plan covering eligible KUB employees established by the KUB Board of Commissioners in accordance with the Charter of the City of Knoxville, Tennessee. The 401 (k) Plan’s assets are held in trust under an agreement between KUB and Fidelity Management Trust Company. Employees hired prior to January 1, 2011 may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. Employees hired on or after January 1, 2011 have an enhanced 401(k) due to the closure of the Defined Benefit Pension Plan. They may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. They also receive a nonelective KUB contribution of from 3 percent to 6 percent, depending on years of service, whether they contribute or not.

Matching contributions were previously remitted to the KUB Pension Plan (a separate defined benefit plan) in the name of the participant for employees hired prior to January 1, 2011. As of December 9, 2015, these Pension match assets moved from the KUB Pension Plan to the 401(k) Plan. Effective December 9, 2015, all matching contributions are remitted to the 401(k) Plan. The match and nonelective contributions for employees hired on or after January 1, 2011 are paid directly by KUB. KUB funded 401(k) matching contributions and nonelective contributions of $1,739,057 (Division’s share $295,640) and $1,593,350 (Division’s share $286,803), respectively, for the years ended June 30, 2016 and 2015.

12. Other Post-Employment Benefits (OPEB)

The Governmental Accounting Standards Board (GASB) established standards for the measurement, recognition, and reporting of other post-employment benefits (OPEB). OPEB includes post-employment benefits other than pension, which, for KUB, is presently limited to post-employment health care. GASB Statement No. 45 (Statement No. 45) requires the recognition of the accrued OPEB liability for the respective year, plus the disclosure of the total unfunded liability.

KUB currently provides post-employment health care benefits to 585 former employees and 593 covered dependents. The cost of coverage is shared with retirees and beneficiaries. KUB recognizes its share of the cost of post-employment health care benefits as an expense as claims are paid.

KUB amended its Group Health Plan in 1999, eliminating post-employment health care benefits for all employees hired on or after July 1, 1999. As of June 30, 2016, 356 active employees were eligible for individual and dependent coverage at separation. To qualify, the employee must meet the Rule of 80 (age plus years of service) with a minimum of 20 years of service, and be enrolled in medical coverage on their last day.

In May 2006, the State of Tennessee adopted Tennessee Code Annotated, Title 8, Chapter 50, Part 12 authorizing governmental entities to establish Trusts for the purpose of pre-funding their respective OPEB liabilities.

Although Statement No. 45 does not require pre-funding of the liability, KUB has determined that it is in the long-term economic interest of KUB and its ratepayers to establish a Trust to pre-fund KUB’s OPEB liability.

Knoxville Utilities Board Other Post-Employment Benefits Trust (the “Trust”) is a single-employer Other Post-Employment Benefits Plan established by the Knoxville Utilities Board (KUB) Board of Commissioners through Resolution No. 1168, as amended, dated October 18, 2007. The applicable documentation was submitted to the State Funding Board and, in December 2007, the State Funding Board approved the Trust. The Trust was also approved by the Internal Revenue Service in June 2008. KUB administers the Trust through a Board of Trustees consisting of seven KUB employees that are appointed by KUB's President and CEO. Any amendments to the Trust involving costs not approved in the operating budget must be approved by KUB's Board of Commissioners, upon recommendation by KUB's President and CEO. All other amendments to the Trust may be approved by KUB's President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The investment of all deposits to the Trust is governed by an Investment Policy, which was adopted by the KUB Board and approved by the State Funding Board.

KUB makes annual contributions to the Trust at an actuarially determined rate. Based on the date of retirement, certain retired plan members are required to contribute specified amounts monthly to maintain health insurance. Those who retired prior to July 1983 have no required monthly premiums for themselves or dependents. The retirees, or their surviving dependents, who retired between August 1983 and January 1998 are required to pay $250 per month for pre-Medicare family health insurance. For individuals who retired after January 1998, the required monthly premium for pre-Medicare health insurance is $250 for single coverage and $500 for family coverage. There is currently no premium for Medicare eligible retirees or dependents.

An actuarial valuation of KUB's Postretirement Benefit Plan was performed for the Trust as of January 1, 2014 for fiscal year June 30, 2015 and January 1, 2015 for fiscal year June 30, 2016. The following table presents the OPEB cost for the year, the amount contributed to the Trust, and changes in the net OPEB obligation for fiscal year ending June 30:

	2016	**2015**
a) Net OPEB Obligation/(Asset) at beginning of fiscal year	$ (174,410)	$ (177,322)
b) Annual Required Contribution (ARC)	953,221	3,497,372
c) Interest on Net OPEB Obligation/(Asset)	(13,081)	(14,186)
d) Adjustment to ARC	(16,427)	(17,098)
e) Annual OPEB Cost **(b+c-d)**	956,567	3,500,284
f) Employer Contributions	953,221	3,497,372
g) Net OPEB Obligation/(Asset) at end of fiscal year **(a+e-f)**	$ (171,064)	$ (174,410)

KUB's annual OPEB cost, the percentage of annual OPEB cost contributed to the Trust, and the net OPEB obligation for fiscal year 2016 and the two preceding years were as follows:

Schedule of Employer Contributions

Actuarial Valuation Date	**Employer Fiscal Year**	**Annual Required Contribution**	**Fiscal Year Actual Contribution**	**Percentage Contributed**	**Net OPEB Obligation**
1/1/2012	6/30/2014	3,327,412	4,057,091	121.93%	(177,322)
1/1/2013	6/30/2015	3,497,372	3,497,372	100.00%	(174,410)
1/1/2014	6/30/2016	953,221	953,221	100.00%	(171,064)

Total contributions to the OPEB Trust for the fiscal year ended June 30, 2016 were $953,221 (Division's share $162,048). The contribution to the Trust was consistent with the annual required contribution, as determined by the Postretirement Benefit Plan's actuarial valuation as of January 1, 2014, which was $953,221 (Division's share $162,048). As of June 30, 2016, the employer's OPEB obligation has been exceeded by $171,064 (Division's share $29,081).

The annual required contribution for the fiscal year ending June 30, 2017, as determined by the Plan's actuarial valuation as of January 1, 2015 is $620,015 (Division's share $105,403).

The actuarial valuation for the Plan as of January 1, 2016 has been completed. The valuation determined that the Plan's actuarial accrued liability was $45,118,624 (Division's share $7,670,166). The actuarial value of the Plan's assets was $48,510,796 (Division's share $8,246,835). As a result, the Plan's unfunded actuarial accrued liability was ($3,392,172) (Division's share ($576,669)). The Plan's actuarial funded ratio was 108 percent. Due to the future implementation of GASB 75, the contributions made for fiscal year ending June 30, 2018 will be the actuarially determined contribution instead of the annual required contribution and the actuarial cost method used to determine the contributions will change from the projected unit credit cost method to the entry age normal cost method. The actuarially determined contribution for fiscal year ending June 30, 2018 will be zero. See Required Supplementary Information for OPEB Schedule of Funding Progress.

The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution and actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

The required schedule of funding progress immediately following the notes to the financial statements presents multi-year trend information about whether the actuarial value of Trust assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point.

Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

Identification of actuarial methods and significant assumptions used to determine the annual required contribution for the fiscal year ending June 30, 2016:

I. Actuarial cost method	Projected unit credit cost method
II. Actuarial value of assets	Smoothed market value with phase-in method using a smoothing period of 5 years
III. Investment return	7.5%, based on the expected portfolio return
Projected salary increases	N/A
Healthcare cost Trend:	
Medicare	2014 - 2030+, ranging from 4.5% to 7.45%
Non-Medicare	2014 - 2030+, ranging from 4.5% to 8.75%
IV. Amortization method	Level dollar closed (30-year)
Remaining amortization period	22 years

The Trust issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017.

13. Related Party Transactions

The Division, in the normal course of operations, is involved in transactions with the City of Knoxville and with other divisions of KUB. Such transactions for the years ended June 30, 2016 and 2015 are summarized as follows:

	2016	2015
City of Knoxville		
Amounts billed by the Division for utilities and related services	$ 590,941	$ 750,765
Payments by the Division in lieu of property tax	3,682,642	3,251,836
Payments by the Division for services provided	94,019	74,607
Other divisions of KUB		
Amounts billed to other divisions for utilities and related services provided	246,060	321,789
Interdivisional rental expense	496,916	453,442
Amounts billed to the Division by other divisions for utilities services provided	268,957	286,315

With respect to these transactions, accounts receivable from the City of Knoxville included in the balance sheet at year end were:

	2016	2015
Accounts receivable	$ 6,644	$ 5,902

14. Natural Gas Supply Contract Commitments

For fiscal year 2016, the Gas Division hedged 67 percent of its total gas purchases via gas supply contracts. As of June 30, 2016, the Gas Division had hedged the price on approximately 20 percent of its anticipated gas purchases for fiscal year 2017.

The Gas Division contracts separately for the purchase, transportation and storage of natural gas. Purchase commitments for the next five years are as follows:

Firm obligations related to purchased gas - demand

	2017	2018	2019	2020	2021
Transportation					
Tennessee Gas Pipeline	$ 3,269,844	$ 3,269,844	$ 3,269,844	$ 1,089,948	$ -
East Tennessee Natural Gas	10,066,388	10,066,388	10,066,388	2,748,496	-
Storage					
Tennessee Gas Pipeline	1,787,976	1,787,976	1,787,976	595,992	-
East Tennessee Natural Gas	757,460	757,460	757,460	-	-
Saltville Natural Gas	1,870,560	1,548,030	580,440	435,330	-
Demand Total	$ 17,752,228	$ 17,429,698	$ 16,462,108	$ 4,869,766	$ -

Firm obligations related to purchased gas - commodity

	2017	2018	2019	2020	2021
Baseload					
Conoco	$ 5,719,700	$ -	$ -	$ -	$ -
Shell Energy	739,680	-	-	-	-
BP	6,104,693	6,181,363	5,874,650	1,801,950	-
CNX	1,709,713	1,648,048	-	-	-
Commodity Total	$ 14,273,786	$ 7,829,411	$ 5,874,650	$ 1,801,950	$ -

The total commodity values presented here are based upon firm supply obligations with each individual natural gas supplier. The firm obligations values for Conoco, Shell Energy, and BP are based upon firm supply obligations and locked prices with those suppliers. The firm obligations value for CNX is based upon firm supply obligations and the applicable four month NYMEX strip prices on June 30, 2016.

15. Other Commitments and Contingencies

In the normal course of business, there are various lawsuits pending against KUB. Management has reviewed these lawsuits with counsel, who is vigorously defending KUB's position and is of the opinion that the ultimate disposition of these matters will not have a material adverse effect on KUB's financial position, results of operations or cash flows.

Knoxville Utilities Board Gas Division
Required Supplemental Information - Schedule of Funding Progress
June 30, 2016
(Unaudited)

Other Post-Employment Benefits (OPEB)

	Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a)/(b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b)-(a)]/(c)
	January 1, 2008	$ -	$ 108,329,141	$ 108,329,141	0%	$ 31,234,509	346.8%
	January 1, 2009	14,593,487	100,726,738	86,133,251	14%	31,846,091	270.5%
	January 1, 2010	21,275,643	58,475,364	37,199,721	36%	30,069,028	123.7%
	January 1, 2011	40,749,815	64,289,254	23,539,439	63%	28,878,791	81.5%
	January 1, 2012	37,907,357	61,603,466	23,696,109	62%	28,269,123	83.8%
	January 1, 2013	38,571,803	63,341,531	24,769,728	61%	27,566,340	89.9%
	January 1, 2014	43,409,955	46,889,808	3,479,853	93%	26,724,154	13.0%
*	January 1, 2015	47,705,478	47,745,640	40,162	100%	25,816,884	0.2%
*	January 1, 2016	48,510,796	45,118,624	(3,392,172)	108%	25,243,127	(13.4%)

***** The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Knoxville Utilities Board Gas Division
Required Supplemental Information - Schedule of Changes in Net Pension Liability and Related Ratios
June 30, 2016
(Unaudited)

	Year ended December 31	
	2015	2014
Total pension liability		
Service cost	$ 4,157,062	$ 4,092,808
Interest	14,812,784	14,698,657
Differences between expected and actual experience	(1,890,334)	-
Benefit payments, including refunds of member contributions	(15,350,926)	(15,533,167)
Net change in total pension liability	1,728,586	3,258,298
Total pension liability - beginning	202,773,764	199,515,466
Total pension liability - ending (a)	$ 204,502,350	$ 202,773,764
Plan fiduciary net position		
Contributions - employer	$ 5,991,887	$ 5,908,541
Contributions - participants	487,546	475,854
Net investment income	(95,430)	22,292,369
Other additions	30,879	29,733
Benefit payments, including refunds of member contributions	(15,274,926)	(15,405,167)
Administrative expense	(397,160)	(378,085)
Death benefits	(76,000)	(128,000)
Net change in plan fiduciary net position**	(9,333,204)	12,795,245
Plan fiduciary net position - beginning**	208,795,394	196,000,149
Plan fiduciary net position - ending (b)**	$ 199,462,190	$ 208,795,394
Plan's net pension liability - ending (a) - (b)	$ 5,040,160	$ (6,021,630)
Plan fiduciary net position as a percentage of the total pension liability	97.54%	102.97%
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Plan's net pension liability as a percentage of covered-employee payroll	9.95%	(11.98%)

Notes to Schedule:

* Information not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented in 2014.

** Excludes amounts related to 401(k) matching contributions.

Knoxville Utilities Board Gas Division
Required Supplemental Information - Schedule of Employer Pension Contributions
June 30, 2016
(Unaudited)

	Year ended December 31 2015	2014
Annual required contribution	$ 5,991,887	$ 5,908,541
Contribution in relation to the annual required contribution	5,991,887	5,908,541
Contribution deficiency	$ -	$ -
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Contributions as a percentage of covered-employee payroll	11.82%	11.76%

Notes to Schedule:

Valuation Dates:	January 1, 2013 and January 1, 2014
Timing:	Actuarially determined contributions for a plan year are based upon 50% of the amounts determined at the actuarial valuations for each of the two prior plan years.

Key methods and assumptions used to determine contribution rates:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014.
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.8% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the Janaury 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation.
Inflation:	2.8 percent

* Schedule of Employer Contribution information is not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented 2014.

Knoxville Utilities Board Gas Division
Supplemental Information - Schedule of Insurance in Force
June 30, 2016
(Unaudited)

Schedule 1

Insurance coverage is for KUB as a consolidated entity.

Crime
Covers losses resulting from employee dishonesty, robbery, burglary, and computer fraud. Limits of coverage - $5,000,000; $250,000 retention.

Directors’ and Officers’ Liability Insurance
Covers KUB personnel appropriately authorized to make decisions on behalf of KUB (including but not limited to Commissioners, President and CEO, Senior Vice Presidents, Vice Presidents, and Directors) for wrongful acts. Limits of coverage - $20,000,000; $1,000,000 corporate deductible, $0 individual deductible.

Employment Practices Liability
Coverage for costs related to actual or alleged employment practices violations for amounts exceeding specified amount ($500,000). Limits of coverage - $10,000,000.

Fiduciary
Covers losses resulting from wrongful acts related to KUB’s Pension, 401(k), and OPEB Trust funds. Limits of coverage - $10,000,000; $150,000 deductible.

Pollution Legal Liability
New conditions coverage for losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - $20,000,000.

Property Insurance
This coverage provides protection of KUB’s property for fire, extended coverage, vandalism and malicious mischief, and coverage on boilers and machinery. Also included are flood and earthquake damage and mechanical failure. Limits of coverage - $250,000,000 per occurrence (subject to certain sublimits); $2,500,000 deductible per occurrence.

Travel Accident
Covers losses related to employees’ business travel. Limits of coverage - $1,500,000 aggregate.

Excess Insurance for General Liability
As a government entity, KUB’s liability is limited under the Tennessee Governmental Tort Liability Act (TCA §29-20-403). KUB is self-insured for up to the first $700,000 of any accident and has insurance of $1,000,000 above this retention.

Excess Insurance for Workers’ Compensation
Covers all losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - Statutory; stop loss coverage applies for aggregate losses over $5,000,000.

Employee Health Plan Stop Loss Coverage
KUB’s employee health plan is self-funded. KUB has purchased stop loss insurance, which covers KUB’s exposure to annual expenses in excess of $400,000 per individual participant.

Knoxville Utilities Board Gas Division
Supplemental Information - Schedule of Debt Maturities by Fiscal Year
June 30, 2016
(Unaudited)

Schedule 2

Continued on Next Page

	L-2005		N-2007		P-2010			Q-2012	
FY	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**	**Rebate***	**Principal**	**Interest**
16-17	725,000	441,278	550,000	27,500	540,000	645,843	226,045	2,065,000	806,548
17-18	760,000	406,840			570,000	628,023	219,808	2,125,000	744,598
18-19	795,000	372,640			595,000	606,363	212,227	2,190,000	680,848
19-20	830,000	336,865			620,000	581,075	203,376	2,260,000	615,148
20-21	865,000	299,515			645,000	553,175	193,611	2,350,000	524,748
21-22	910,000	260,590			670,000	521,731	182,606	2,445,000	430,748
22-23	945,000	223,053			695,000	488,231	170,881	2,540,000	332,948
23-24	980,000	182,890			725,000	453,481	158,718	2,645,000	231,348
24-25	1,025,000	141,240			750,000	413,606	144,762	760,000	125,548
25-26	1,065,000	96,140			785,000	372,358	130,325	780,000	102,748
26-27	1,120,000	49,280			815,000	328,200	114,870	800,000	79,348
27-28					845,000	279,300	97,755	830,000	54,348
28-29					880,000	228,600	80,010	855,000	27,788
29-30					915,000	175,800	61,530		
30-31					950,000	120,900	42,315		
31-32					1,000,000	62,000	21,700		
32-33									
33-34									
34-35									
Total	$ 10,020,000	$ 2,810,331	$ 550,000	$ 27,500	$ 12,000,000	$ 6,458,686	$ 2,260,539	$ 22,645,000	$ 4,756,714

*Series P-2010 bonds were issued as federally taxable Build America Bonds. KUB will receive a 35 percent interest rebate payment from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8% reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is in effect until intervening Congressional action, at which time the sequestration rate is subject to change.

Knoxville Utilities Board Gas Division
Supplemental Information - Schedule of Debt Maturities by Fiscal Year
June 30, 2016
(Unaudited)

Schedule 2

Continued from Previous Page

	R-2012		S-2013		T-2013		U-2015		Totals		Grand Total (P + I)	Grand Total (Less Rebate)
FY	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest		
16-17	400,000	282,530	570,000	374,100	500,000	1,011,825	100,000	397,638	5,450,000	3,987,262	9,437,262	9,211,217
17-18	425,000	270,530	595,000	351,300	500,000	996,825	615,000	395,637	5,590,000	3,793,753	9,383,753	9,163,945
18-19	425,000	257,780	615,000	327,500	500,000	976,825	660,000	377,187	5,780,000	3,599,143	9,379,143	9,166,916
19-20	450,000	240,781	645,000	302,900	500,000	956,825	680,000	357,387	5,985,000	3,390,981	9,375,981	9,172,605
20-21	475,000	222,781	695,000	277,100	500,000	936,825	710,000	323,387	6,240,000	3,137,531	9,377,531	9,183,920
21-22	475,000	203,781	715,000	249,300	500,000	916,825	740,000	287,887	6,455,000	2,870,862	9,325,862	9,143,256
22-23	500,000	184,781	730,000	227,850	500,000	901,825	795,000	250,888	6,705,000	2,609,576	9,314,576	9,143,695
23-24	525,000	169,781	745,000	205,950	500,000	886,200	805,000	233,000	6,925,000	2,362,650	9,287,650	9,128,932
24-25	550,000	159,281	790,000	183,600	1,550,000	869,950	845,000	208,850	6,270,000	2,102,075	8,372,075	8,227,313
25-26	575,000	142,781	800,000	159,900	1,600,000	813,763	880,000	183,500	6,485,000	1,871,190	8,356,190	8,225,865
26-27	575,000	130,560	840,000	135,900	1,650,000	749,763	895,000	154,900	6,695,000	1,627,951	8,322,951	8,208,081
27-28	600,000	117,625	875,000	110,700	1,700,000	683,763	985,000	123,573	5,835,000	1,369,309	7,204,309	7,106,554
28-29	625,000	99,625	905,000	84,450	1,750,000	615,763	975,000	89,100	5,990,000	1,145,326	7,135,326	7,055,316
29-30	650,000	84,000	940,000	57,300	1,950,000	543,575	955,000	59,850	5,410,000	920,525	6,330,525	6,268,995
30-31	675,000	64,500	970,000	29,100	2,000,000	460,700	1,040,000	31,200	5,635,000	706,400	6,341,400	6,299,085
31-32	725,000	44,250			2,000,000	373,200			3,725,000	479,450	4,204,450	4,182,750
32-33	750,000	22,500			2,000,000	283,200			2,750,000	305,700	3,055,700	3,055,700
33-34					2,100,000	193,200			2,100,000	193,200	2,293,200	2,293,200
34-35					2,100,000	96,600			2,100,000	96,600	2,196,600	2,196,600
Total	$ 9,400,000	$ 2,697,867	$ 11,430,000	$ 3,076,950	$ 24,400,000	$ 13,267,452	$ 11,680,000	$ 3,473,984	$ 102,125,000	$ 36,569,484	$ 138,694,484	$ 136,433,945

Knoxville Utilities Board Gas Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)

Schedule 3

Rate Class	Base Charge	Number of Customers
Residential (G-2)	For the regular monthly billing period for the months of November to April, inclusive: Customer charge per month $7.65 First 30 therms per month at $0.9670 per therm Excess over 30 therms per month at $0.7548 per therm For the regular monthly billing periods for the months of May to October, inclusive: Customer charge per month $7.65 First 50 therms per month $0.7883 per therm Excess over 50 therms per month at $0.6697 per therm	90,395
Commercial (G-4)	Available to any commercial or industrial customer: Customer charge per month $16.00 First 250 therms per month at $0.8923 per therm Excess over 250 therms per month at $0.7784 per therm	9,122
Commercial (G-6)	Available to any commercial or industrial customer incurring a demand of twenty-seven therms or more during the current monthly billing period or during any of the eleven net preceding monthly billing periods. The net rate is the sum of the following demand and commodity charges: Customer charge: $130.00 per month Demand charge: $1.90 per therm of demand Commodity charge: First 30,000 therms per month at $0.5230 per therm Excess over 30,000 therms per month at $0.4319 per therm	260
Industrial (G-7)	Service under Rate Schedule G-7 shall be available to any customer who meets the following conditions: (a) Customer's annual Interruptible Gas use, on an actual or projected basis, shall not be less than 25,000 dekatherms; (b) Customer shall be permitted to purchase only one (1) dekatherm of Firm Gas under Rate Schedule G-7 for each two (2) dekatherms of Interruptible Gas which are purchased; (c) Customer must have standby equipment of sufficient capacity capable of providing the customer's normal gas service requirements for a period of five (5) working days without replenishment when Interruptible Gas is completely interrupted. Customer shall maintain such equipment ready for operation at any time and shall utilize a fuel other than gas furnished by KUB and shall be subject to periodic inspections by KUB to ensure compliance with this provision; and (d) KUB must determine that its existing distribution system facilities are adequate and available for the requested service.	13

Knoxville Utilities Board Gas Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)

Schedule 3

Rate Class	Base Charge	Number of Customers

The net rate is the sum of the following demand and commodity charges:

Customer charge:	$300.00 per month
Demand charge:	$19.00 per month per dekatherm of demand
Commodity charge:	(a) Firm Gas - $4.319 per dekatherm (b) Interruptible Gas - (i) First 3,000 dekatherms per month at $4.026 per dekatherm; excess of 3,000 to 20,000 dekatherms per month at $3.445 per dekatherm; plus excess over 20,000 to 50,000 dekatherms per month at $2.671 per dekatherm; excess over 50,000 dekatherms per month at $2.460 per dekatherm (c) Supplemental Gas - The Commodity Charge for Supplemental Gas shall be the total of: (a) the cost per dekatherm to KUB for the applicable Day of acquiring Supplemental Gas on the open market, subject to the approval of the Customer to purchase Supplemental Gas at or above such price and (b) the costs incurred by KUB in transporting such Supplemental Gas via connecting pipelines to one or more of KUB's delivery points.
Transportation charge:	$1.996 per dekatherm for the first 3,000 dekatherms of gas Redelivered plus Unauthorized Gas; plus $1.415 per dekatherm for each dekatherm from 3,000 to and including 20,000 dekatherms of gas Redelivered plus Unauthorized Gas; plus $.641 per dekatherm for each dekatherm from 20,000 to and including 50,000 dekatherms of gas Redelivered plus Unauthorized Gas; plus $.430 per dekatherm for the excess over 50,000 dekatherms of gas Redelivered plus Unauthorized Gas.
Unauthorized Gas charge:	$15.00 per dekatherm of Unauthorized Gas as a penalty, plus the total of: (a) the cost per dekatherm of obtaining such gas on the open market as determined by the higher of (1) the applicable Gulf Coast Price Index for the applicable Day as published in *Gas Daily* or, if *Gas Daily* is no longer published, in a comparable reliable source for natural gas prices or (2) the applicable first of the month Gulf Coast Price Index as published in *Inside FERC*, or if *Inside FERC* is no longer published, in a comparable reliable source for natural gas prices and (b) the costs incurred by KUB in transporting such Unauthorized Gas via connecting pipelines to one or more of KUB's delivery points.

Knoxville Utilities Board Gas Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)
Schedule 3

Rate Class	Base Charge	Number of Customers
G-11	Service under Rate Schedule G-11 shall be available to any customer who meets the following conditions: (a) Customer's annual gas usage (excluding Firm Gas), on an actual or projected basis, shall not be less than 25,000 dekatherms; (b) Customer shall be permitted to purchase only one (1) dekatherm of Firm Gas under Rate Schedule G-11 for each two (2) dekatherms of Transport Gas delivered by KUB to the Customer; (c) Customer must have standby equipment of sufficient capacity capable of providing the customer's normal gas service requirements for a period of five (5) working days without replenishment when Transport Gas is completely interrupted. Customer shall maintain such equipment ready for operation at any time and shall utilize a fuel other than gas furnished by KUB and shall be subject to periodic inspections by KUB to ensure compliance with this provision; (d) Customer's use under this rate shall not work a hardship on any other customers of KUB, nor adversely affect any other class of KUB's customers and further provided the Customer's use under this rate shall not adversely affect KUB's gas purchase plans and/or effective utilization of the daily demands under KUB's gas purchase contracts with its suppliers, as solely determined by KUB. (e) KUB must determine that its existing distribution system facilities are adequate and available for the requested service; and (f) Customer must execute a Transportation Service Agreement for interruptible transportation gas service. The net rate is the sum of the following charges: Customer charge: $400.00 Demand charge: $19.00 per dekatherm of demand Firm Gas charge: $4.319 per dekatherm Transportation charge: $1.996 per dekatherm for the first 3,000 dekatherms of non-Firm gas delivered to Customer; plus $1.415 per dekatherm for each dekatherm from 3,000 to and including 20,000 dekatherms of non-Firm gas delivered to Customer; plus $.641 per dekatherm for each dekatherm from 20,000 to and including 50,000 dekatherms of non-Firm gas delivered to Customer; plus $.430 per dekatherm for the excess over 50,000 dekatherms of non-Firm gas delivered to Customer. Standby Gas charge: The charge for Standby Gas shall be the total of: (a) the cost per dekatherm to KUB for the applicable Day of acquiring Standby Gas on the open market, subject to the approval of the Customer to purchase Standby Gas at or above such price and (b) the costs incurred by KUB in transporting such Standby Gas via connecting pipelines to one or more of KUB's delivery points.	14

Knoxville Utilities Board Gas Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)
Schedule 3

Rate Class	Base Charge	Number of Customers
	Unauthorized Gas charge: $15.00 per dekatherm of Unauthorized Gas as a penalty, plus the total of: (a) the cost per dekatherm of obtaining such gas on the open market as determined by the higher of (1) the applicable Gulf Coast Price Index for the applicable Day as published in *Gas Daily* or, if *Gas Daily* is no longer published, in a comparable reliable source for natural gas prices or (2) the applicable first of the month Gulf Coast Price Index as published in *Inside FERC* , or if *Inside FERC* is no longer published, in a comparable reliable source for natural gas prices and (b) the costs incurred by KUB in transporting such Unauthorized Gas via connecting pipelines to one or more of KUB's delivery points. Other charges: Imbalance Charges, and any pipeline scheduling, balancing, transportation, or other similar charges incurred by KUB in connection with the transportation of gas on behalf of the Customer, as applicable.	
G-12	Service under Rate Schedule G-12 shall be available to any customer when the following conditions are met: (a) Customer's annual gas usage, on an actual or projected basis, shall not be less than 12,500 dekatherms; (b) KUB must determine that its existing distribution system facilities are adequate and available for the requested service; (c) Customer must execute a Transportation Service Agreement for firm transportation gas service; and (d) Customer's use under this rate shall not work a hardship on any other customers of KUB, nor adversely affect any other class of KUB's customers and further provided the Customer's use under this rate shall not adversely affect KUB's gas purchase plans and/or effective utilization of the daily demands under KUB's gas purchase contracts with its suppliers, as solely determined by KUB. The net rate is the sum of the following charges: Customer charge: $400.00 Demand charge: $6.20 per dekatherm of demand Transportation charge: $2.256 per dekatherm for the first 3,000 dekatherms of gas delivered to Customer; plus $1.532 per dekatherm for each dekatherm from 3,000 to and including 20,000 dekatherms of gas delivered to Customer; plus $.731 per dekatherm for each dekatherm from 20,000 to and including 50,000 dekatherms of gas delivered to Customer; plus $.575 per dekatherm for the excess over 50,000 dekatherms of gas delivered to Customer.	4

Knoxville Utilities Board Gas Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)

Schedule 3

Rate Class	Base Charge		Number of Customers
	Standby Gas charge:	The charge for Standby Gas shall be the total of: (a) the cost per dekatherm to KUB for the applicable Day of acquiring Standby Gas on the open market, subject to the approval of the Customer to purchase Standby Gas at or above such price and (b) the costs incurred by KUB in transporting such Standby Gas via connecting pipelines to one or more of KUB's delivery points.	
	Unauthorized Gas charge:	$15.00 per dekatherm of Unauthorized Gas as a penalty, plus the total of: (a) the cost per dekatherm of obtaining such gas on the open market as determined by the higher of (1) the applicable Gulf Coast Price Index for the applicable Day as published in *Gas Daily* or, if *Gas Daily* is no longer published, in a comparable reliable source for natural gas prices or (2) the applicable first of the month Gulf Coast Price Index as published in *Inside FERC* , or if *Inside FERC* is no longer published, in a comparable reliable source for natural gas prices and (b) the costs incurred by KUB in transporting such Unauthorized Gas via connecting pipelines to one or more of KUB's delivery points.	
	Other charges:	Imbalance Charges, and any pipeline scheduling, balancing, transportation, or other similar charges incurred by KUB in connection with the transportation of gas on behalf of the Customer, as applicable.	

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

Board of Commissioners
Gas Division of the Knoxville Utilities Board
Knoxville, Tennessee

Report on the Financial Statements

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Gas Division (the Division) of the Knoxville Utilities Board, a component unit of the City of Knoxville, Tennessee, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements, and have issued our report thereon dated October 27, 2016.

Internal Control over Financial Reporting

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

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

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

Board of Commissioners
Gas Division of the Knoxville Utilities Board
Knoxville, Tennessee

Compliance and Other Matters

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

Purpose of Report

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

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

KUB

Knoxville Utilities Board

Water Division

Financial Statements and Supplemental Information
June 30, 2016 and 2015

Knoxville Utilities Board Water Division
Index
June 30, 2016 and 2015

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Report of Independent Auditors

Board of Commissioners
Water Division of the Knoxville Utilities Board
Knoxville, Tennessee

We have audited the accompanying financial statements of the Water Division (the Division) of the Knoxville Utilities Board, a component unit of the City of Knoxville, Tennessee, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements as listed in the index.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Division'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 Division'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 the Water Division of the Knoxville Utilities Board as of June 30, 2016 and 2015, and the changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Commissioners
Water Division of the Knoxville Utilities Board
Knoxville, Tennessee

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 24 and the required supplementary information on pages 51 through 53 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Division's basic financial statements. The supplemental information is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplemental information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 27, 2016, on our consideration of the Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

Knoxville Utilities Board (KUB), comprised of the Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions. The Water Division (Division) provides services to certain customers in Knox County and in two surrounding counties in East Tennessee. The Division's accounts are maintained in conformity with the Uniform System of Accounts of the National Association of Regulatory Utility Commissioners (NARUC) and the Governmental Accounting Standards Board (GASB), as applicable. The financial statements present only the Water Division and do not purport to, and do not, present fairly the consolidated financial position of Knoxville Utilities Board at June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Division's discussion and analysis is designed to (a) assist the reader in focusing on significant financial issues, (b) provide an overview of the Division's financial activity, (c) identify major changes in the Division's financial position, and (d) identify any financial concerns.

The Division's Management Discussion and Analysis (MD&A) focuses on the fiscal year ending June 30, 2016 activities, resulting changes and current known facts, and should be read in conjunction with the Division's financial statements.

Water Division Highlights

System Highlights

KUB serves 78,980 water system customers over a 188 square mile service area. KUB maintains 1,411 miles of service mains, 28 storage facilities, 24 booster pump stations, and one treatment plant, which provided 12 billion gallons of water to KUB's water customers in fiscal year 2016. The average daily flow for fiscal year 2016 was 32.9 million gallons.

The water system has added approximately 715 customers over the past three years representing annual growth of less than one percent.

The Division generated $2 million of additional revenue during the fiscal year as a result of the July 2015 water rate increase, adopted by the KUB Board of Commissioners to help fund the Division's Century II infrastructure program.

The typical residential water customer's average monthly bill was $22.45 as of June 30, 2016 (based on monthly use of 500 cubic feet or 3,740 gallons). The monthly bill increased $1 compared to the prior fiscal year, the result of the July 2015 water rate increase.

Water sales volumes have been impacted by the use of more efficient appliances and the conservation efforts of customers. As a result, water sales volumes have declined 7 percent in the past decade.

Century II Infrastructure Program

Century II is KUB's proactive long-range program to improve and maintain the electric, natural gas, water and wastewater systems for its customers. It includes the maintenance and asset replacement strategies for each system and establishes sustainable replacement cycles. Century II moves KUB into its second century of service by improving each system through sound planning, resource allocation, and continued, but accelerated, investment.

KUB's Century II programs were resumed in 2011, after a break due to the economic recession. At that time, the KUB Board of Commissioners formally endorsed a ten year funding plan for the water system, including a combination of rate increases and debt issues. The Board also approved three years of annual water rate increases for fiscal years 2012 through 2014.

In April 2014, KUB management provided the Board an updated assessment of the overall condition of each utility system and the progress made during the resumption of the Century II program. A revised ten-year funding plan for the water system, including recommendations for annual rate increases and debt issues to fully fund the programs for each division, was included in the assessment.

In June 2014, the Board approved the proposed three annual rate increases for the Water Division. The July 2014 and July 2015 rate increases generated $3.6 million and $2 million of additional annual Water Division revenue, respectively, while the July 2016 rate increase will result in additional annual Water Division revenue of $2 million.

In fiscal year 2015, KUB concluded the smart grid pilot project, of which a portion of the project was funded by a United States Department of Energy Smart Grid Investment Grant (SGIG). This grant was received by KUB in 2009 as part of the American Reinvestment and Recovery Act (ARRA). Based upon the success of that pilot, KUB formed a plan to move forward with a Century II Grid Modernization initiative, which includes advanced metering for all KUB customers, a telecommunication system linking critical KUB infrastructure, and an increased investment in automation technology to help operate KUB's energy and water distribution systems.

KUB is in the process of implementing a 15-year initiative to ensure KUB will continue to provide high-quality, reliable water service to its customers over the long-term. KUB maintains a single water treatment plant for its system. In lieu of building a second treatment facility to ensure capacity will be available to meet the needs of current and future water customers, KUB will invest approximately $120 million in various redundant facilities at its existing Mark B. Whitaker Water Treatment Plant over the next 11 years.

KUB remains on track with its Century II water system infrastructure program. In fiscal year 2016, KUB replaced 14.3 miles of galvanized water main and 7.2 miles of cast iron main. Other notable Century II water system improvements projects included replacing water main on Cumberland Avenue to accommodate the City of Knoxville's Cumberland Avenue Streetscape project and the Downtown Century II project.

Financial Highlights

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division's net position during the year increased $6 million compared to a $5 million increase last fiscal year. A restatement to the fiscal year 2014's net position based on a change in method of accounting for pension expense reduced the total net position by $0.1 million during fiscal year 2015.

Operating revenue increased $3.3 million or 7.4 percent, the result of additional revenue from the water rate increase effective July 2015 and a 0.8 percent increase in water sales volumes.

Operating expenses increased $2 million or 5.9 percent. Operating and maintenance expenses (O&M) increased $0.6 million compared to the prior year. Depreciation expense increased $1.3 million or 16.2 percent. Taxes and tax equivalents increased $0.1 million from the prior year.

Interest income was up $0.1 million from the prior fiscal year. Interest expense was $0.2 million higher than the prior year, due to additional interest expense from bonds sold in the August 2014 and April 2015.

Capital contributions were $0.1 million higher than the prior fiscal year, the result of increased contributed assets from developers.

Total plant assets (net) increased $23.2 million or 9 percent due to water main replacement, treatment plant improvements and upgrades to various information systems.

Long-term debt represented 46.9 percent of the Division's capital structure as of June 30, 2016, as compared to 48.6 percent last year. Capital structure equals long-term debt (which includes the current and long term portion of revenue bonds and notes) plus net position.

The Division's bond covenants require a debt service coverage ratio of at least 1.2 times the maximum principal and interest payments over the life of the Division's outstanding bonds. Current year debt coverage for the fiscal year was 2.41. Maximum debt service coverage was 2.32

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division's net position during the year increased $5 million compared to a $1.5 million increase last fiscal year. A restatement to the prior fiscal year's net position based on a change in method of accounting for pension expense reduced the total net position by $0.1 million during fiscal year 2015. This change resulted in a net increase of $4.9 million or 3.2 percent in the Division's net position.

Operating revenue increased $4.8 million or 12.2 percent, the net result of additional revenue from the Century II water rate increases, which were effective January and July 2014, and a 1.6 percent increase in water sales volumes.

Operating expenses increased $1.3 million or 3.8 percent. Operating and maintenance expenses (O&M) decreased $0.2 million compared to the prior year. Depreciation expense increased $0.9 million or 12.4 percent. Taxes and tax equivalents increased $0.6 million from the prior year.

Interest income was consistent with the prior fiscal year. However, interest expense was $0.2 million higher than the prior year, due to additional interest expense from bonds sold in the August 2014 and April 2015.

Capital contributions were $0.1 million higher than the prior fiscal year, the result of increased contributed assets from developers.

Total plant assets (net) increased $18.4 million or 7.7 percent due to main replacement, treatment plant improvements and information system upgrades.

KUB sold two series of water system revenue bonds during fiscal year 2015 for the purpose of funding water system capital improvements totaling $28 million. The $20 million bond issue in April 2015 was accelerated to take advantage of the low interest rate environment which impacted the Division's debt rate and debt service coverage levels for fiscal year 2015. Long-term debt represented 48.6 percent of the Division's capital structure as of June 30, 2015, as compared to 44.8 percent last year. Capital structure equals long-term debt (which includes the current and long term portion of revenue bonds and notes) plus net position.

The Division's bond covenants require a debt service coverage ratio of at least 1.2 times the maximum principal and interest payments over the life of the Division's outstanding bonds. Current year debt coverage for the fiscal year was 2.35. Maximum debt service coverage was 2.06.

Knoxville Utilities Board Water Division - Financial Statements

The Division's financial performance is reported under three basic financial statements: the Statement of Net Position; the Statement of Revenues, Expenses, and Changes in Net Position; and the Statement of Cash Flows.

Statement of Net Position

The Division reports its assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position in the Statement of Net Position. Assets are classified as current, restricted, water plant in service, or other assets.

Liabilities are classified as current, other, or long-term debt. Net position is classified as net investment in capital assets; restricted; or unrestricted. Net position tells the user what the Division has done with its accumulated earnings, not just the balance.

Net investment in capital assets reflects the book value of all capital assets less the outstanding balances of debt used to acquire, construct, or improve those assets.

Restricted net position are assets that have been limited to specific uses by the Division's bond covenants or through resolutions passed by the KUB Board.

Unrestricted net position are a residual classification; the amount remaining after reporting net position as either invested in capital or restricted is reported there.

Statement of Revenues, Expenses, and Changes in Net Position

The Division reports its revenues and expenses (both operating and non-operating) on the Statement of Revenues, Expenses, and Changes in Net Position. In addition, any capital contributions or assets donated by developers are reported on this statement.

Total revenue less total expense equals the change in net position for the reporting period. Net position at the beginning of the period is increased or decreased, as applicable, by the change in net position for the reporting period.

The change in net position for the reporting period is added to the net position segment of the Statement of Net Position.

Statement of Cash Flows

The Division reports cash flows from operating activities, capital and related financing activities, and investing activities on the Statement of Cash Flows. This statement tells the user the Division's sources and uses of cash during the reporting period.

The statement indicates the Division's beginning cash balance and ending cash balance and how it was either increased or decreased during the reporting period.

The statement also reconciles cash flow to operating income as it appears on the Statement of Revenues, Expenses, and Changes in Net Position.

Condensed Financial Statements

Statement of Net Position

The following table reflects the condensed Statement of Net Position for the Water Division compared to the prior year and the year preceding the prior year.

Statements of Net Position
As of June 30

(in thousands of dollars)	2016	2015	2014
Current, restricted and other assets	$ 33,888	$ 55,083	$ 43,995
Capital assets, net	281,258	258,139	239,706
Deferred outflows of resources	3,273	2,459	260
Total assets and deferred outflows of resources	318,419	315,681	283,961
Current and other liabilities	13,097	10,996	10,584
Long-term debt outstanding	142,132	146,857	121,264
Deferred inflows of resources	197	829	-
Total liabilities and deferred inflows of resources	155,426	158,682	131,848
Net position			
Net investment in capital assets	138,069	110,579	116,197
Restricted	1,523	1,375	1,219
Unrestricted	23,401	45,045	34,697
Total net position	$ 162,993	$ 156,999	$ 152,113

Normal Impacts on Statement of Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Net Position presentation.

- Change in net position (from Statement of Revenues, Expenses, and Change in Net Position): impacts (increase/decrease) current and other assets and/or capital assets and unrestricted net position.

- Issuing debt for capital: increases deferred outflows of resources and long-term debt.

- Spending debt proceeds on new capital: reduces current assets and increases capital assets.

- Spending of non-debt related current assets on new capital: (a) reduces current assets and increases capital assets and (b) reduces unrestricted net position and increases net investment in capital assets.

- Principal payment on debt: (a) reduces current and other assets and reduces long-term debt and (b) reduces unrestricted net position and increases net investment in capital assets.

- Reduction of capital assets through depreciation: reduces capital assets and net investment in capital assets.

Impacts and Analysis

Current, Restricted and Other Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Current, restricted and other assets decreased $21.2 million or 38.5 percent. The decrease reflects the utilization of $9.9 million in bond proceeds and an $11.9 million decrease in the Division's general fund cash (consisting of cash and cash equivalents, short-term investments, and long-term investments). These decreases were offset by a $0.5 million increase in operating contingency reserves.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current, restricted and other assets increased $11.1 million or 25.2 percent. The increase reflects a higher level of unused bond proceeds of $9.9 million and a $1.2 million increase in operating contingency reserves. These increases were offset by a $0.9 million decrease in the Division's general fund cash (consisting of cash and cash equivalents, short-term investments, and long-term investments).

Capital Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Capital assets, net of depreciation, increased $23.2 million or 9 percent. Capital expenditures included $13.5 million for water main replacement, $7.5 million for treatment plant and system improvements, $2.8 million for the replacement and relocation of water system assets to accommodate Tennessee Department of Transportation (TDOT) highway improvement projects and $1.1 million for upgrades to various information systems. $4.9 million of water system assets were retired during the fiscal year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Capital assets, net of depreciation, increased $18.4 million or 7.7 percent. Capital expenditures included $12.5 million for water main replacement, $7.8 million for treatment plant and system improvements and $1.1 million for information system upgrades. $2 million of water system assets were retired during the fiscal year.

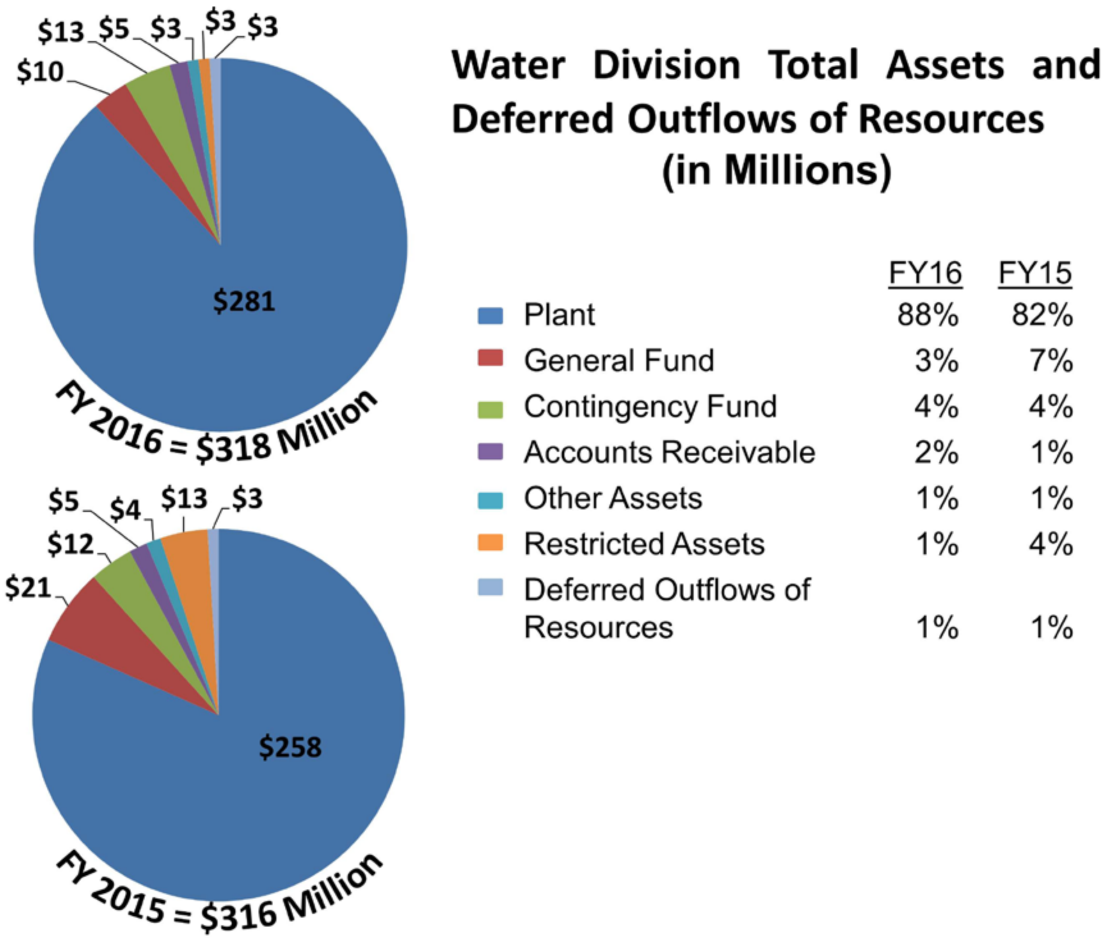
Deferred Outflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred outflows of resources increased $0.8 million compared to the prior fiscal year. This increase was the net effect of an increase in pension outflow of $0.9 million and a decrease of unamortized bond refunding costs of $0.1 million.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred outflows of resources increased $2.2 million compared to the prior fiscal year. The unamortized bond refunding costs increased $1.8 million due to the April 2015 issuance of $23 million in revenue refunding bonds.



Water Division Total Assets and Deferred Outflows of Resources (in Millions)

	FY16	FY15
■ Plant	88%	82%
■ General Fund	3%	7%
■ Contingency Fund	4%	4%
■ Accounts Receivable	2%	1%
■ Other Assets	1%	1%
■ Restricted Assets	1%	4%
■ Deferred Outflows of Resources	1%	1%

Current and Other Liabilities

Fiscal Year 2016 Compared to Fiscal Year 2015

Current and other liabilities increased $2.1 million over the prior fiscal year. Accounts payable at year end were $0.9 million higher and the actuarially determined net pension obligation of $0.7 million was recognized in fiscal year 2016.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current and other liabilities increased $0.4 million over the prior fiscal year due to a $0.8 million increase in the current portion of revenue bonds and a $0.3 million increase in accounts payable.

Long-Term Debt

Fiscal Year 2016 Compared to Fiscal Year 2015

Long-term debt decreased $4.7 million or 3.2 percent primarily due to $4.6 million of long-term bond debt that shifted to current liabilities as payable within the next year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Long-term debt increased $25.6 million or 21.1 percent, the combined result of additional revenue bonds of $8 million issued in August 2014 and $20 million issued April 2015. The increase was partially offset by the scheduled repayment of bond debt.

Deferred Inflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred inflows decreased $0.6 million compared to the prior fiscal year due to differences in pension inflows.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred inflows of resources were $0.8 million due to the addition of pension inflow.

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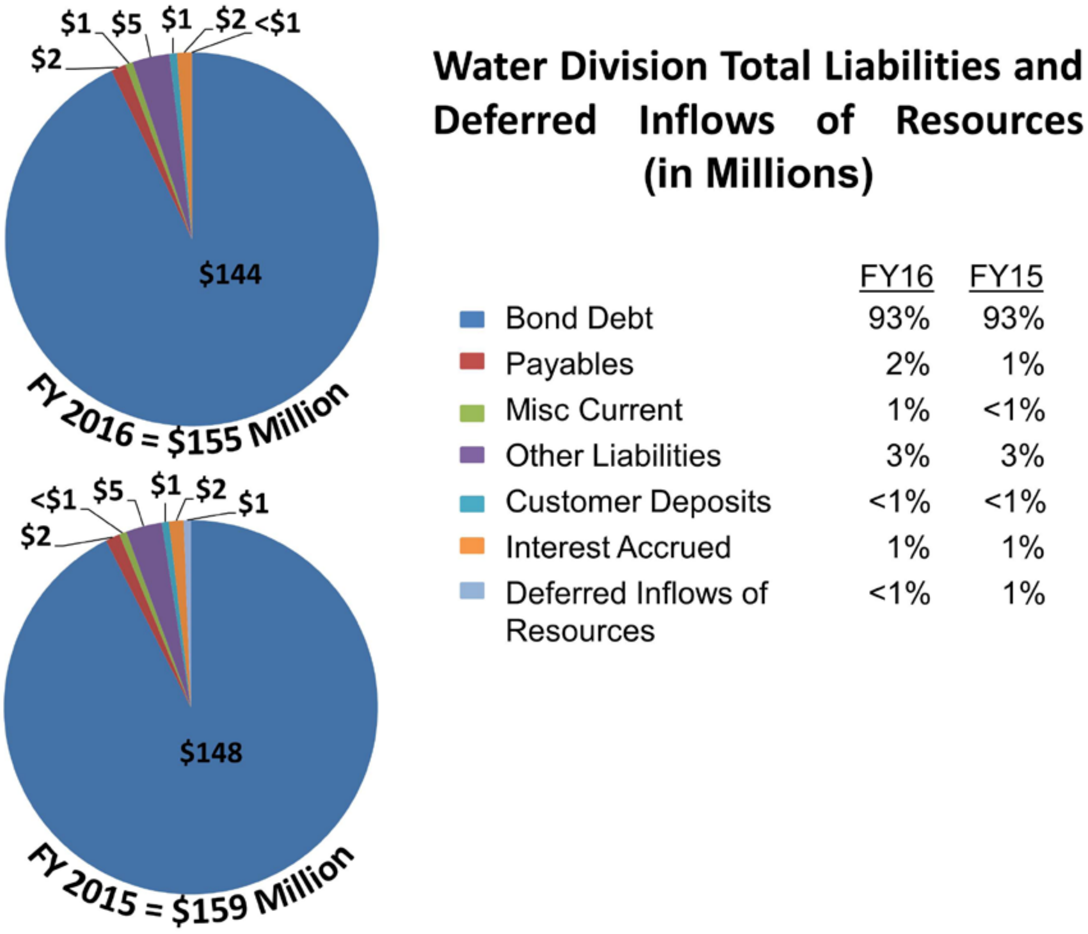

	FY16	FY15
Bond Debt	93%	93%
Payables	2%	1%
Misc Current	1%	<1%
Other Liabilities	3%	3%
Customer Deposits	<1%	<1%
Interest Accrued	1%	1%
Deferred Inflows of Resources	<1%	1%

Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

Net position increased $6 million this fiscal year. Net investment in capital assets increased $27.5 million, due to an increase to net plant in service of $23.2 million. Unrestricted net position decreased $21.6 million, primarily due to an $11.9 million decrease in general fund cash and a $9.9 decrease in unused bond proceeds compared to June of the prior year. Restricted assets increased $0.1 million, due to additional funds restricted for debt service.

Fiscal Year 2015 Compared to Fiscal Year 2014

Net position increased $4.9 million this fiscal year. Net investment in capital assets decreased $5.6 million, due to the net effect of an increase to net plant in service of $18.4 million and additional debt of $28 million. Unrestricted net position increased $10.3 million, primarily due to unused bond proceeds for capital improvements in the general fund. Restricted assets increased $0.2 million, due to additional funds restricted for debt service.

Statement of Revenues, Expenses, and Changes in Net Position

The following table reflects the condensed Statement of Revenues, Expenses, and Changes in Net Position for the Water Division compared to the prior year and the year preceding the prior year.

Statements of Revenues, Expenses, and Changes in Net Position
For the Years Ended June 30

(in thousands of dollars)	2016	2015	2014
Operating revenues	$ 47,453	$ 44,173	$ 39,374
Operating expenses			
Treatment	4,186	3,789	3,355
Distribution	12,645	13,046	13,635
Customer service	1,666	1,653	1,517
Administrative and general	4,838	4,206	4,364
Depreciation	9,055	7,795	6,934
Taxes and tax equivalents	3,717	3,622	3,042
Total operating expenses	36,107	34,111	32,847
Operating income	11,346	10,062	6,527
Interest income	194	135	126
Interest expense	(5,612)	(5,421)	(5,258)
Other income/(expense)	(235)	(23)	(73)
Change in net position before capital contributions	5,693	4,753	1,322
Capital Contributions	301	233	158
Change in net position	$ 5,994	$ 4,986	$ 1,480

Normal Impacts on Statement of Revenues, Expenses, and Changes in Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Revenues, Expenses, and Change in Net Position presentation.

- Operating revenues are largely determined by the volumes of water sold during the fiscal year. Any change (increase/decrease) in retail water rates would also be a cause of change in operating revenue.

- Operating expenses (treatment, distribution, customer service, administrative and general) are normally impacted by changes in areas including, but not limited to, labor cost (staffing, wage rates), active employee and retiree medical costs, chemicals, and water system maintenance.

- Depreciation expense is impacted by plant additions and retirements during the fiscal year.

- Taxes and tax equivalents are impacted by plant additions/retirements and changes in property tax rates.

- Interest expense is impacted by the level of interest rates and investments.

- Interest expense on debt is impacted by the level of outstanding debt and the interest rates on the outstanding debt.

- Other income/(expenses) is impacted by miscellaneous non-operating revenues and expenses.

- Capital contributions are impacted by a donation of facilities/infrastructure to KUB by developers and governmental agencies. The contributions are recognized as revenue and recorded as plant in service based on the fair market value of the asset(s).

Impacts and Analysis

Change in Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division's net position during the year increased $6 million compared to a $5 million increase last fiscal year. A restatement to fiscal year 2014's net position based on a change in method of accounting for the pension reduced the total net position by $0.1 million.

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division's net position during the year increased $5 million compared to a $1.5 million increase last fiscal year. A restatement to the prior fiscal year's net position based on a change in method of accounting for the pension reduced the total net position by $0.1 million. This change resulted in a net increase of $4.9 million or 3.2 percent in the Division's net position.

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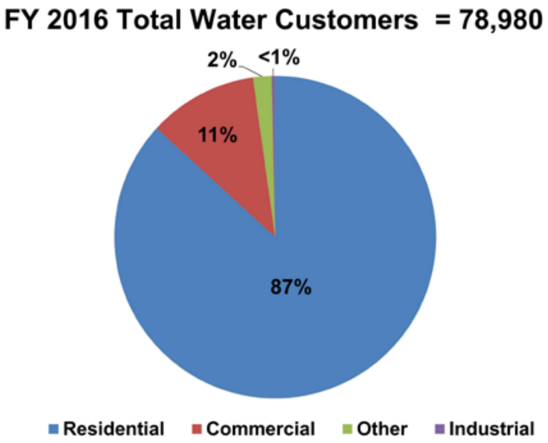
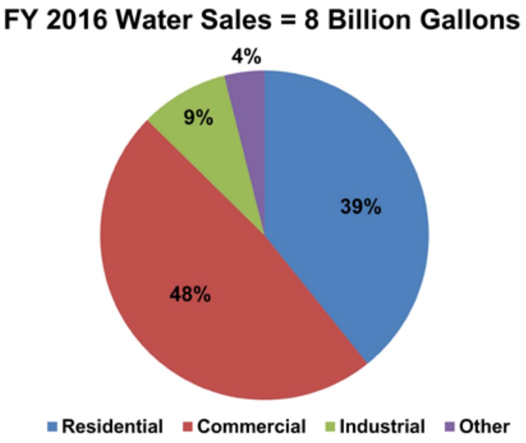
Margin from Sales

Fiscal Year 2016 Compared to Fiscal Year 2015

Operating revenues increased $3.3 million or 7.4 percent, reflecting additional revenue from the July 2015 water rate increase and a one percent increase in sales volumes. Operating expenses rose $2 million and interest expense increased $0.2 million.





Residential customers represented 87 percent of water customers and accounted for 39 percent of water sales volumes for the year. Commercial and industrial customers accounted for the largest portion (57 percent) of total sales volumes during the year.

KUB's ten largest water customers accounted for 11.9 percent of KUB's billed water volumes. Those ten customers represent five industrial and five commercial customers, including three governmental customers.

Residential water sales volumes were 1.6 percent lower than the prior fiscal year. Residential sales were lower throughout the majority of the year, due to higher precipitation levels during the fiscal year.

Commercial sales volumes increased 0.4 percent compared to the prior year. Industrial sales volumes increased 2.8 percent compared to the prior year.

KUB has added 715 water customers over the past three years, representing annual growth of less than one percent. Water system growth has slowed in recent years, in large part due to the slowdown of new housing construction.

Fiscal year 2016 water sales volumes were slightly higher than the prior fiscal year, reflecting higher water sales for commercial and industrial customers. Sales volumes have remained relatively consistent by customer class over the last three years.

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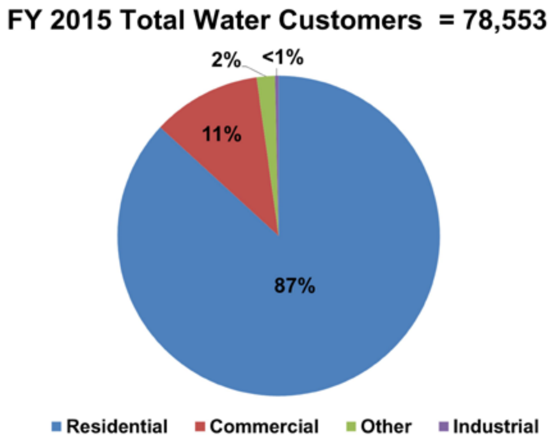
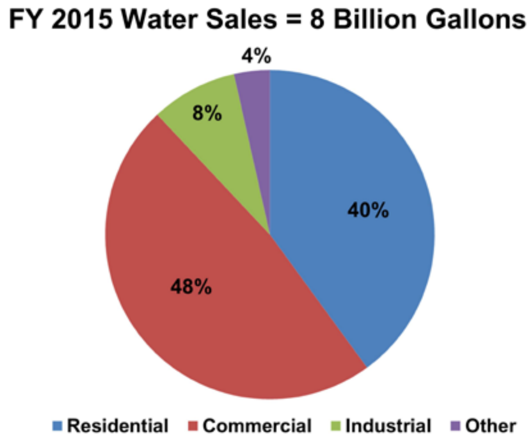
Fiscal Year 2015 Compared to Fiscal Year 2014

Operating revenues increased $4.8 million or 12.2 percent, reflecting additional revenue from the January and July 2014 water rate increases. Operating expenses rose $1.3 million, interest expense increased $0.2 million, and capital contributions from developers increased $0.1 million.


FY 2015 Total Water Customers = 78,553


FY 2015 Water Sales = 8 Billion Gallons

Residential customers represented 87 percent of water customers and accounted for 40 percent of water sales volumes for the year. Commercial and industrial customers accounted for the largest portion (56 percent) of total sales volumes during the year.

KUB's ten largest water customers accounted for 11.1 percent of KUB's billed water volumes. Those ten customers represent five industrial and five commercial customers, including three governmental customers.

Residential water sales volumes were 0.8 percent higher than the prior fiscal year. Residential sales were higher throughout the majority of the year, due to lower precipitation levels during the fiscal year.

Commercial sales volumes increased 1.9 percent compared to the prior year. Industrial sales volumes decreased 1.3 percent compared to the prior year.

KUB has added 568 water customers over the past three years, representing annual growth of less than one percent. Water system growth has slowed in recent years, in large part due to the slowdown of new housing construction.

Fiscal year 2015 water sales volumes were higher than the prior fiscal year, reflecting higher water sales for residential and commercial customers. Sales volumes have remained relatively consistent by customer class over the last three years.

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Operating Expenses

Fiscal Year 2016 Compared to Fiscal Year 2015

Operating expenses increased $2 million or 5.9 percent. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as treatment, distribution, customer service and administrative and general.

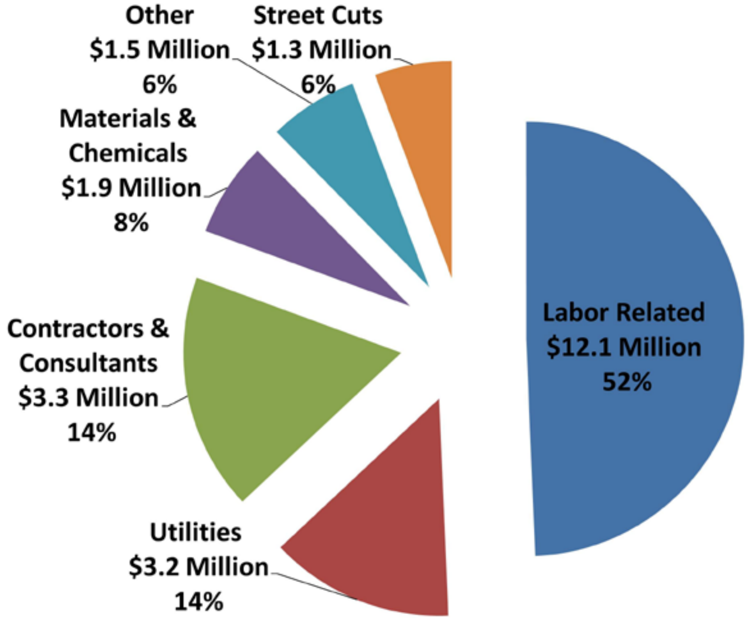
- Treatment expenses increased $0.4 million or 10.5 percent, primarily reflecting higher labor related expenses.

- Distribution expenses were $0.4 million or 3.1 percent lower than the prior fiscal year, due to a decline in outside contractor costs.

- Customer service expenses were consistent with the prior fiscal year.

- Administrative and general expenses increased $0.6 million due to higher pension expenses.

FY 2016 Water O&M Expense = $23.3 Million



- Depreciation expense was up $1.3 million primarily due to Century II initiatives to replace mains and the accelerated depreciation of existing meters that are to be replaced as part of KUB's Grid Modernization project. In addition, $4.9 million of assets were retired during fiscal year 2016.

- Taxes and tax equivalents increased $0.1 million from prior fiscal year due to increased plant in service levels.

Fiscal Year 2015 Compared to Fiscal Year 2014

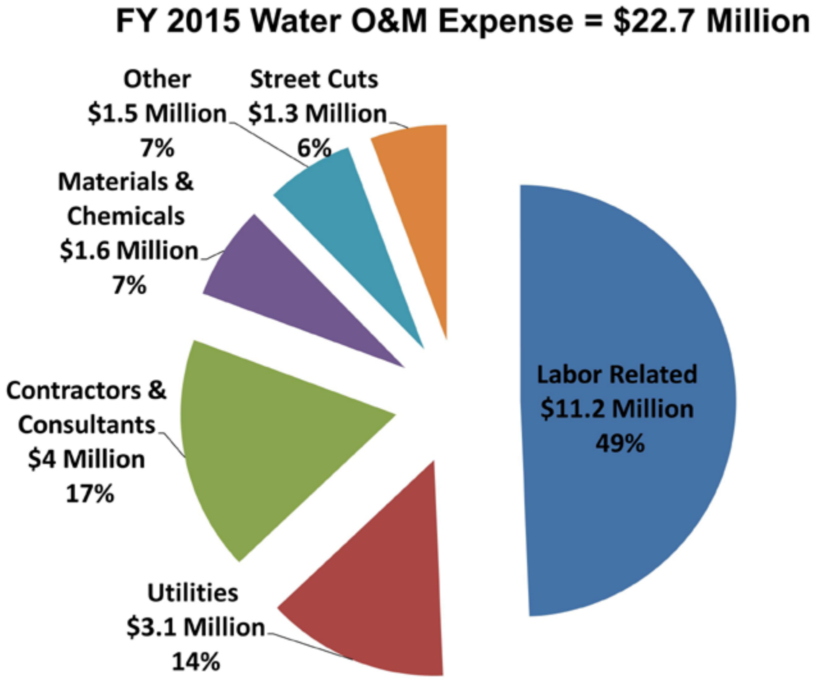
Operating expenses increased $1.3 million or 3.8 percent. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as treatment, distribution, customer service and administrative and general.

- Treatment expenses increased $0.4 million or 12.9 percent, primarily reflecting higher outside consultant expenses associated with a coagulation optimization study for the water treatment plant.

- Distribution expenses were $0.6 million or 4.3 percent lower than the prior fiscal year, due to a decline in outside contractor costs and street cut expenses.

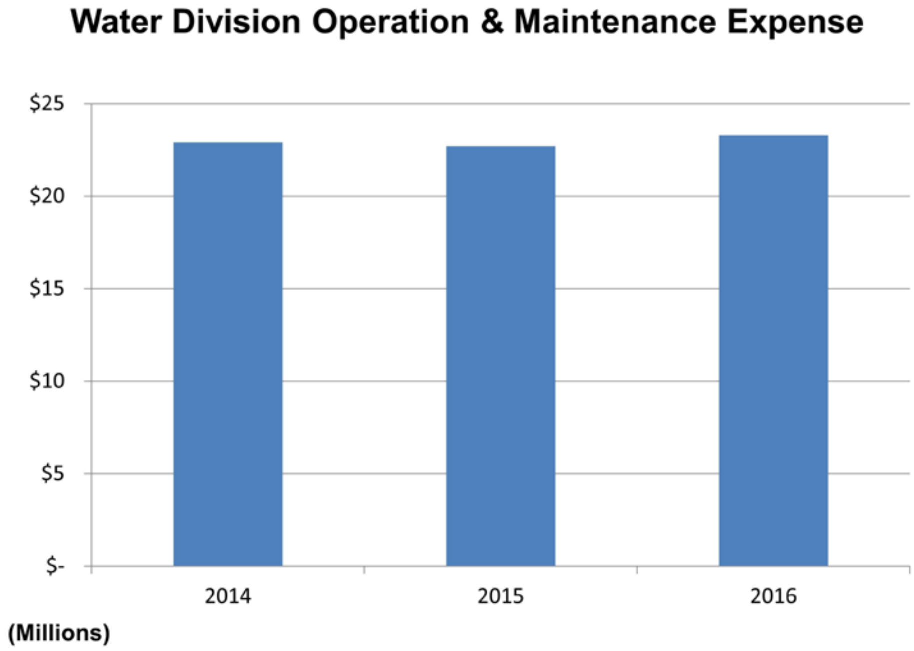
- Customer service expenses increased $0.1 million or 9 percent.

- Administrative and general expenses decreased $0.1 million or 3.6 percent.



- Depreciation expense was up $0.9 million reflecting a full year of depreciation on $23.9 million of water system assets added the previous fiscal year and a partial year of depreciation on $14.2 million of assets added in fiscal year 2015. In addition, $2.1 million of assets were retired during fiscal year 2015.

- Taxes and tax equivalents increased $0.6 million from prior fiscal year due to an increase in tax equivalent payments to the City of Knoxville. The City of Knoxville's property tax rate increased this year and higher plant in service levels contributed to the growth in tax equivalent payments.



Other Income and Expense

Fiscal Year 2016 Compared to Fiscal Year 2015

Interest income was up $0.1 million from the prior fiscal year.

Interest expense increased $0.2 million, reflecting additional interest expense from revenue bonds sold in fiscal year 2015.

Other income (net) decreased $0.2 million compared to the prior fiscal year.

Capital contributions by developers were $0.1 million higher than the prior fiscal year.

Fiscal Year 2015 Compared to Fiscal Year 2014

Interest income was consistent with the prior fiscal year.

Interest expense increased $0.2 million, reflecting interest expense from the $28 million in revenue bonds sold in fiscal year 2015.

Other income (net) was increased $0.1 million compared to the prior fiscal year.

Capital contributions by developers were $0.1 million higher than fiscal year 2014.

Capital Assets

Capital Assets
As of June 30
(Net of Depreciation)

(in thousands of dollars)

	2016	2015	2014
Production Plant	$ 58	$ 62	$ 76
Pumping & Treatment Plant	50,067	39,411	41,201
Distribution Plant			
Distribution Mains	$ 141,200	126,124	117,714
Transmission Mains	22,295	19,182	19,506
Services & Meters	19,349	18,541	18,561
Other Accounts	11,620	11,057	10,891
Total Distribution Plant	194,464	$ 174,904	$ 166,672
Total General Plant	$ 9,172	8,133	8,240
Total Water Plant	253,761	$ 222,510	$ 216,189
Work In Progress	27,497	35,629	23,517
Total Net Plant	$ 281,258	$ 258,139	$ 239,706

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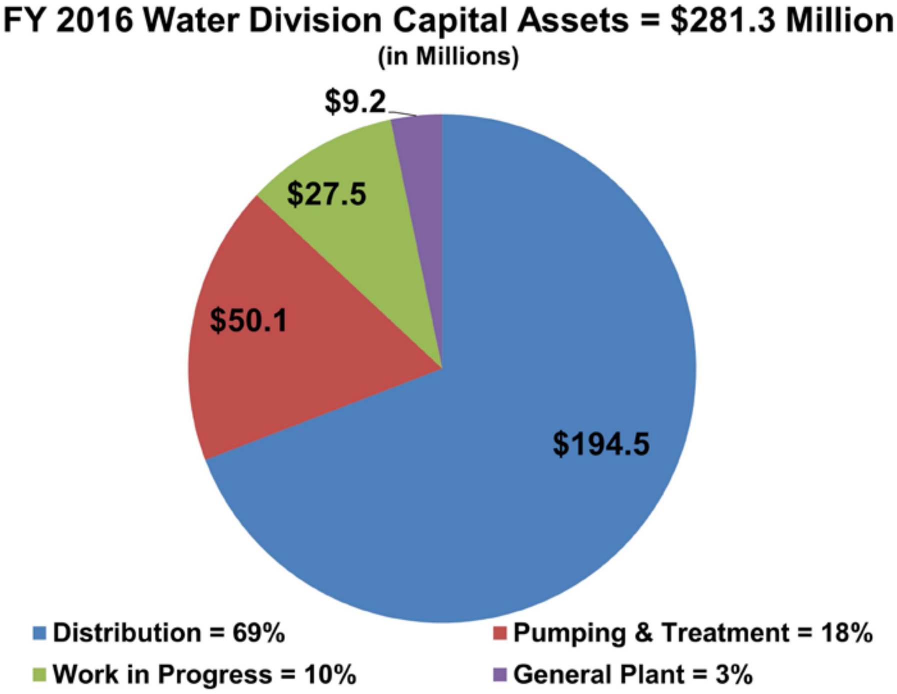
Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, the Division had $281.3 million invested in a variety of capital assets, as reflected in the schedule of capital assets, which represented a net increase (including additions, retirements, and depreciation) of $23.2 million or 9 percent over the end of the last fiscal year.



Major capital asset expenditures during the year were as follows:

- $13.5 million for galvanized and cast iron water main replacement
- $7.5 million for major plant and system improvements
- $2.8 million for replacement and relocation of water system assets to accommodate TDOT highway improvement projects
- $1.1 million for upgrades to various information systems

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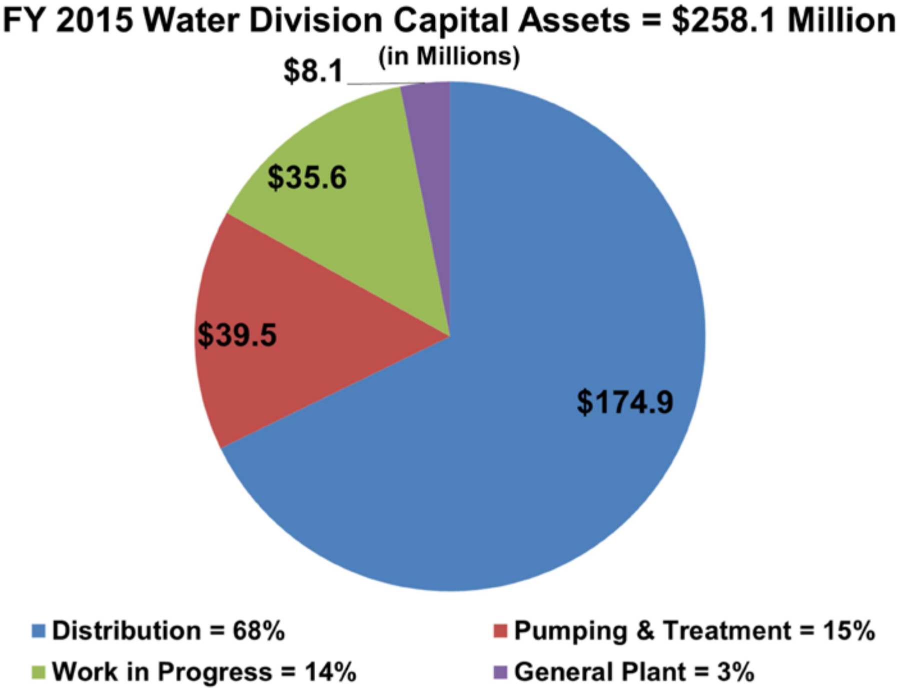
Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, the Division had $258.1 million invested in a variety of capital assets, as reflected in the schedule of capital assets, which represented a net increase (including additions, retirements, and depreciation) of $18.4 million or 7.7 percent over the end of the last fiscal year.



Major capital asset expenditures during the year were as follows:

- $12.5 million for galvanized and cast iron water main replacement
- $7.8 million for major plant and system improvements
- $1.1 million for information system upgrades

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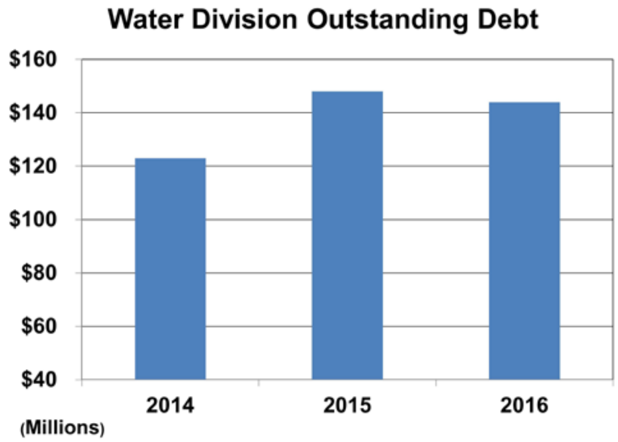
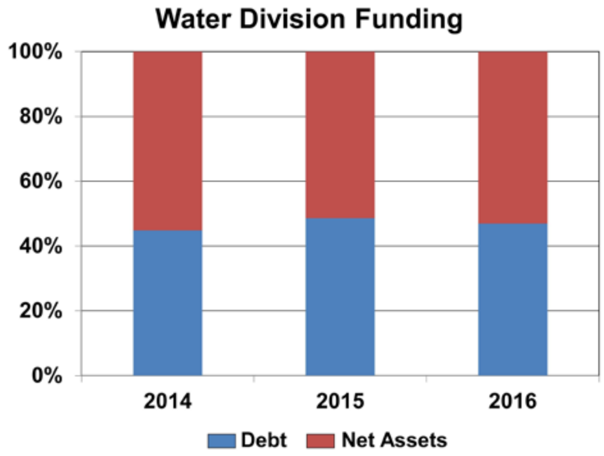
Debt Administration

As of June 30, 2016 the Water Division had $144 million in outstanding water system bonds. The bonds are secured solely by revenues of the Water Division. Debt as a percentage of the Division's capital structure was 46.9 percent in 2016, 48.6 percent in 2015, and 44.8 percent at the end of fiscal year 2014. KUB's Debt Management Policy limits the Division's debt ratio to 60 percent or less.

Outstanding Debt
As of June 30

(in thousands of dollars)	**2016**	**2015**	**2014**
Revenue bonds	$ 143,990	$ 148,400	$ 123,385
Total outstanding debt	$ 143,990	$ 148,400	$ 123,385





The Division will pay $54.1 million in principal payments over the next ten years, representing 37.6 percent of the outstanding bonds. KUB's Debt Management Policy requires a minimum of 30 percent of water debt principal be repaid over the next ten years.

Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, the Division had $144 million in outstanding debt (including the current portion of revenue bonds), compared to $148.4 million last year, a decrease of $4.4 million or 3 percent. The decrease is attributable to the scheduled repayment of bond debt. The Division's weighted average cost of debt as of June 30, 2016 was 3.82 percent.

The Division's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2016, the Division's revenue bonds were rated AAA by Standard & Poor's and Aa2 by Moody's Investors Service. The Standard and Poor's water rating represented the highest credit rating available from Standard and Poor's.

Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, the Division had $148.4 million in outstanding debt (including the current portion of revenue bonds), compared to $123.4 million last year, an increase of $25 million or 20.3 percent. The Division's weighted average cost of debt as of June 30, 2015 was 3.82 percent.

The increase is attributable to the issuance of revenue bonds during the fiscal year of $8 million in August 2014 and $20 million in April 2015. The increase was partially offset by the scheduled repayment of bond debt.

In April 2015, KUB issued $23 million of revenue refunding bonds. The refunding of certain bonds at lower interest rates will provide debt service savings of $2.4 million over the life of the bonds.

The Division's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2015, the Division's revenue bonds were rated AAA by Standard & Poor's and Aa2 by Moody's Investors Service. The Standard and Poor's water rating represented an upgrade for water system bonds and the highest credit rating available from Standard and Poor's. In the rating report on the water system bonds, Standard & Poor's stated "the upgrade is based on the water system's extremely strong financial risk profile, which we view as sustainable over time after reviewing management's long-term financial forecast."

Impacts on Future Financial Position

KUB anticipates adding 100 additional water system customers during fiscal year 2017.

In June 2014, the KUB Board adopted three years of rate increases for all four Divisions to help fund the ongoing Century II infrastructure programs for each system. The first and second rate increases were effective July 2014 and July 2015. The remaining water rate increase will be effective July 2016. The July 2016 rate increase will result in additional annual water system revenue of $2 million.

KUB sold $25 million in water system revenue bonds in July 2016 for the purpose of funding water system capital improvements. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.72 percent.

KUB sold $20.9 million in water system revenue refunding bonds in July 2016 for the purpose of refinancing existing debt at lower interest rates. KUB will realize a total debt service savings of $2.5 million over the life of the bonds ($2.2 million on a net present value basis). The true interest cost of the bonds, which were sold through a competitive bidding process was 2.07 percent.

As part of the rating process for the $25 million in revenue bonds and $20.9 million in revenue refunding bonds, Moody's upgraded its rating on KUB's water system bonds to Aa1 from Aa2. Aa1 is the second to highest bond credit rating assigned by Moody's Investors Service. In its formal rating report, Moody's stated "the upgrade to Aa1 reflects the well-managed financial operations of the water system that continues to provide for solid debt service coverage and liquidity, a mature service area, and a manageable debt profile." The AAA bond rating from Standard and Poor's was reaffirmed. In its formal rating report on the water bonds Standard and Poor's noted "based on our financial management assessment we view KUB to be "1" on a scale of 1-6, with "1" being the strongest."

In April 2016, KUB management presented the fiscal year 2017 budget to the KUB Board of Commissioners that accommodates the projected level of capital investment for the fiscal year. Over the course of the next ten years, KUB plans to spend approximately $108 million dollars on Grid Modernization, of which the Division's share is $24.1 million. In July 2016, the four-year deployment of advanced meters began.

GASB Statement No. 82, *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73* is effective for fiscal years beginning after June 15, 2016. GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* and GASB No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* are effective for periods beginning after June 15, 2017. KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

No other facts, decisions, or conditions are currently known which would have a significant impact on the Division's financial position or results of operations during fiscal year 2016.

Financial Contact

The Division's financial statements are designed to present users (citizens, customers, investors, and creditors) with a general overview of the Division's financial position and results of operations for the fiscal years ending June 30, 2016 and 2015. If you have questions about the statements or need additional financial information, contact KUB's Chief Financial Officer at 445 South Gay Street, Knoxville, Tennessee 37902.

Knoxville Utilities Board Water Division
Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Assets and Deferred Outflows of Resources		
Current assets:		
Cash and cash equivalents	$ 9,392,817	$ 21,304,494
Short-term contingency fund investments	4,293,789	411,198
Other current assets	199,139	198,678
Accrued interest receivable	6,896	5,985
Accounts receivable, less allowance of uncollectible accounts of $58,504 in 2016 and $49,412 in 2015	5,360,089	4,987,019
Inventories	1,221,125	1,037,326
Prepaid expenses	50,480	39,980
Total current assets	20,524,335	27,984,680
Restricted assets:		
Water bond fund	3,354,126	2,969,210
Other funds	2,784	5,707
Unused bond proceeds	-	9,928,179
Total restricted assets	3,356,910	12,903,096
Water plant in service	361,343,360	325,586,934
Less accumulated depreciation	(107,582,378)	(103,077,327)
	253,760,982	222,509,607
Retirement in progress	16,582	94,481
Construction in progress	27,480,060	35,534,671
Net plant in service	281,257,624	258,138,759
Other assets:		
Net pension asset	-	782,812
Long-term contingency fund investments	8,384,342	11,751,074
Other	1,623,210	1,661,676
Total other assets	10,007,552	14,195,562
Total assets	315,146,421	313,222,097
Deferred outflows of resources:		
Pension outflow	1,346,448	410,436
Unamortized bond refunding costs	1,926,554	2,048,783
Total deferred outflows of resources	3,273,002	2,459,219
Total assets and deferred outflows of resources	$ 318,419,423	$ 315,681,316

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Water Division
Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Liabilities, Deferred Inflows, and Net Position		
Current liabilities:		
Current portion of revenue bonds	$ 4,560,000	$ 4,410,000
Sales tax collections payable	284,220	265,897
Accounts payable	2,739,011	1,832,317
Accrued expenses	579,507	486,462
Customer deposits plus accrued interest	804,794	767,050
Accrued interest on revenue bonds	1,834,026	1,599,555
Total current liabilities	10,801,558	9,361,281
Other liabilities:		
Accrued compensated absences	1,601,156	1,524,489
Net pension liability	655,221	-
Other	39,036	110,299
Total other liabilities	2,295,413	1,634,788
Long-term debt:		
Water revenue bonds	139,430,000	143,990,000
Unamortized premiums/discounts	2,702,182	2,866,890
Total long-term debt	142,132,182	146,856,890
Total liabilities	155,229,153	157,852,959
Deferred inflows of resources:		
Pension inflow	196,595	829,180
Total deferred inflows of resources	196,595	829,180
Total liabilities and deferred inflows of resources	155,425,748	158,682,139
Net position		
Net investment in capital assets	138,069,365	110,579,425
Restricted for:		
Debt service	1,520,100	1,369,655
Other	2,784	5,707
Unrestricted	23,401,426	45,044,390
Total net position	162,993,675	156,999,177
Total liabilities, deferred inflows, and net position	$ 318,419,423	$ 315,681,316

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Water Division

Statements of Revenues, Expenses and Changes in Net Position

Years Ended June 30, 2016 and 2015

	2016	**2015**
Operating revenues	$ 47,453,401	$ 44,173,190
Operating expenses		
Treatment	4,186,197	3,789,101
Distribution	12,644,428	13,045,508
Customer service	1,666,099	1,653,476
Administrative and general	4,838,122	4,206,064
Provision for depreciation	9,055,221	7,794,763
Taxes and tax equivalents	3,717,163	3,621,768
Total operating expenses	36,107,230	34,110,680
Operating income	11,346,171	10,062,510
Non-operating revenues (expenses)		
Contributions in aid of construction	895,530	475,386
Interest and dividend income	194,146	134,691
Interest expense	(5,611,878)	(5,421,300)
Amortization of debt costs	(38,926)	1,262
Write-down of plant for costs recovered through contributions	(895,530)	(475,386)
Other	(196,211)	(23,992)
Total non-operating revenues (expenses)	(5,652,869)	(5,309,339)
Change in net position before capital contributions	5,693,302	4,753,171
Capital contributions	301,196	232,696
Change in net position	5,994,498	4,985,867
Net position, beginning of year, as previously reported	156,999,177	152,112,627
Change in method of accounting for pension	-	(99,317)
Net position, beginning of year, as restated	156,999,177	152,013,310
Net position, end of year	$ 162,993,675	$ 156,999,177

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Water Division
Statements of Cash Flows
Years Ended June 30, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Cash receipts from customers	$ 46,572,780	$ 43,258,927
Cash receipts from other operations	1,132,220	585,142
Cash payments to suppliers of goods or services	(13,130,199)	(14,012,339)
Cash payments to employees for services	(10,805,634)	(9,284,435)
Payment in lieu of taxes	(2,976,406)	(2,943,719)
Net cash provided by operating activities	20,792,761	17,603,576
Cash flows from capital and related financing activities:		
Net proceeds from bond issuance	-	27,817,078
Principal paid on revenue bonds and notes payable	(4,410,000)	(3,765,000)
Decrease (increase) in unused bond proceeds	9,928,179	(9,928,179)
Interest paid on revenue bonds and notes payable	(5,377,407)	(5,212,045)
Acquisition and construction of water plant	(32,992,061)	(26,693,360)
Changes in water bond fund, restricted	(384,915)	(86,174)
Proceeds received on disposal of plant	9,435	-
Cash received from developers and individuals for capital purposes	895,530	475,386
Net cash used in capital and related financing activities	(32,331,239)	(17,392,294)
Cash flows from investing activities:		
Purchase of investment securities	(882,048)	(2,243,833)
Maturities of investment securities	410,830	8,053,080
Interest received	193,235	142,666
Other property and investments	(95,216)	(37,162)
Net cash provided by (used in) investing activities	(373,199)	5,914,751
Net increase (decrease) in cash and cash equivalents	(11,911,677)	6,126,033
Cash and cash equivalents, beginning of year	21,304,494	15,178,461
Cash and cash equivalents, end of year	$ 9,392,817	$ 21,304,494
Reconciliation of operating income to net cash provided by operating activities		
Operating income	$ 11,346,171	$ 10,062,510
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	9,331,667	8,008,940
Changes in operating assets and liabilities:		
Accounts receivable	(373,069)	(421,148)
Inventories	(183,799)	(45,461)
Prepaid expenses	(10,500)	5,317
Other assets	(40,478)	(455,412)
Sales tax collections payable	18,323	28,506
Accounts payable and accrued expenses	737,964	308,054
Customer deposits plus accrued interest	37,744	34,791
Other liabilities	(71,262)	77,479
Net cash provided by operating activities	$ 20,792,761	$ 17,603,576
Noncash capital activities:		
Acquisition of plant assets through developer contributions	$ 301,196	$ 232,696

The accompanying notes are an integral part of these financial statements.

1. Description of Business

Knoxville Utilities Board (KUB), comprised of the Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions including setting rates. The Water Division (Division) provides services to certain customers in Knox County and in two surrounding counties in East Tennessee. The Division's accounts are maintained in conformity with the Uniform System of Accounts of the National Association of Regulatory Utility Commissioners (NARUC) and the Governmental Accounting Standards Board (GASB), as applicable. The financial statements present only the Water Division and do not purport to, and do not, present fairly the consolidated financial position of Knoxville Utilities Board at June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

2. Significant Accounting Policies

Basis of Accounting

In conformity with Generally Accepted Accounting Principles (GAAP), KUB follows the provisions of GASB Statement No. 34 (Statement No. 34), *Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* as amended by GASB Statement No. 63 (Statement No. 63), *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position.* Statement No. 34 established standards for external financial reporting for all state and local governmental entities. Under Statement No. 63, financial statements include deferred outflows of resources and deferred inflows of resources, in addition to assets and liabilities, and will report *net position* instead of net assets. In addition, KUB follows GASB Statement No. 62 (Statement No. 62), *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* as it relates to certain items for regulatory accounting. Regulatory accounting allows a regulated utility to defer a cost (a regulatory asset) or recognize an obligation (a regulatory liability) if it is probable that through the rate making process, there will be a corresponding increase or decrease in future revenues. Accordingly, KUB has recognized certain regulatory assets and regulatory liabilities in the accompanying Statements of Net Position.

The financial statements are prepared on the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred. The accounting and financial reporting treatment applied to the Division is determined by measurement focus. The transactions of the Division are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the Statement of Net Position. Net position (i.e., total assets and deferred outflows of resources net of total liabilities and deferred inflows of resources) is segregated into net investment in capital assets, restricted for capital activity and debt service, and unrestricted components.

Recently Adopted New Accounting Pronouncements

In February 2015, the Governmental Accounting Standards Board (GASB) issued Statement No. 72 (Statement No. 72), *Fair Value Measurement and Application.* Statement No. 72 is intended to provide guidance for determining a fair value measurement for financial reporting purposes and for applying fair value to certain investments and disclosures related to all fair value measurements.

In June 2015, the GASB issued GASB Statement No. 73 (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 Provision of GASB Statements 67 and 68.* The requirements of this Statement will improve financial reporting by establishing a single framework for the presentation of information about pensions and enhance comparability.

In June 2015, the GASB issued GASB Statement No. 76 (Statement No. 76), *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to simplify the hierarchy of generally accepted accounting principles (GAAP) used to prepare financial statements of state and local governmental entities. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments,* and amends Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, paragraphs 64, 74, and 82.

In December 2015, the GASB issued GASB Statement No. 79 (Statement No. 79), *Certain External Investment Pools and Pool Participants.* This statement establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes.

Statements No. 72, 73, 76, and 79 are effective for fiscal years beginning after June 15, 2015.

Water Plant

Water plant and other property are stated on the basis of original cost. The cost of current repairs and minor replacements is charged to operating expense. The cost of renewals and improvements is capitalized. The original cost of utility plant assets retired or otherwise disposed of and the cost of removal less salvage value is charged to accumulated depreciation. When other property is retired, the related asset and accumulated depreciation are removed from the accounts, and the gain or loss is included in the results of operations.

The provision for depreciation of water plant in service is based on the estimated useful lives of the assets, which range from three to sixty-seven years, and is computed using the straight-line method. Pursuant to NARUC, the caption "Provision for depreciation" in the Statements of Revenues, Expenses and Changes in Net Position does not include depreciation for transportation equipment of $276,446 in fiscal year 2016 and $214,178 in fiscal year 2015. Under regulatory accounting, interest costs are expensed as incurred with construction of plant assets.

Operating Revenue

Operating revenue consists primarily of charges for services provided by the principal operations of the KUB Water Division. Operating revenue is recorded when the service is rendered, on a cycle basis, and includes an estimate of unbilled revenue. Revenues are reported net of bad debt expense of $140,244 in fiscal year 2016 and $169,110 in fiscal year 2015.

Non-operating Revenue

Non-operating revenue consists of revenues that are related to financing and investing types of activities and result from non-exchange transactions or ancillary activities.

Expense

When an expense is incurred for purposes for which there are both restricted and unrestricted net assets available, it is KUB’s policy to apply those expenses to restricted net assets to the extent such are available and then to unrestricted net assets.

Net Position

GASB Statement No. 63 requires the classification of net position into three components – net investment in capital assets; net position-restricted; and net position-unrestricted.

These classifications are defined as follows:

- Net investment in capital assets – This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt also should be included in this component of net position. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

- Net position-restricted – This component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported.

- Net position-unrestricted – This component of net position consists of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

Contributions in Aid of Construction and Capital Contributions

Contributions in aid of construction are cash collections from customers or others for a particular purpose, generally the construction of new facilities to serve new customers in excess of the investment KUB is willing to make for a particular incremental revenue source. KUB reduces the plant account balances to which contributions relate by the actual amount of the contribution and recognizes the contributions as non-operating revenue in accordance with Statement No. 62.

Capital contributions represent contributions of utility plant infrastructure constructed by developers and others in industrial parks and other developments, and transferred to KUB upon completion of construction and the initiation of utility service. In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, such contributions are recognized as revenues and capital assets upon receipt.

Inventories

Inventories, consisting of plant materials and operating supplies, are valued at the lower of average cost or replacement value.

Change in Method of Accounting for Pension

In June 2012, the Governmental Accounting Standards Board (GASB) issued Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, which revises existing standards of financial reporting for pensions. In addition, during November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, which requires deferred outflow of resources to be recognized for any contributions made subsequent to the measurement date of the beginning net pension liability. These standards were adopted by KUB in 2015 and resulted in a restatement of 2015 beginning net position of $763,975 (Division's share $99,317).

Pension Plan

KUB's employees are participants in the Knoxville Utilities Board Pension Plan as authorized by the Charter of the City of Knoxville §1107(J) (Note 10). KUB's policy is to fully fund the annual actuarially determined contributions. As required by GASB Statement No. 68, KUB measures net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30, 2016 and 2015 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 are based on a December 31, 2015 and 2014 measurement date, respectively.

Investments

Investments are carried at fair value as determined by quoted market prices at the reporting date.

Self-Insurance

KUB has established self-insurance programs covering portions of workers' compensation, employee health, environmental liability, general liability, property and casualty liability, and automobile liability claims. A liability is accrued for claims as they are incurred. When applicable, claims in excess of the self-insured risk are covered by KUB's insurance carrier. Additionally, KUB provides certain lifetime health benefits to eligible retired employees under a self-insurance plan administered by a third party.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates are based on historical experience and various other assumptions that KUB believes are reasonable under the circumstances. However, future events are subject to change and the best estimates and judgments routinely require adjustment. Estimates are used for, but not limited to, inventory valuation, allowance for uncollectible accounts, depreciable lives of plant assets, unbilled revenue volumes, pension trust valuations, OPEB trust valuations, insurance liability reserves, and potential losses from contingencies and litigation. Actual results could differ from those estimates.

Restricted and Designated Assets

Certain assets are restricted by bond resolutions for the construction of utility plant and debt repayment. Certain additional assets are designated by management for contingency purposes and economic development.

Cash Equivalents

For purposes of the Statements of Cash Flows, KUB considers all unrestricted and undesignated highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

Deferred Outflows and Inflows of Resources

Deferred outflows of resources are items previously reported as assets related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. Deferred inflows of resources are items previously reported as liabilities related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. Deferred outflows of resources also include employer pension contributions made subsequent to the measurement date of the net pension liability and before the end of the employer's reporting period in accordance with Statement No. 71. Deferred inflows and deferred outflows also include the net difference between projected and actual earnings on pension plan

investments and differences between expected and actual experience in accordance with Statement No. 68.

Debt Premium/Discount

KUB records unamortized premium and discount on debt as a separate line item in the Long Term Debt section of the Financial Statements. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Debt Issuance Costs

In accordance with regulatory accounting, KUB records debt issuance costs as an Other Asset. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Deferred Gain/Loss on Refunding of Debt

KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Compensated Absences

KUB accrues a liability for earned but unpaid paid-time off (PTO) days.

Subsequent Events

KUB has evaluated events and transactions through October 27, 2016, the date these financial statements were issued, for items that should potentially be recognized or disclosed. KUB sold $25 million in water system revenue bonds in July 2016 for the purpose of funding water system capital improvements in fiscal year 2017. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.72 percent. KUB sold $20.9 million in water system revenue refunding bonds in July 2016 with an average interest rate of 2.5 percent to advance refund $19.9 million of outstanding bonds with an average interest rate of 4.18 percent. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.07 percent. The net proceeds of $22 million (after payment of $0.3 million in underwriting fees and other issuance costs plus premium of $1 million and an additional issuer equity contribution of $0.4 million) were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the bonds. As a result, the bonds will be considered defeased and the liability for those bonds will be removed from the financial statements. This refunding decreases total debt service payments over the next 17 years by $2.5 million resulting in an economic gain (difference between the present values of the debt service payments on the old and new debt) of $2.2 million.

Recently Issued Accounting Pronouncements

In June 2015, the GASB issued two related Statements that affect accounting and financial reporting by state and local governments for postemployment benefits other than pensions (OPEB). GASB Statement No. 74 (Statement No. 74), *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* addresses reporting by OPEB plans that administer benefits on behalf of governments. GASB Statement No. 75 (Statement No. 75), *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* addresses reporting by governments that provide OPEB to their employees. Statement No. 74 is effective for fiscal years beginning after June 15, 2016, and Statement No. 75 is effective for fiscal years beginning after June 15, 2017.

In March 2016, the GASB issued GASB Statement No. 82 (Statement No. 82), *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to the presentation of payroll-related measures in required supplementary information, the selection of assumptions and treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes and the classification of payments made by employers to satisfy employee contribution obligations. Statement No. 82 is effective for fiscal years beginning after June 15, 2016.

KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

3. Deposits and Investments

KUB follows the provisions of Statement No. 40 of the Governmental Accounting Standards Board, *Deposit and Investment Risk Disclosures an amendment of GASB Statement No. 3*. This Statement establishes and modifies disclosure requirements for state and local governments related to deposit and investment risks. KUB classifies its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*.

KUB's investment policy provides the framework for the administration and investment of cash deposits. The investment policy follows Tennessee State law and defines the parameters under which KUB funds should be invested. State law authorizes KUB to invest in obligations of the United States Treasury, its agencies and instrumentalities; certificates of deposit; repurchase agreements; money market funds; and the State Treasurer's Investment Pool.

Interest Rate Risk. KUB's primary investment objectives are to place investments in a manner to ensure the preservation of capital, remain sufficiently liquid to meet all operating requirements, and maximize yield of return. KUB minimizes its exposure to interest rate risk by adhering to Tennessee State law requirements for the investment of public funds. This includes limiting investments to those types described above and limiting maturity horizons. The maximum maturity is four years from the date of investment. KUB also limits its exposure by holding investments to maturity unless cash flow requirements dictate otherwise.

Credit Risk. KUB's investment policy, as required by state law, is to apply the prudent-person rule: Investments are made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable income to be derived, as well as the probable safety of their capital. KUB's Agency Bond investments are rated Aaa by Moody's Investors Service.

Custodial Credit Risk. KUB's investment policy limits exposure to custodial credit risk by restricting insurance limits are collateralized with government securities held in KUB's name by a third-party custodian bank(s) acting as KUB's agent(s), or through the State of Tennessee's collateral pool. Financial institutions that participate in the collateral pool are subject to special assessment; therefore, the deposits are considered insured. A portion of KUB's investments are generally held in the State of Tennessee Local Government Investment Pool (LGIP). The LGIP is a part of the State Pooled Investment Fund and is sponsored by the State of Tennessee Treasury Department. Tennessee Code Annotated ¶9-4-701 *et seq*. authorizes local governments to invest in the LGIP. None of KUB's investments are exposed to custodial credit risk.

Classification of deposits and investments per Statement of Net Position:

	2016	2015
Current assets		
Cash and cash equivalents	$ 9,392,817	$ 21,304,494
Short-term contingency fund investments	4,293,789	411,198
Other assets		
Long-term contingency fund investments	8,350,127	11,726,424
Restricted assets		
Unused bond proceeds	-	9,927,990
Water bond fund	3,354,126	2,969,210
Other funds	2,784	5,707
	$ 25,393,643	$ 46,345,023

The above amounts do not include accrued interest of $34,215 in fiscal year 2016 and $24,839 in fiscal year 2015. Interest income is recorded on an accrual basis.

Investments and maturities of KUB's deposits and investments as held by financial institutions as of June 30, 2016:

	Deposit and Investment Maturities (in Years)		
	Fair Value	Less Than 1	1-5
Supersweep NOW and Other Deposits	$ 10,647,281	$ 10,647,281	$ -
State Treasurer's Investment Pool	1,297,013	1,297,013	-
Agency Bonds	14,914,916	4,293,789	10,621,127
Certificates of deposits	2,305,263	2,057,013	248,250
	$ 29,164,473	$ 18,295,096	$ 10,869,377

KUB categorizes its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*. The hierarchy is based on the valuation inputs used to measure the fair value of an asset with a maturity at purchase greater than one year. 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.

KUB has the following recurring fair value measurements as of June 30, 2016:

- U.S. Agency bonds of $10,621,127, which have a maturity at purchase of greater than one year, are valued using quoted market prices (Level 1 inputs)
- Certificates of deposits of $248,250, which have a maturity at purchase of greater than one year, are valued at interest rates and yield curves observable at commonly quoted intervals (Level 2 inputs)

KUB measures investments with a maturity at purchase of one year or less at amortized cost, which is considered a fair value equivalent due to their nature. Investments in the State Treasurer's Investment Pool are measured at net asset value (NAV) per share.

4. Accounts Receivable

Accounts receivable consists of the following:

	2016	2015
Wholesale and retail customers		
Billed services	$ 3,386,932	$ 3,275,895
Unbilled services	1,846,174	1,596,039
Other	185,487	164,497
Allowance for uncollectible accounts	(58,504)	(49,412)
	$ 5,360,089	$ 4,987,019

5. Accounts Payable and Accruals

Accounts payable and accruals were composed of the following:

	2016	2015
Trade accounts	$ 2,739,011	$ 1,832,317
Salaries and wages	350,902	265,669
Self-insurance liabilities	228,605	220,793
	$ 3,318,518	$ 2,318,779

6. Long-Term Obligations

Long-term debt consists of the following:

	Balance June 30, 2015	Additions	Payments	Defeased	Balance June 30, 2016	Amounts Due Within One Year
S-2005 - 3.5 - 5.0%	$ 6,735,000	$ -	$ 440,000	$ -	$ 6,295,000	$ 465,000
T-2007 - 4.0 - 5.5%	1,450,000	-	700,000	-	750,000	750,000
U-2009 - 3.0 - 4.5%	23,450,000	-	825,000	-	22,625,000	875,000
W-2011 - 2.0 - 4.0%	23,350,000	-	550,000	-	22,800,000	550,000
X-2012 - 3.0 - 5.0%	9,150,000	-	485,000	-	8,665,000	515,000
Y-2013 - 3.0 - 4.0%	9,235,000	-	265,000	-	8,970,000	280,000
Z-2013 - 2.0 - 5.0%	24,150,000	-	475,000	-	23,675,000	500,000
AA-2014 - 2.0 - 4.0%	7,875,000	-	150,000	-	7,725,000	150,000
BB-2015 - 2.0 - 5.0%	23,005,000	-	170,000	-	22,835,000	100,000
CC-2015 - 2.0 - 4.0%	20,000,000	-	350,000	-	19,650,000	375,000
Total bonds	$ 148,400,000	$ -	$ 4,410,000	$ -	$ 143,990,000	$ 4,560,000
Unamortized Premium	2,866,890	-	164,708	-	2,702,182	-
Total long term debt	$ 151,266,890	$ -	$ 4,574,708	$ -	$ 146,692,182	$ 4,560,000

	Balance June 30, 2014	Additions	Payments	Defeased	Balance June 30, 2015	Amounts Due Within One Year
R-2005 - 3.5 - 5.0%	$ 255,000	$ -	$ 255,000	$ -	$ -	$ -
S-2005 - 3.5 - 5.0%	7,160,000	-	425,000	-	6,735,000	440,000
T-2007 - 4.0 - 5.5%	24,350,000	-	675,000	22,225,000	1,450,000	700,000
U-2009 - 3.0 - 4.5%	24,250,000	-	800,000	-	23,450,000	825,000
W-2011 - 2.0 - 4.0%	23,900,000	-	550,000	-	23,350,000	550,000
X-2012 - 3.0 - 5.0%	9,610,000	-	460,000	-	9,150,000	485,000
Y-2013 - 3.0 - 4.0%	9,260,000	-	25,000	-	9,235,000	265,000
Z-2013 - 2.0 - 5.0%	24,600,000	-	450,000	-	24,150,000	475,000
AA-2014 - 2.0 - 4.0%	-	8,000,000	125,000	-	7,875,000	150,000
BB-2015 - 2.0 - 5.0%	-	23,005,000	-	-	23,005,000	170,000
CC-2015 - 2.0 - 4.0%	-	20,000,000	-	-	20,000,000	350,000
Total bonds	$ 123,385,000	$ 51,005,000	$ 3,765,000	$ 22,225,000	$ 148,400,000	$ 4,410,000
Unamortized Premium	1,518,734	1,493,612	102,471	42,985	2,866,890	-
Total long term debt	$ 124,903,734	$ 52,498,612	$ 3,867,471	$ 22,267,985	$ 151,266,890	$ 4,410,000

Debt service over remaining term of the debt is as follows:

Fiscal Year	Total Principal	Interest	Grand Total
2017	$ 4,560,000	$ 5,502,077	$ 10,062,077
2018	4,710,000	5,308,927	10,018,927
2019	4,870,000	5,127,527	9,997,527
2020	5,100,000	4,923,477	10,023,477
2021	5,280,000	4,746,427	10,026,427
2022 - 2026	29,580,000	20,683,800	50,263,800
2027 - 2031	34,690,000	14,947,082	49,637,082
2032 - 2036	26,225,000	8,892,033	35,117,033
2037 - 2041	19,725,000	4,382,187	24,107,187
2042 - 2045	9,250,000	901,469	10,151,469
Total	$ 143,990,000	$ 75,415,006	$ 219,405,006

The Division has pledged sufficient revenue, after deduction of all current operating expenses (exclusive of tax equivalents), to meet bond principal and interest payments when due. The requirements for the bonds are being met through monthly deposits to the Water Bond Fund, as required by the bond covenants. As of June 30, 2016, these bond covenants had been satisfied.

During fiscal year 2006, KUB's Water Division issued Series S 2005 bonds to retire certain existing debt and fund water system capital improvements. Concurrent with the issuance of these bonds, KUB transferred funds to an irrevocable trust to pay a portion of the Series P 2001 bonds, as such amounts mature.

During fiscal year 2008, KUB's Water Division issued Series T 2007 bonds to fund water system capital improvements.

During fiscal year 2010, KUB's Water Division issued Series U 2009 bonds to fund water system capital improvements.

During fiscal year 2012, KUB's Water Division issued Series W 2011 bonds to fund water system capital improvements. KUB's Water Division also issued Series X 2012 bonds to retire Series Q 2004 bonds.

During fiscal year 2013, KUB's Water Division issued Series Y 2013 bonds to retire a portion of outstanding Series R 2005 bonds.

During fiscal year 2014, KUB's Water Division issued Series Z 2013 bonds to fund water system capital improvements.

During fiscal year 2015, KUB's Water Division issued Series BB 2015 bonds to retire a portion of outstanding Series T 2007 bonds. KUB's Water Division also issued Series AA 2014 and Series CC 2015 bonds to fund water system capital improvements.

In prior years, certain revenue bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the liability for the defeased bonds, $22.2 million at June 30, 2016, and the trust account assets are not included in the financial statements.

Other liabilities consist of the following:

	Balance June 30, 2015	Increase	Decrease	Balance June 30, 2016
Accrued compensated absences	$ 1,524,489	$ 2,496,404	$ (2,419,737)	$ 1,601,156
Other	110,299	117,737	(189,000)	39,036
	$ 1,634,788	$ 2,614,141	$ (2,608,737)	$ 1,640,192

7. Lease Commitments

KUB has non-cancelable operating lease commitments for office equipment, property, and vehicles, summarized for the following fiscal years:

2017	$ 59,805
2018	57,857
2019	33,869
2020	1,065
Total operating minimum lease payments	$ 152,596

8. Capital Assets

Capital asset activity was as follows:

	Balance June 30, 2015	Increase	Decrease	Balance June 30, 2016
Production Plant	$ 727,863	$ -	$ -	$ 727,863
Pumping & Treatment Plant	65,525,607	12,961,992	(280,318)	78,207,281
Distribution Plant				
Distribution Mains	156,114,567	17,443,111	(798,145)	172,759,533
Transmission Mains	27,338,065	3,580,781	(471,020)	30,447,826
Services & Meters	29,722,371	2,759,765	(2,537,255)	29,944,881
Other Accounts	22,220,382	1,321,165	(370,155)	23,171,392
Total Distribution Plant	$ 235,395,385	$ 25,104,822	$ (4,176,575)	$ 256,323,632
Total General Plant	23,938,079	2,603,382	(456,877)	26,084,584
Total Water Plant	$ 325,586,934	$ 40,670,196	$ (4,913,770)	$ 361,343,360
Less Accumulated Depreciation	(103,077,327)	(9,373,580)	4,868,529	(107,582,378)
Net Plant Assets	$ 222,509,607	$ 31,296,616	$ (45,241)	$ 253,760,982
Work In Progress	35,629,152	32,415,132	(40,547,642)	27,496,642
Total Net Plant	$ 258,138,759	$ 63,711,748	$ (40,592,883)	$ 281,257,624

	Balance June 30, 2014	Increase	Decrease	Balance June 30, 2015
Production Plant	$ 727,863	$ -	$ -	$ 727,863
Pumping & Treatment Plant	65,538,290	229,177	(241,860)	65,525,607
Distribution Plant				
Distribution Mains	145,877,358	10,657,161	(419,952)	156,114,567
Transmission Mains	27,261,415	84,477	(7,827)	27,338,065
Services & Meters	29,841,733	882,602	(1,001,964)	29,722,371
Other	21,679,780	690,660	(150,058)	22,220,382
Total Distribution Plant	$ 224,660,286	$ 12,314,900	$ (1,579,801)	$ 235,395,385
Total General Plant	22,552,206	1,612,164	(226,291)	23,938,079
Total Water Plant	$ 313,478,645	$ 14,156,241	$ (2,047,952)	$ 325,586,934
Less Accumulated Depreciation	(97,290,740)	(8,049,680)	2,263,093	(103,077,327)
Net Plant Assets	$ 216,187,905	$ 6,106,561	$ 215,141	$ 222,509,607
Work In Progress	23,517,782	26,268,395	(14,157,025)	35,629,152
Total Net Plant	$ 239,705,687	$ 32,374,956	$ (13,941,884)	$ 258,138,759

9. Risk Management

KUB is exposed to various risks of loss related to active and retiree medical claims; injuries to workers; theft of, damage to, and destruction of assets; environmental damages; and natural disasters. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported.

These liabilities are included in accrued expenses in the Statement of Net Position. The liability is KUB's best estimate based on available information. At June 30, 2016 and 2015, the amount of these liabilities was $228,605 and $220,793, respectively, resulting from the following changes:

	2016	**2015**
Balance, beginning of year	$ 220,793	$ 204,465
Current year claims and changes in estimates	1,825,029	1,840,260
Claims payments	(1,817,217)	(1,823,932)
Balance, end of year	$ 228,605	$ 220,793

10. Pension Plan

Description of Plan

The Knoxville Utilities Board Pension Plan (the Plan) is a governmental plan as defined by the Employee Retirement Income Security Act of 1974 ("ERISA" or the "Act"), is not subject to any of the provisions of the Act, and was revised January 1, 2014 to include all prior approved amendments. The Plan is a single-employer contributory, defined benefit pension plan established by Knoxville Utilities Board ("KUB") Resolution No. 980 dated February 18, 1999, effective July 1, 1999, as authorized by the Charter of the City of Knoxville §1107(J). The Plan is designed to provide retirement, disability and death benefits to KUB employees. KUB administers the Plan through an Administrative Committee consisting of seven KUB employees that are appointed by KUB's President and CEO. Any amendments to the Plan involving costs not approved in the operating budget must be adopted by KUB's Board of Commissioners, upon recommendation by KUB's President and CEO. All other amendments to the Plan may be approved by KUB's President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The Plan issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017. For purposes of this disclosure, presentation is on a consolidated basis unless division's share is specified.

Effective January 1, 2011, KUB closed the Plan such that persons employed or re-employed by KUB on or after January 1, 2011, are not eligible to participate, but that eligible employees hired prior to January 1, 2011, who have not separated from service, shall continue as Participants and to accrue benefits under the Plan.

Participants in the Plan consisted of the following as of December 31:

	2015	2014
Inactive plan members:		
Terminated vested participants	39	40
Retirees and beneficiaries	628	627
Active plan members	692	725
Total	1,359	1,392

Retirement Benefits

The Plan provides three benefit arrangements for KUB participants, retirees, and beneficiaries.

The Plan provides pension benefits through the Career Equity Program ("CEP") for eligible employees hired on or after January 1, 1999, and for eligible former "City System Plan A" participants who elected CEP coverage as of July 1, 1999. The guaranteed pension benefit payable to a participant who has completed five or more years of service (or reached the normal retirement date, if earlier) upon termination of KUB employment shall be a lump sum equal to the participant's average compensation times their benefit percentage, as defined in the Plan document, or an annuity may be chosen by the participant.

In addition, the Plan provided retirement benefits through "Plan A" for former City System Plan A participants who elected not to participate in the CEP. Plan A is a closed plan and is not available to KUB employees hired after July 1, 1999. Plan A provides for early retirement benefits with 25 years of service and normal retirement benefits at age 62 or later. Benefits provided to Plan A participants include several different forms of monthly annuity payments.

The Plan also provides retirement benefits through "Plan B" for former "City System Plan B" participants. Plan B is a closed plan providing benefits to participants not covered by Social Security. Benefits provided to Plan B participants include several different forms of monthly annuity payments available to participants.

Effective January 1, 2012, KUB began to provide for additional monthly supplements, which will not be subject to cost of living adjustments, to certain former employees and surviving dependents of former employees who are eligible for and have elected coverage under the KUB retiree medical plan and are eligible for Medicare. This was done to address the loss of drug coverage under the KUB retiree medical plan and to assist such individuals in obtaining prescription drug coverage under Medicare Part D.

Contributions

Participation in Plan A requires employee contributions of 3 percent of the first $4,800 of annual earnings and 5 percent of annual earnings in excess of $4,800. Plan B participants may not make contributions to the Plan. KUB contributions are determined by the enrolled actuary of the Plan and equal the amount necessary to provide the benefits under the Plan determined by the application of accepted actuarial methods and assumptions. The method of funding shall be consistent with Plan objectives.

Plan Funding

KUB maintains a Funding Policy for the Plan in accordance with Tennessee State Law. The primary goal of the Policy is to document the method KUB has adopted to provide assurance that future KUB and employee contributions and current Plan assets will be sufficient to fund all benefits expected to be paid to current active, inactive and retired Plan participants and their beneficiaries. Per the Funding Policy, KUB fully funds its annual Actuarially Determined Contribution.

Investments

The Plan's investments are held by State Street Bank and Trust Company (the "Trustee"). The Plan's policy in regard to the allocation of invested assets is established by the Investment Committee and approved by the KUB Board of Commissioners and may only be amended by the KUB Board of Commissioners. It is the policy of the Investment Committee to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes. The following was the Plan's adopted asset allocation policy as of December 31, 2015:

Asset Class	Target Allocation
Domestic equity – large cap	20% - 50%
Domestic equity – mid cap	0% - 15%
Domestic equity – small cap	0% - 15%
Domestic equity - convertible securities	0% - 10%
Non-U.S. equity	0% - 20%
Real estate equity	0% - 10%
Fixed income – aggregate bonds	5% - 25%
Fixed income – long-term bonds	10% - 25%
Cash and deposits	0% - 5%

Contributions of $5,669,380 and $6,314,399 for 2014 and 2013, respectively, were made during KUB's fiscal years ending June 30, 2016 and 2015, respectively. Of these amounts, $737,019 and $820,872 are attributable to the Water Division. The contribution was determined as part of the January 1, 2014 valuation using the Individual Entry Age Normal funding method. The objective under this method is to fund each participant's benefits under the Plan as payments which are level as a percentage of salary, starting on the original participation date (employment date) and continuing until the assumed retirement, termination, disability or death. The actuarial valuation for the Plan year ending December 31, 2015 resulted in an actuarially determined contribution of $4,816,913 for the fiscal year ending June 30, 2017, based on the Plan's current funding policy. The Water Division's portion of this contribution is $626,199.

Subsequent to June 30, 2016, the actuarial valuation for the Plan year ending December 31, 2016 was completed. The actuarial valuation resulted in an actuarially determined contribution of $3,756,283 for the fiscal year ending June 30, 2018, based on the Plan's current funding policy. The Water Division's portion of this contribution is $488,317. For the Plan year ending December 31, 2016, the Plan's actuarial funded ratio was 103.04 percent.

The actuarial valuations for the Plan years ending December 31, 2015 and 2016, which determine the actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Implementation of GASB 68

In fiscal year 2015, KUB adopted GASB Statement No. 68*, Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*("GASB 68"), which requires measurement of the net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 will be based on the December 31, 2015 and 2014 measurement date, respectively. The Division's share of the net pension liability at June 30, 2016 is $655,221 and the net pension asset at June 30, 2015 is $782,812.

GASB 68 requires certain disclosures related to the net pension liability of the Plan as disclosed below:

		2015		**2014**
Total pension liability	$	204,502,350	$	202,773,764
Plan fiduciary net position		199,462,190		(208,795,394)
Plan's net pension liability (asset)	$	5,040,160	$	(6,021,630)
Plan fiduciary net position as a percentage of the total pension liability		97.54%		102.97%

Changes in Net Pension Liability are as follows:

		Total Pension Liability (a)		Increase (Decrease) Plan Fiduciary Net Position (b)		Net Pension Liability (a) - (b)
Balances at December 31, 2014	$	202,773,764	$	208,795,394	$	(6,021,630)
Changes for the year:						
Service cost		4,157,062		-		4,157,062
Interest		14,812,784		-		14,812,784
Differences between Expected and Actual Experience		(1,890,334)		-		(1,890,334)
Changes of Assumptions		-		-		-
Contributions - employer		-		5,991,887		(5,991,887)
Contributions - rollovers		-		482,060		(482,060)
Contributions - member		-		5,486		(5,486)
Net investment income		-		(64,551)		64,551
Benefit payments		(15,350,926)		(15,350,926)		-
Administrative expense		-		(397,160)		397,160
Net changes		1,728,586		(9,333,204)		11,061,790
Balances at December 31, 2015	$	204,502,350	$	199,462,190	$	5,040,160

Actuarial Assumptions

The total pension liability was determined by an actuarial valuation as of December 31, 2015 and 2014, using the following actuarial assumptions, applied to all periods included in the measurement:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.80% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the January 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation
Inflation	2.8 percent

The actuarial assumptions used in the December 31, 2015 valuation were based on the results of an actuarial experience study for the period January 1, 2009 through December 31, 2013.

The long-term expected rate of return on Plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of Plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the Plan's target asset allocation as of December 31, 2015 and 2014 are summarized in the following table. The real rate of return reported for fixed income is for aggregate fixed income. The Plan has both aggregate and long duration fixed income.

	Long Term Expected Real Rate of Return	
Asset Class	**2015**	**2014**
Domestic equity	7.2%	6.0%
Non-U.S. equity	7.4%	7.0%
Real estate equity	6.5%	5.7%
Fixed income	3.7%	1.8%
Cash and deposits	2.6%	0.5%

Discount rate

The discount rate used to measure the total pension liability was 7.5 percent as of January 1, 2015 and 2014. The projection of cash flows used to determine the discount rate assumed that participant contributions will be made at the current contribution rate and that KUB contributions will be made at rates equal to the actuarially determined contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the net pension liability to changes in the discount rate

The following presents the net pension liability of the Plan as of December 31, 2015, calculated using the discount rate of 7.5 percent, as well as what the Plan's net pension liability would be if it were calculated using a discount rate that is one percent lower (6.5 percent) or one percent higher (8.5 percent) than the current rate:

	1% Decrease (6.5%)	**Current Discount Rate (7.5%)**	**1% Increase (8.5%)**
Plan's net pension liability	$ 17,128,897	$ 5,040,160	$ (5,963,331)

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

For the year ended June 30, 2015, KUB recognized pension expense of $2,749,905 (Division’s share $357,488).

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in expense over the average expected remaining service life of all active and inactive members. As of the measurement date, this recognition period was 3.72 years. However, there were no experience gains or losses, and there were no assumption changes during the measurement year.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment gain of $7,972,887. $1,594,577 of that gain was recognized in the current year and an identical amount will be recognized in each of the next four years, resulting in a deferred inflow of resources of $6,378,310 (Division’s share $829,180). The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over the next five years. In addition, KUB recorded a deferred outflow of resources of $3,157,199 (Division’s share $410,436) at June 30, 2015 for employer contributions made between December 31, 2014 and June 30, 2015.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ -
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	-	6,378,310
Contributions subsequent to measurement date	3,157,199	-
Total	$ 3,157,199	$ 6,378,310

For the year ended June 30, 2016, KUB recognized pension expense of $4,665,035 (Division’s share $606,455).

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in the pension expense over the average expected remaining service life of all active and inactive members, determined as of the beginning of the measurement period. As of December 31, 2014, this average was 5.00 years. During the measurement year, there were no assumption or benefit changes. There was an experience gain of $1,890,334 with $378,067 of that recognized in the current year and in each of the next four years.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment loss of $15,382,915. $3,076,583 of that loss was recognized in the current year and an identical amount will be recognized in each of the next four years. Unrecognized investment gains from prior periods were $6,378,310 of which $1,594,577 was recognized as a reduction in pension expense in the current year.

Experience gains this year created a deferred inflow of resources of $1,512,267 (Division's share $196,595). The combination of unrecognized investment losses this year along with unrecognized net investment gains from prior periods results in a deferred outflow of resources as of December 31, 2015 of $7,522,599 (Division's share $977,938). The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over future years. In addition, KUB recorded a deferred outflow of resources of $2,834,692 (Division's share $368,510) at June 30, 2016 for employer contributions made between December 31, 2015 and June 30, 2016.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ 1,512,267
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	7,522,599	-
Contributions subsequent to measurement date	2,834,692	-
Total	$ 10,357,291	$ 1,512,267

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

Year ended June 30:	
2017	$ 3,938,630
2018	1,103,939
2019	1,103,938
2020	2,698,517
Thereafter	-

11. Defined Contribution Plan

The KUB Asset Accumulation 401(k) Plan (the "401(k) Plan") is a defined contribution 401(k) employee retirement savings plan covering eligible KUB employees established by the KUB Board of Commissioners in accordance with the Charter of the City of Knoxville, Tennessee. The 401(k) plan's assets are held in trust under an agreement between KUB and Fidelity Management Trust Company. Employees hired prior to January 1, 2011 may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. Employees hired on or after January 1, 2011 have an enhanced 401(k) due to the closure of the Defined Benefit Pension Plan. They may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. They also receive a nonelective KUB contribution of from 3 percent to 6 percent, depending on years of service, whether they contribute or not.

Matching contributions were previously remitted to the KUB Pension Plan (a separate defined benefit plan) in the name of the participant for employees hired prior to January 1, 2011. As of December 9, 2015, these Pension match assets moved from the KUB Pension Plan to the 401(k) Plan. Effective December 9, 2015, all matching contributions are remitted to the 401(k) Plan. The match and nonelective contributions for employees hired on or after January 1, 2011 are paid directly by KUB. KUB funded 401(k) matching contributions and nonelective contributions of

$1,739,057 (Division's share $226,077) and $1,593,350 (Division's share $207,135), respectively, for the years ended June 30, 2016 and 2015.

12. Other Post-Employment Benefits (OPEB)

The Governmental Accounting Standards Board (GASB) established standards for the measurement, recognition, and reporting of other post-employment benefits (OPEB). OPEB includes post-employment benefits other than pension, which, for KUB, is presently limited to post-employment health care. GASB Statement No. 45 (Statement No. 45) requires the recognition of the accrued OPEB liability for the respective year, plus the disclosure of the total unfunded liability.

KUB currently provides post-employment health care benefits to 585 former employees and 593 covered dependents. The cost of coverage is shared with retirees and beneficiaries. KUB recognizes its share of the cost of post-employment health care benefits as an expense as claims are paid.

KUB amended its Group Health Plan in 1999, eliminating post-employment health care benefits for all employees hired on or after July 1, 1999. As of June 30, 2016, 356 active employees were eligible for individual and dependent coverage at separation. To qualify, the employee must meet the Rule of 80 (age plus years of service) with a minimum of 20 years of service, and be enrolled in medical coverage on their last day.

In May 2006, the State of Tennessee adopted Tennessee Code Annotated, Title 8, Chapter 50, Part 12 authorizing governmental entities to establish Trusts for the purpose of pre-funding their respective OPEB liabilities.

Although Statement No. 45 does not require pre-funding of the liability, KUB has determined that it is in the long-term economic interest of KUB and its ratepayers to establish a Trust to pre-fund KUB's OPEB liability.

Knoxville Utilities Board Other Post-Employment Benefits Trust (the "Trust") is a single-employer Other Post-Employment Benefits Plan established by the Knoxville Utilities Board (KUB) Board of Commissioners through Resolution No. 1168, as amended, dated October 18, 2007. The applicable documentation was submitted to the State Funding Board and, in December 2007, the State Funding Board approved the Trust. The Trust was also approved by the Internal Revenue Service in June 2008. KUB administers the Trust through a Board of Trustees consisting of seven KUB employees that are appointed by KUB's President and CEO. Any amendments to the Trust involving costs not approved in the operating budget must be approved by KUB's Board of Commissioners, upon recommendation by KUB's President and CEO. All other amendments to the Trust may be approved by KUB's President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The investment of all deposits to the Trust is governed by an Investment Policy, which was adopted by the KUB Board and approved by the State Funding Board.

KUB makes annual contributions to the Trust at an actuarially determined rate. Based on the date of retirement, certain retired plan members are required to contribute specified amounts monthly to maintain health insurance. Those who retired prior to July 1983 have no required monthly premiums for themselves or dependents. The retirees, or their surviving dependents, who retired between August 1983 and January 1998 are required to pay $250 per month for pre-Medicare family health insurance. For individuals who retired after January 1998, the required monthly premium for pre-Medicare health insurance is $250 for single coverage and $500 for family coverage. There is currently no premium for Medicare eligible retirees or dependents.

An actuarial valuation of KUB's Postretirement Benefit Plan was performed for the Trust as of January 1, 2014 for fiscal year June 30, 2015 and January 1, 2015 for fiscal year June 30, 2016.

The following table presents the OPEB cost for the year, the amount contributed to the Trust, and changes in the net OPEB obligation for fiscal year ending June 30:

		2016	**2015**
a)	Net OPEB Obligation/(Asset) at beginning of fiscal year	$ (174,410)	$ (177,322)
b)	Annual Required Contribution (ARC)	953,221	3,497,372
c)	Interest on Net OPEB Obligation/(Asset)	(13,081)	(14,186)
d)	Adjustment to ARC	(16,427)	(17,098)
e)	Annual OPEB Cost **(b+c-d)**	956,567	3,500,284
f)	Employer Contributions	953,221	3,497,372
g)	Net OPEB Obligation/(Asset) at end of fiscal year **(a+e-f)**	$ (171,064)	$ (174,410)

KUB's annual OPEB cost, the percentage of annual OPEB cost contributed to the Trust, and the net OPEB obligation for fiscal year 2016 and the two preceding years were as follows:

Schedule of Employer Contributions

Actuarial Valuation Date	**Employer Fiscal Year**	**Annual Required Contribution**	**Fiscal Year Actual Contribution**	**Percentage Contributed**	**Net OPEB Obligation**
1/1/2012	6/30/2014	3,327,412	4,057,091	121.93%	(177,322)
1/1/2013	6/30/2015	3,497,372	3,497,372	100.00%	(174,410)
1/1/2014	6/30/2016	953,221	953,221	100.00%	(171,064)

Total contributions to the OPEB Trust for the fiscal year ended June 30, 2016 were $953,221 (Division's share $123,919). The contribution to the Trust was consistent with the annual required contribution, as determined by the Postretirement Benefit Plan's actuarial valuation as of January 1, 2014, which was $953,221 (Division's share $123,919). As of June 30, 2016, the employer's OPEB obligation has been exceeded by $171,064 (Division's share $22,238).

The annual required contribution for the fiscal year ending June 30, 2017, as determined by the Plan's actuarial valuation as of January 1, 2015 is $620,015 (Division's share $80,602).

The actuarial valuation for the Plan as of January 1, 2016 has been completed. The valuation determined that the Plan's actuarial accrued liability was $45,118,624 (Division's share $5,865,421). The actuarial value of the Plan's assets was $48,510,796 (Division's share $6,306,403). As a result, the Plan's unfunded actuarial accrued liability was ($3,392,172) (Division's share ($440,982)). The Plan's actuarial funded ratio was 108 percent. Due to the future implementation of GASB 75, the contributions made for fiscal year ending June 30, 2018 will be the actuarially determined contribution instead of the annual required contribution and the actuarial cost method used to determine the contributions will change from the projected unit credit cost method to the entry age normal cost method. The actuarially determined contribution for fiscal year ending June 30, 2018 will be zero. See Required Supplementary Information for OPEB Schedule of Funding Progress.

The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution and actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

The required schedule of funding progress immediately following the notes to the financial statements presents multi-year trend information about whether the actuarial value of Trust assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point.

Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

Identification of actuarial methods and significant assumptions used to determine the annual required contribution for the fiscal year ending June 30, 2016:

I. Actuarial cost method	Projected unit credit cost method
II. Actuarial value of assets	Smoothed market value with phase-in method using a smoothing period of 5 years
III. Investment return	7.5%, based on the expected portfolio return
Projected salary increases	N/A
Healthcare cost Trend:	
Medicare	2014 - 2030+, ranging from 4.5% to 7.45%
Non-Medicare	2014 - 2030+, ranging from 4.5% to 8.75%
IV. Amortization method	Level dollar closed (30-year)
Remaining amortization period	22 years

The Trust issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017.

13. Related Party Transactions

The Division, in the normal course of operations, is involved in transactions with the City of Knoxville and with other divisions of KUB. Such transactions for the years ended June 30, 2016 and 2015 are summarized as follows:

	2016	**2015**
City of Knoxville		
Amounts billed by the Division for utilities and related services	$ 4,005,989	$ 3,894,557
Payments by the Division in lieu of property tax	2,976,406	2,943,719
Payments by the Division for services provided	607,858	507,095
Other divisions of KUB		
Amounts billed to other divisions for utilities and related services provided	397,610	327,109
Interdivisional rental expense	207,433	214,469
Interdivisional rental income	127,304	92,415
Amounts billed to the Division by other divisions for utilities services provided	2,811,375	2,964,224

With respect to these transactions, accounts receivable from the City of Knoxville included in the balance sheet at year end were:

	2016	**2015**
Accounts receivable	$ 325,488	$ 295,804

14. Other Commitments and Contingencies

In the normal course of business, there are various lawsuits pending against KUB. Management has reviewed these lawsuits with counsel, who is vigorously defending KUB's position and is of the opinion that the ultimate disposition of these matters will not have a material adverse effect on KUB's financial position, results of operations or cash flows.

Knoxville Utilities Board Water Division

Required Supplementary Information – Schedule of Funding Progress

June 30, 2016

(Unaudited)

Other Post-Employment Benefits (OPEB)

Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a)/(b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b)-(a)]/(c)
January 1, 2008	$ -	$ 108,329,141	$ 108,329,141	0%	$ 31,234,509	346.8%
January 1, 2009	14,593,487	100,726,738	86,133,251	14%	31,846,091	270.5%
January 1, 2010	21,275,643	58,475,364	37,199,721	36%	30,069,028	123.7%
January 1, 2011	40,749,815	64,289,254	23,539,439	63%	28,878,791	81.5%
January 1, 2012	37,907,357	61,603,466	23,696,109	62%	28,269,123	83.8%
January 1, 2013	38,571,803	63,341,531	24,769,728	61%	27,566,340	89.9%
January 1, 2014	43,409,955	46,889,808	3,479,853	93%	26,724,154	13.0%
* January 1, 2015	47,705,478	47,745,640	40,162	100%	25,816,884	0.2%
* January 1, 2016	48,510,796	45,118,624	(3,392,172)	108%	25,243,127	(13.4%)

* The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Knoxville Utilities Board Water Division

Required Supplementary Information – Schedule of Changes in Net Pension Liability and Related Ratios

June 30, 2016

(Unaudited)

	Year ended December 31	
	2015	2014
Total pension liability		
Service cost	$ 4,157,062	$ 4,092,808
Interest	14,812,784	14,698,657
Differences between expected and actual experience	(1,890,334)	-
Benefit payments, including refunds of member contributions	(15,350,926)	(15,533,167)
Net change in total pension liability	1,728,586	3,258,298
Total pension liability - beginning	202,773,764	199,515,466
Total pension liability - ending (a)	$ 204,502,350	$ 202,773,764
Plan fiduciary net position		
Contributions - employer	$ 5,991,887	$ 5,908,541
Contributions - participants	487,546	475,854
Net investment income	(95,430)	22,292,369
Other additions	30,879	29,733
Benefit payments, including refunds of member contributions	(15,274,926)	(15,405,167)
Administrative expense	(397,160)	(378,085)
Death benefits	(76,000)	(128,000)
Net change in plan fiduciary net position**	(9,333,204)	12,795,245
Plan fiduciary net position - beginning**	208,795,394	196,000,149
Plan fiduciary net position - ending (b)**	$ 199,462,190	$ 208,795,394
Plan's net pension liability - ending (a) - (b)	$ 5,040,160	$ (6,021,630)
Plan fiduciary net position as a percentage of the total pension liability	97.54%	102.97%
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Plan's net pension liability as a percentage of covered-employee payroll	9.95%	(11.98%)

Notes to Schedule:

* Information not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented in 2014.

** Excludes amounts related to 401(k) matching contributions.

Knoxville Utilities Board Water Division
Required Supplementary Information – Schedule of Employer Pension Contributions
June 30, 2016
(Unaudited)

	Year ended December 31	
	2015	2014
Annual required contribution	$ 5,991,887	$ 5,908,541
Contribution in relation to the annual required contribution	5,991,887	5,908,541
Contribution deficiency	$ -	$ -
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Contributions as a percentage of covered-employee payroll	11.82%	11.76%

Notes to Schedule:

Valuation Dates:	January 1, 2013 and January 1, 2014
Timing:	Actuarially determined contributions for a plan year are based upon 50% of the amounts determined at the actuarial valuations for each of the two prior plan years.

Key methods and assumptions used to determine contribution rates:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014.
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.8% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the Janaury 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation.
Inflation:	2.8 percent

* Schedule of Employer Contribution information is not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented 2014.

Knoxville Utilities Board Water Division

Supplemental Information - Schedule of Insurance in Force

June 30, 2016

(Unaudited) Schedule 1

Insurance coverage is for KUB as a consolidated entity.

Crime

Covers losses resulting from employee dishonesty, robbery, burglary, and computer fraud. Limits of coverage - $5,000,000; $250,000 retention.

Directors' and Officers' Liability Insurance

Covers KUB personnel appropriately authorized to make decisions on behalf of KUB (including but not limited to Commissioners, President and CEO, Senior Vice Presidents, Vice Presidents, and Directors) for wrongful acts. Limits of coverage - $20,000,000; $1,000,000 corporate deductible, $0 individual deductible.

Employment Practices Liability

Coverage for costs related to actual or alleged employment practices violations for amounts exceeding specified amount ($500,000). Limits of coverage - $10,000,000.

Fiduciary

Covers losses resulting from wrongful acts related to KUB's Pension, 401(k), and OPEB Trust funds. Limits of coverage - $10,000,000; $150,000 deductible.

Pollution Legal Liability

New conditions coverage for losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - $20,000,000.

Property Insurance

This coverage provides protection of KUB's property for fire, extended coverage, vandalism and malicious mischief, and coverage on boilers and machinery. Also included are flood and earthquake damage and mechanical failure. Limits of coverage - $250,000,000 per occurrence (subject to certain sublimits); $2,500,000 deductible per occurrence.

Travel Accident

Covers losses related to employees' business travel. Limits of coverage - $1,500,000 aggregate.

Excess Insurance for General Liability

As a government entity, KUB's liability is limited under the Tennessee Governmental Tort Liability Act (TCA §29-20-403). KUB is self-insured for up to the first $700,000 of any accident and has insurance of $1,000,000 above this retention.

Excess Insurance for Workers' Compensation

Covers all losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - Statutory; stop loss coverage applies for aggregate losses over $5,000,000.

Employee Health Plan Stop Loss Coverage

KUB's employee health plan is self-funded. KUB has purchased stop loss insurance, which covers KUB's exposure to annual expenses in excess of $400,000 per individual participant.

Knoxville Utilities Board Water Division
Supplemental Information - Schedule of Debt Maturities by Fiscal Year
June 30, 2016
(Unaudited)

Schedule 2

Continued on Next Page

	S-2005		T-2007		U-2009		W-2011		X-2012		Y-2013	
FY	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**
16-17	465,000	267,521	750,000	41,250	875,000	931,625	550,000	871,750	515,000	345,750	280,000	282,200
17-18	485,000	244,271			925,000	896,625	550,000	844,250	535,000	320,000	300,000	273,800
18-19	500,000	224,871			950,000	859,625	550,000	827,750	565,000	293,250	320,000	261,800
19-20	520,000	204,871			1,000,000	821,625	550,000	805,750	590,000	265,000	340,000	249,000
20-21	545,000	183,421			1,050,000	781,625	550,000	789,250	625,000	235,500	350,000	235,400
21-22	570,000	160,940			1,125,000	739,625	550,000	772,750	655,000	204,250	375,000	221,400
22-23	590,000	137,428			1,175,000	694,625	500,000	756,250	670,000	184,600	400,000	210,150
23-24	615,000	112,353			1,225,000	647,625	500,000	741,250	690,000	164,500	415,000	198,150
24-25	640,000	86,215			1,300,000	598,625	500,000	726,250	710,000	143,800	435,000	185,700
25-26	665,000	58,695			1,350,000	546,625	500,000	710,625	735,000	120,725	450,000	172,650
26-27	700,000	30,100			1,425,000	492,625	500,000	693,125	765,000	95,000	470,000	159,150
27-28					1,500,000	435,625	500,000	673,125	790,000	64,400	1,250,000	145,050
28-29					1,575,000	375,625	500,000	655,625	820,000	32,800	1,300,000	107,550
29-30					1,650,000	308,688	500,000	635,625			2,285,000	68,550
30-31					1,750,000	238,563	500,000	617,500				
31-32					1,825,000	164,188	500,000	598,750				
32-33					1,925,000	86,625	500,000	580,000				
33-34							2,000,000	560,000				
34-35							2,000,000	480,000				
35-36							2,000,000	400,000				
36-37							2,000,000	320,000				
37-38							2,000,000	240,000				
38-39							2,000,000	160,000				
39-40							2,000,000	80,000				
40-41												
41-42												
42-43												
43-44												
44-45												
	$ 6,295,000	$ 1,710,686	$ 750,000	$ 41,250	$ 22,625,000	$ 9,620,189	$ 22,800,000	$ 14,539,625	$ 8,665,000	$ 2,469,575	$ 8,970,000	$ 2,770,550

Knoxville Utilities Board Water Division
Supplemental Information - Schedule of Debt Maturities by Fiscal Year
June 30, 2016
(Unaudited)

Schedule 2

Continued from Previous Page

	Z-2013		AA-2014		BB-2015		CC-2015		TOTAL		Grand
FY	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Total
16-17	500,000	1,004,625	150,000	261,750	100,000	791,700	375,000	703,906	4,560,000	5,502,077	10,062,077
17-18	500,000	989,625	150,000	257,250	865,000	786,700	400,000	696,406	4,710,000	5,308,927	10,018,927
18-19	525,000	979,625	150,000	252,750	885,000	743,450	425,000	684,406	4,870,000	5,127,527	9,997,527
19-20	550,000	963,875	175,000	246,750	950,000	699,200	425,000	667,406	5,100,000	4,923,477	10,023,477
20-21	575,000	947,375	175,000	243,250	960,000	680,200	450,000	650,406	5,280,000	4,746,427	10,026,427
21-22	600,000	930,125	175,000	238,000	1,000,000	661,000	475,000	632,406	5,525,000	4,560,496	10,085,496
22-23	625,000	912,125	200,000	231,000	1,050,000	611,000	475,000	613,406	5,685,000	4,350,584	10,035,584
23-24	625,000	893,375	200,000	223,000	1,110,000	558,500	500,000	599,156	5,880,000	4,137,909	10,017,909
24-25	650,000	874,625	200,000	215,000	1,170,000	503,000	525,000	587,906	6,130,000	3,921,121	10,051,121
25-26	675,000	852,688	225,000	209,000	1,210,000	467,900	550,000	574,782	6,360,000	3,713,690	10,073,690
26-27	700,000	828,219	225,000	202,250	1,245,000	428,575	550,000	560,344	6,580,000	3,489,388	10,069,388
27-28	750,000	800,219	225,000	195,500	1,260,000	385,000	575,000	543,844	6,850,000	3,242,763	10,092,763
28-29	775,000	770,219	250,000	188,750	1,275,000	340,900	600,000	526,594	7,095,000	2,998,063	10,093,063
29-30	800,000	738,250	250,000	181,250	1,315,000	296,275	625,000	508,594	7,425,000	2,737,232	10,162,232
30-31	825,000	704,250	275,000	173,438	2,740,000	256,825	650,000	489,060	6,740,000	2,479,636	9,219,636
31-32	850,000	669,188	275,000	164,844	2,800,000	174,625	675,000	467,938	6,925,000	2,239,533	9,164,533
32-33	900,000	632,000	300,000	155,906	2,900,000	90,625	700,000	446,000	7,225,000	1,991,156	9,216,156
33-34	925,000	591,500	300,000	146,156			725,000	418,000	3,950,000	1,715,656	5,665,656
34-35	950,000	549,875	325,000	136,032			750,000	389,000	4,025,000	1,554,907	5,579,907
35-36	1,000,000	507,125	325,000	124,656			775,000	359,000	4,100,000	1,390,781	5,490,781
36-37	1,025,000	460,875	350,000	113,282			800,000	330,906	4,175,000	1,225,063	5,400,063
37-38	1,075,000	413,469	350,000	101,031			825,000	301,906	4,250,000	1,056,406	5,306,406
38-39	1,100,000	363,750	375,000	88,781			875,000	272,000	4,350,000	884,531	5,234,531
39-40	1,150,000	308,750	375,000	75,656			900,000	237,000	4,425,000	701,406	5,126,406
40-41	1,200,000	251,250	400,000	62,531			925,000	201,000	2,525,000	514,781	3,039,781
41-42	1,225,000	191,250	425,000	48,031			975,000	164,000	2,625,000	403,281	3,028,281
42-43	1,275,000	130,000	450,000	32,625			1,000,000	125,000	2,725,000	287,625	3,012,625
43-44	1,325,000	66,250	450,000	16,313			1,050,000	85,000	2,825,000	167,563	2,992,563
44-45							1,075,000	43,000	1,075,000	43,000	1,118,000
	$ 23,675,000	$ 18,324,502	$ 7,725,000	$ 4,584,782	$ 22,835,000	$ 8,475,475	$ 19,650,000	$ 12,878,372	$ 143,990,000	$ 75,415,006	$ 219,405,006

Knoxville Utilities Board Water Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)

Schedule 3

Rate Class	Base Charge	Number of Customers
Residential Inside City rate	For water furnished to premises entirely within the corporate limits of the City of Knoxville:	55,363

Commodity Charge

First	2	100 Cubic Feet Per Month at $0.25 Per 100 Cubic Feet
Over	2	100 Cubic Feet Per Month at $2.65 Per 100 Cubic Feet

Additional Monthly Customer Charge

For	5/8" meter	$	14.00
For	1" meter		28.10
For	1 1/2" meter		40.00
For	2" meter		56.00

Residential Outside City rate	For water furnished to premises upon which any water faucet or other outlet is outside the corporate limits of the City of Knoxville:	13,194

Commodity Charge

First	2	100 Cubic Feet Per Month at $0.30 Per 100 Cubic Feet
Over	2	100 Cubic Feet Per Month at $3.20 Per 100 Cubic Feet

Additional Monthly Customer Charge

For	5/8" meter	$	15.40
For	1" meter		32.40
For	1 1/2" meter		46.40
For	2" meter		65.40

Knoxville Utilities Board Water Division
Supplemental Information - Schedule of Current Rates in Force
June 30, 2016
(Unaudited)
Schedule 3

Rate Class	Base Charge	Number of Customers
Non-Residential Inside City rate/ Industrial Park rate	For water furnished to premises entirely within the corporate limits of the City of Knoxville or within the boundaries of an area recognized as an industrial park by the Tennessee Department of Economic and Community Development:	9,712

Commodity Charge

First	2	100 Cubic Feet Per Month at $1.55 Per 100 Cubic Feet
Next	8	100 Cubic Feet Per Month at $3.45 Per 100 Cubic Feet
Next	90	100 Cubic Feet Per Month at $4.25 Per 100 Cubic Feet
Next	300	100 Cubic Feet Per Month at $3.05 Per 100 Cubic Feet
Next	4,600	100 Cubic Feet Per Month at $2.00 Per 100 Cubic Feet
Next	5,000	100 Cubic Feet Per Month at $1.00 Per 100 Cubic Feet

Additional Monthly Customer Charge

For	5/8" meter	$ 14.00
For	1" meter	28.10
For	1 1/2" meter	40.00
For	2" meter	56.00
For	3" meter	127.00
For	4" meter	210.00
For	6" meter	460.00
For	8" meter	809.00
For	10" meter	1,232.00
For	12" meter	1,823.00

Rate Class	Base Charge	Number of Customers
Non-Residential Outside City rate	For water furnished to premises upon which any water faucet or other outlet is outside the corporate limits of the City of Knoxville, excluding premises within the boundaries of an area recognized as an industrial park by the Tennessee Department of Economic and Community Development:	711

Commodity Charge

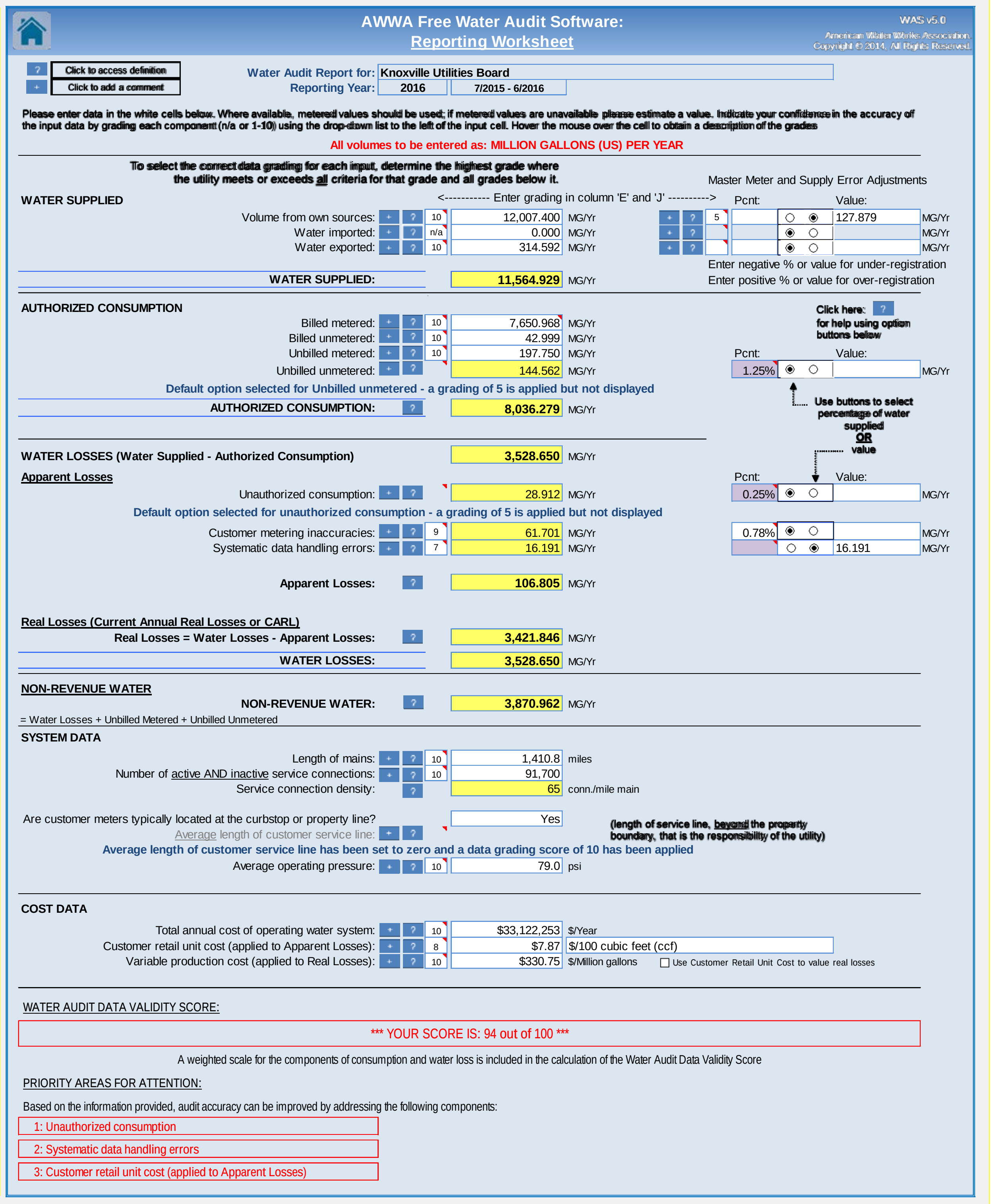
First	2	100 Cubic Feet Per Month at $1.85 Per 100 Cubic Feet
Next	8	100 Cubic Feet Per Month at $4.00 Per 100 Cubic Feet
Next	90	100 Cubic Feet Per Month at $5.10 Per 100 Cubic Feet
Next	300	100 Cubic Feet Per Month at $3.60 Per 100 Cubic Feet
Next	4,600	100 Cubic Feet Per Month at $2.40 Per 100 Cubic Feet
Next	5,000	100 Cubic Feet Per Month at $1.20 Per 100 Cubic Feet

Additional Monthly Customer Charge

For	5/8" meter	$ 15.40
For	1" meter	32.40
For	1 1/2" meter	46.40
For	2" meter	65.40
For	3" meter	151.00
For	4" meter	253.00
For	6" meter	552.00
For	8" meter	970.00
For	10" meter	1,477.00
For	12" meter	2,189.00

The following unaudited Schedule of Unaccounted for Water is attached as required by the Tennessee Code Annotated. For reports submitted January 1, 2013 and later, the American Water Works Association (AWWA) water loss reporting model must be used. For fiscal year 2015, water utilities are required to have a Validity Score greater than 70 and maintain non-revenue water as a percent by cost of operating system of less than 25%. For fiscal year 2016, water utilities are required to have a Validity Score greater than 70 and maintain non-revenue water as a percent by cost of operating system of less than 25%. For fiscal year 2015, KUB reported a Validity Score of 94 and non-revenue water as a percent by cost of operating system of 10.2%. For fiscal year 2016, KUB reported a Validity Score of 94 and non-revenue water as a percent by cost of operating system of 7.2%. See Supplemental Information Schedule 4 for the AWWA Reporting Worksheet.

Knoxville Utilities Board Water Division
Supplemental Information - Schedule of Unaccounted for Water
June 30, 2016
(Unaudited) Schedule 4



AWWA Free Water Audit Software:
Reporting Worksheet

WAS v5.0
American Water Works Association.
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? Click to access definition
\+ Click to add a comment

Water Audit Report for: Knoxville Utilities Board
Reporting Year: 2016 7/2015 - 6/2016

Please enter data in the white cells below. Where available, metered values should be used; if metered values are unavailable please estimate a value. Indicate your confidence in the accuracy of the input data by grading each component (n/a or 1-10) using the drop-down list to the left of the input cell. Hover the mouse over the cell to obtain a description of the grades

All volumes to be entered as: MILLION GALLONS (US) PER YEAR

To select the correct data grading for each input, determine the highest grade where the utility meets or exceeds all criteria for that grade and all grades below it.

Master Meter and Supply Error Adjustments

WATER SUPPLIED

<------------ Enter grading in column 'E' and 'J' ---------->

					Pcnt:		Value:	
Volume from own sources:	10	12,007.400	MG/Yr	5		○ ●	127.879	MG/Yr
Water imported:	n/a	0.000	MG/Yr			● ○		MG/Yr
Water exported:	10	314.592	MG/Yr			● ○		MG/Yr

Enter negative % or value for under-registration
Enter positive % or value for over-registration

WATER SUPPLIED: 11,564.929 MG/Yr

AUTHORIZED CONSUMPTION

Click here: ? for help using option buttons below

				Pcnt:		Value:	
Billed metered:	10	7,650.968	MG/Yr				
Billed unmetered:	10	42.999	MG/Yr				
Unbilled metered:	10	197.750	MG/Yr				
Unbilled unmetered:		144.562	MG/Yr	1.25%	● ○		MG/Yr

Default option selected for Unbilled unmetered - a grading of 5 is applied but not displayed

AUTHORIZED CONSUMPTION: 8,036.279 MG/Yr

Use buttons to select percentage of water supplied **OR** value

WATER LOSSES (Water Supplied - Authorized Consumption) 3,528.650 MG/Yr

Apparent Losses

				Pcnt:		Value:	
Unauthorized consumption:		28.912	MG/Yr	0.25%	● ○		MG/Yr

Default option selected for unauthorized consumption - a grading of 5 is applied but not displayed

Customer metering inaccuracies:	9	61.701	MG/Yr	0.78%	● ○		MG/Yr
Systematic data handling errors:	7	16.191	MG/Yr		○ ●	16.191	MG/Yr

Apparent Losses: 106.805 MG/Yr

Real Losses (Current Annual Real Losses or CARL)
Real Losses = Water Losses - Apparent Losses: 3,421.846 MG/Yr

WATER LOSSES: 3,528.650 MG/Yr

NON-REVENUE WATER
NON-REVENUE WATER: 3,870.962 MG/Yr
= Water Losses + Unbilled Metered + Unbilled Unmetered

SYSTEM DATA

Length of mains:	10	1,410.8	miles
Number of active AND inactive service connections:	10	91,700	
Service connection density:		65	conn./mile main

Are customer meters typically located at the curbstop or property line? Yes
Average length of customer service line: (length of service line, beyond the property boundary, that is the responsibility of the utility)
Average length of customer service line has been set to zero and a data grading score of 10 has been applied
Average operating pressure: 10 79.0 psi

COST DATA

Total annual cost of operating water system:	10	$33,122,253	$/Year
Customer retail unit cost (applied to Apparent Losses):	8	$7.87	$/100 cubic feet (ccf)
Variable production cost (applied to Real Losses):	10	$330.75	$/Million gallons

☐ Use Customer Retail Unit Cost to value real losses

WATER AUDIT DATA VALIDITY SCORE:

*** YOUR SCORE IS: 94 out of 100 ***

A weighted scale for the components of consumption and water loss is included in the calculation of the Water Audit Data Validity Score

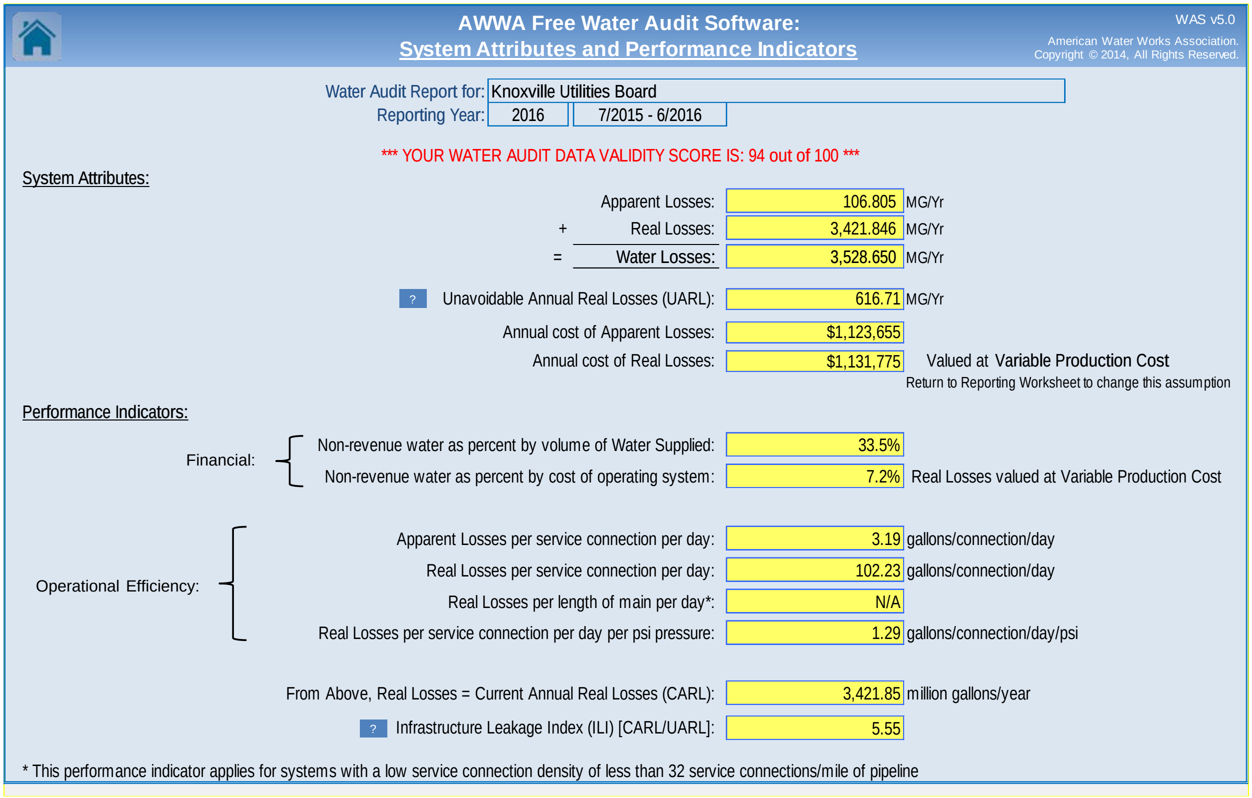
PRIORITY AREAS FOR ATTENTION:

Based on the information provided, audit accuracy can be improved by addressing the following components:

1: Unauthorized consumption
2: Systematic data handling errors
3: Customer retail unit cost (applied to Apparent Losses)

Knoxville Utilities Board Water Division
Supplemental Information - Schedule of Unaccounted for Water
June 30, 2016
(Unaudited)

Schedule 4



AWWA Free Water Audit Software:
System Attributes and Performance Indicators

WAS v5.0
American Water Works Association.
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Water Audit Report for: Knoxville Utilities Board
Reporting Year: 2016 | 7/2015 - 6/2016

*** YOUR WATER AUDIT DATA VALIDITY SCORE IS: 94 out of 100 ***

System Attributes:

Apparent Losses:	106.805	MG/Yr
+ Real Losses:	3,421.846	MG/Yr
= Water Losses:	3,528.650	MG/Yr
? Unavoidable Annual Real Losses (UARL):	616.71	MG/Yr
Annual cost of Apparent Losses:	$1,123,655	
Annual cost of Real Losses:	$1,131,775	Valued at Variable Production Cost

Return to Reporting Worksheet to change this assumption

Performance Indicators:

Financial:	Non-revenue water as percent by volume of Water Supplied:	33.5%	
	Non-revenue water as percent by cost of operating system:	7.2%	Real Losses valued at Variable Production Cost
Operational Efficiency:	Apparent Losses per service connection per day:	3.19	gallons/connection/day
	Real Losses per service connection per day:	102.23	gallons/connection/day
	Real Losses per length of main per day*:	N/A	
	Real Losses per service connection per day per psi pressure:	1.29	gallons/connection/day/psi
	From Above, Real Losses = Current Annual Real Losses (CARL):	3,421.85	million gallons/year
	? Infrastructure Leakage Index (ILI) [CARL/UARL]:	5.55	

* This performance indicator applies for systems with a low service connection density of less than 32 service connections/mile of pipeline

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

Board of Commissioners
Water Division of the Knoxville Utilities Board
Knoxville, Tennessee

Report on the Financial Statements

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Water Division (the Division) of the Knoxville Utilities Board, a component unit of the City of Knoxville, Tennessee, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements, and have issued our report thereon dated October 27, 2016.

Internal Control over Financial Reporting

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

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

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

Board of Commissioners
Water Division of the Knoxville Utilities Board
Knoxville, Tennessee

Compliance and Other Matters

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

Purpose of Report

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

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

Knoxville Utilities Board

Wastewater Division

Financial Statements and Supplemental Information
June 30, 2016 and 2015

KUB Board of Commissioners

Nikitia Thompson - Chair

Sara Hedstrom Pinnell - Vice Chair

Dr. Jerry W. Askew

Kathy Hamilton

Celeste Herbert

Eston Williams

John Worden

Management

Mintha Roach
President and
Chief Executive Officer

Bill Elmore
Executive Vice President and
Chief Operating Officer

Mark Walker
Senior Vice President and
Chief Financial Officer

Susan Edwards
Senior Vice President and
Chief Administrative Officer

Eddie Black
Senior Vice President

Mike Bolin
Vice President

Julie Childers
Vice President

Derwin Hagood
Vice President

Dawn Mosteit
Vice President

Paul Randolph
Vice President

Dennis Upton
Vice President

Knoxville Utilities Board Wastewater Division
Index
June 30, 2016 and 2015

9717 Cogdill Road
Suite 201
Knoxville, TN 37932

C&J COULTER & JUSTUS, P.C.

phone: (865) 637-4161
fax: (865) 524-2952
web: cj-pc.com

Report of Independent Auditors

Board of Commissioners
Wastewater Division of the Knoxville Utilities Board
Knoxville, Tennessee

We have audited the accompanying financial statements of the Wastewater Division (the Division) of the Knoxville Utilities Board, a component unit of the City of Knoxville, Tennessee, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements as listed in the index.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Division'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 Division'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 the Wastewater Division of the Knoxville Utilities Board as of June 30, 2016 and 2015, and the changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Commissioners
Wastewater Division of the Knoxville Utilities Board
Knoxville, Tennessee

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 24 and the required supplementary information on pages 52 through 54 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Division's basic financial statements. The supplemental information is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplemental information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 27, 2016, on our consideration of the Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016

Knoxville Utilities Board (KUB), comprised of the Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions. The Wastewater Division (Division) provides services to certain customers in Knox County and in two surrounding counties in East Tennessee. The Division's accounts are maintained in conformity with the Uniform System of Accounts of the National Association of Regulatory Utility Commissioners (NARUC) and the Governmental Accounting Standards Board (GASB), as applicable. The financial statements present only the Wastewater Division and do not purport to, and do not, present fairly the consolidated financial position of Knoxville Utilities Board at June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Division’s discussion and analysis is designed to (a) assist the reader in focusing on significant financial issues, (b) provide an overview of the Division’s financial activity, (c) identify major changes in the Division’s financial position, and (d) identify any financial concerns.

The Division’s Management Discussion and Analysis (MD&A) focuses on the fiscal year ending June 30, 2016 activities, resulting changes and current known facts, and should be read in conjunction with the Division’s financial statements.

Wastewater Division Highlights

System Highlights

The wastewater service area covers 243 square miles and includes 70,265 wastewater customers. KUB maintains 1,317 miles of services mains, 75 pump stations, and 4 treatment plants to treat 13.9 billion gallons of wastewater on an annual basis. The average daily flow is 38.1 million gallons.

KUB has added approximately 737 wastewater system customers over the past three years representing annual growth of less than one percent.

The typical residential wastewater customer’s average monthly wastewater bill was $53.50 as of June 30, 2016, representing an increase of $3 compared to June 30, 2015. The increase in the monthly bill reflects a rate increase effective October 2015.

KUB’s treatment plants continue to meet high standards of operation. KUB’s Kuwahee, Eastbridge, Loves Creek and Fourth Creek wastewater treatment plants were awarded Operational Excellence awards from the Tennessee Kentucky Water Environment Association for having one or less permit violations within the 2015 calendar year. The treatment plants additionally won awards at various levels based on performance from the National Association of Clean Water Agencies for peak performance. The Eastbridge wastewater treatment plant was awarded a Platinum award for continued outstanding compliance performance over multiple years. Kuwahee and Loves Creek wastewater treatment plants won Gold Awards for having no permit violations in 2015 and the Fourth Creek wastewater treatment plant was awarded Silver for having only one permit violation in 2015.

KUB continued to maintain certification with the National Biosolids Partnership following a rigorous review process and independent audit that was conducted in December 2015. (Biosolids are nutrient-rich organic matter produced by wastewater treatment that can be recycled as fertilizer).

Century II Infrastructure Program

Century II is KUB's proactive long-range program to improve and maintain the electric, natural gas, water and wastewater systems for its customers. It includes the maintenance and asset replacement strategies for each system and establishes sustainable replacement cycles. Century II moves KUB into its second century of service by improving each system through sound planning, resource allocation, and continued, but accelerated, investment.

In 2013, the Board extended the funding approach for Century II to include the wastewater system, although the Wastewater Division had maintained a ten-year funding plan since the inception of the Federal Consent Decree (see below). The Board formally endorsed and adopted by resolution, a ten year funding plan for the Wastewater Division, which includes a combination of rate increases and debt issues to fully fund the wastewater system's Century II program.

In April 2014, KUB management provided the Board an updated assessment of the overall condition of each utility system, including a recommendation for annual rate increases for each division for the next three fiscal years.

In June 2014, the Board approved the proposed three annual rate increases for the Wastewater Division. The first and second rate increases went into effect in October 2014 and October 2015. The third rate increase will go into effect October 2016. The wastewater rate increases will each produce an additional $4.7 million of annual sales revenue.

In fiscal year 2016, KUB rehabilitated or replaced 28 miles of wastewater system main, exceeding the target level of 25 miles, while staying within the Division's total capital budget.

Consent Decree

In February 2005, a Consent Decree was entered into federal court regarding the operation of KUB's wastewater system. Under the terms of the Consent Decree, the remediation of identified sanitary sewer overflows (SSOs) on KUB's wastewater system had to be completed by June 30, 2016. KUB completed all the requirements of the Consent Decree for the collection system two years in advance of the deadline.

The Consent Decree also required KUB to perform an evaluation of the wet weather performance and capacity of its wastewater treatment plants. In July 2007, KUB submitted a Composite Correction Plan (CCP) for its wastewater treatment plants to EPA for review. The development and filing of the CCP was a requirement of the federal order of February 2005. The CCP includes recommended improvements to KUB's Kuwahee and Fourth Creek treatment plants to address wet weather capacity issues noted in prior assessments. The EPA approved the CCP in January 2009 including a recommended schedule of plant improvements that extends beyond the expiration date of the original Consent Decree. An amendment to the Consent Decree incorporating and establishing this schedule was agreed to by all parties and was entered on June 23, 2009. The purpose of the Amendment is to allow KUB to complete a portion of work outlined in the CCP after the Consent Decree deadline of June 30, 2016. The CCP provides for a biologically enhanced high-rate clarification (the BEHRC) secondary treatment system to be installed at the Fourth Creek treatment plant by June 30, 2018 and at the Kuwahee treatment plant by June 30, 2021. The total cost of such improvements is estimated to be approximately $120 million.

KUB's funding plan for the Consent Decree includes long-term bonds and a series of rate increases phased in over the term of the order. Bond proceeds fund all types of wastewater capital projects, the majority of which are related to the Consent Decree. As of June 30, 2016, the Wastewater Division had issued $485 million in bonds to fund system capital improvements since the inception of the Consent Decree. The Board approved two 50 percent rate increases, which went into effect in April 2005 and

January 2007. The Board also approved an 8 percent rate increase, which was effective in September 2008, two 12 percent rate increases, which were effective in April 2011 and October 2012, and three 6 percent rate increases effective October 2014, October 2015 and October 2016. KUB anticipates additional bond issues and rate increases over the next decade to help fund wastewater capital improvements.

KUB successfully completed the first cycle of Maintenance Operation Management (MOM) requirements one year before the deadline by inspecting 99.5% of manholes and gravity mains, smoke testing 99.9% of gravity mains, performing required inspections of pump stations and the related force mains, and completing all Corrective Action Plan/Engineering Report (CAP/ER) projects. KUB initiated the second MOM cycle that continues to focus on the prevention of SSOs. As part of the Century II initiative, formally known as the PACE10 program, KUB has installed storage tanks providing 34 million gallons of wastewater storage to control wet weather overflows and rehabilitated or replaced approximately 334.9 miles of collection system pipe. KUB also continues to maintain a proactive operations and maintenance plan for the wastewater collection system including inspection, grease control, and private lateral enforcement. The result of the Pace10/Century II initiative has been an 82 percent reduction in SSOs.

As of June 30, 2016, the Wastewater Division had completed its twelfth full year under the Consent Decree, spending $529.5 million on capital investments to meet Consent Decree requirements. During fiscal year 2016, the Wastewater Division incurred $37.3 million in total expenditures related to Consent Decree requirements, including $3.3 million for operating costs and $34 million in capital improvements which included the rehabilitation or replacement of 28 miles of wastewater main. During the fiscal year, $26.5 million was spent on sewer mini-basin rehabilitation and replacement. Trunk line rehabilitation and replacement accounted for $2 million of capital expenditures, while pump station improvements accounted for $4.6 million.

Financial Highlights

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division's net position during the year increased $9.5 million compared to a $7.8 million increase last fiscal year. A restatement to the fiscal year 2014's net position based on a change in method of accounting for pension expense reduced the total net position by $0.2 million during fiscal year 2015. This change resulted in a net increase of $7.6 million or 3 percent in the Division's net position in fiscal year 2015.

Operating revenue increased $4.4 million or 5.6 percent, the result of additional revenue generated during the fiscal year from the rate increase effective October 2015, along with a 1.1 percent increase in wastewater sales volumes.

Operating expenses increased $2.1 million or 4 percent. Operating and maintenance (O&M) expenditures increased $0.6 million or 2 percent. Depreciation expense rose $1.2 million or 7.1 percent. Taxes and tax equivalents increased $0.2 million or 5.5 percent.

Interest income was $0.2 million higher than the prior fiscal year. Interest expense increased $0.8 million or 4.2 percent, reflecting additional interest expense on revenue bonds sold in fiscal year 2015. Other income (net) was $0.3 million lower.

Capital contributions increased $0.3 million, the result of an increase in donated assets from developers compared to the previous fiscal year.

Total plant assets (net) increased $22.9 million or 3.4 percent since the end of last fiscal year.

Long-term debt represented 64.5 percent of the Division's capital structure as of June 30, 2016, as compared to 65.8 percent last year. The decrease is the result of scheduled repayment of debt during the fiscal year. Capital structure equals long-term debt (which includes the current and long-term portion of revenue bonds and notes) plus net position.

The Division's bond covenants require a debt service coverage ratio of at least 1.2 times the maximum principal and interest payments over the life of the Division's outstanding bonds. Current year debt coverage for the fiscal year was 1.85. Maximum debt service coverage was 1.68.

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division's net position during the year increased $7.8 million compared to a $5.7 million increase last fiscal year. A restatement to the prior fiscal year's net position based on a change in method of accounting for pension expense reduced the total net position by $0.2 million during fiscal year 2015. This change resulted in a net increase of $7.6 million or 3 percent in the Division's net position.

Operating revenue increased $4.2 million or 5.5 percent, the result of additional revenue generated during the fiscal year from the rate increase effective October 2014, along with a 0.9 percent increase in wastewater sales volumes.

Operating expenses increased $2.5 million or 5 percent. Operating and maintenance (O&M) expenditures increased $1.2 million or 4.2 percent. Depreciation expense rose $1 million or 6.5 percent. Taxes and tax equivalents increased $0.2 million or 5.1 percent.

Interest income was consistent with the prior fiscal year. Interest expense increased $0.1 million or less than one percent reflecting additional interest expense on $60 million in revenue bonds sold in fiscal year 2015. Other income (net) was $0.4 million higher.

Capital contributions increased $0.1 million, the result of an increase in donated assets from developers compared to the previous fiscal year.

Total plant assets (net) increased $21.9 million or 3.4 percent since the end of last fiscal year.

KUB sold two series of wastewater system revenue bonds during fiscal year 2015 for the purpose of funding wastewater system capital improvements totaling $60 million. The $30 million bond issue in April 2015 was accelerated to take advantage of the low interest rate environment which impacted the Division's debt rate and debt service coverage levels for fiscal year 2015. Long-term debt represented 65.8 percent of the Division's capital structure as of June 30, 2015, as compared to 63.9 percent last year. The increase is the net result of the issuance of revenue bonds in August 2014 and April 2015 offset the scheduled repayment of debt during the fiscal year. Capital structure equals long-term debt (which includes the current and long-term portion of revenue bonds and notes) plus net position.

The Division's bond covenants require a debt service coverage ratio of at least 1.2 times the maximum principal and interest payments over the life of the Division's outstanding bonds. Current year debt coverage for the fiscal year was 1.65. Maximum debt service coverage was 1.55.

Knoxville Utilities Board Wastewater Division - Financial Statements

The Division’s financial performance is reported under three basic financial statements: the Statement of Net Position; the Statement of Revenues, Expenses and Changes in Net Position; and the Statement of Cash Flows.

Statement of Net Position

The Division reports its assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position in the Statement of Net Position. Assets are classified as current, restricted, wastewater plant in service, or other assets.

Liabilities are classified as current, other, or long-term debt. Net position is classified as net investment in capital assets; restricted; or unrestricted. Net position tells the user what the Division has done with its accumulated earnings, not just the balance.

Net investment in capital assets reflects the book value of all capital assets less the outstanding balances of debt used to acquire, construct, or improve those assets.

Restricted net position are assets that have been limited to specific uses by the Division’s bond covenants or through resolutions passed by the KUB Board.

Unrestricted net position is a residual classification; the amount remaining after reporting net position is either invested in capital or restricted is reported there.

Statement of Revenues, Expenses and Changes in Net Position

The Division reports its revenues and expenses (both operating and non-operating) on the Statement of Revenues, Expenses and Changes in Net Position. In addition, any capital contributions or assets donated by developers are reported on this statement.

Total revenue less total expense equals the change in net position for the reporting period. Net position at the beginning of the period is increased or decreased, as applicable, by the change in net position for the reporting period.

The change in net position for the reporting period is added to the net position segment of the Statement of Net Position.

Statement of Cash Flows

The Division reports cash flows from operating activities, capital and related financing activities, and investing activities on the Statement of Cash Flows. This statement tells the user the Division’s sources and uses of cash during the reporting period.

The statement indicates the Division’s beginning cash balance and ending cash balance and how it was either increased or decreased during the reporting period.

The statement also reconciles cash flow to operating income as it appears on the Statement of Revenues, Expenses and Changes in Net Position.

Condensed Financial Statements

Statement of Net Position

The following table reflects the condensed Statement of Net Position for the Wastewater Division compared to the prior year and the year preceding the prior year.

Statements of Net Position
As of June 30

(in thousands of dollars)	2016	2015	2014
Current, restricted and other assets	$ 80,075	$ 104,099	$ 66,802
Capital assets, net	687,056	664,178	642,302
Deferred outflows of resources	19,413	18,593	10,064
Total assets and deferred outflows of resources	786,544	786,870	719,168
Current and other liabilities	22,630	19,981	19,979
Long-term debt outstanding	492,466	503,955	445,190
Deferred inflows of resources	333	1,339	-
Total liabilities and deferred inflows of resources	515,429	525,275	465,169
Net position			
Net investment in capital assets	205,784	172,144	201,947
Restricted	2,737	2,624	2,263
Unrestricted	62,594	86,827	49,789
Total net position	$ 271,115	$ 261,595	$ 253,999

Normal Impacts on Statement of Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Net Position presentation.

- Change in net position (from Statement of Revenues, Expenses and Changes in Net Position): impacts (increase/decrease) current and other assets and/or capital assets and unrestricted net position.
- Issuing debt for capital: increases deferred outflows of resources and long-term debt.
- Spending debt proceeds on new capital: reduces current assets and increases capital assets.
- Spending of non-debt related current assets on new capital: (a) reduces current assets and increases capital assets and (b) reduces unrestricted net position and increases net investment in capital assets.
- Principal payment on debt: (a) reduces current and other assets and reduces long-term debt and (b) reduces unrestricted net position and increases net investment in capital assets.
- Reduction of capital assets through depreciation: reduces capital assets and net investment in capital assets.

Impacts and Analysis

Current, Restricted and Other Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Current, restricted and other assets decreased $24 million or 23.1 percent, reflecting the utilization of $15.6 million in bond proceeds and a $9.1 million decrease in general fund cash for the primary purpose of funding wastewater capital improvements. Operating contingency reserves increased $1.1 million and accounts receivable increased $0.3 million.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current, restricted and other assets increased $37.3 million or 55.8 percent, reflecting a $17.4 million increase in the general fund balance and $15.6 million in unused bond proceeds. Operating contingency reserves increased $2.4 million and accounts receivable increased $0.6 million.

Capital Assets

Fiscal Year 2016 Compared to Fiscal Year 2015

Capital assets increased $22.9 million or 3.4 percent, the result of capital expenditures, net of depreciation. Major capital expenditures during the year included $32.6 million for major system improvements related to Century II (previously reported as PACE 10 expenditures), and $1.8 million for upgrades to various information systems, and $1.3 million for the replacement and relocation of wastewater system assets to accommodate Tennessee Department of Transportation (TDOT) highway improvement projects.

Fiscal Year 2015 Compared to Fiscal Year 2014

Capital assets increased $21.9 million or 3.4 percent, the result of capital expenditures, net of depreciation. Major capital expenditures during the year included $25.3 million for major system improvements related to Century II (previously reported as PACE 10 expenditures), $7 million for general system improvements and $1.8 million for information system upgrades.

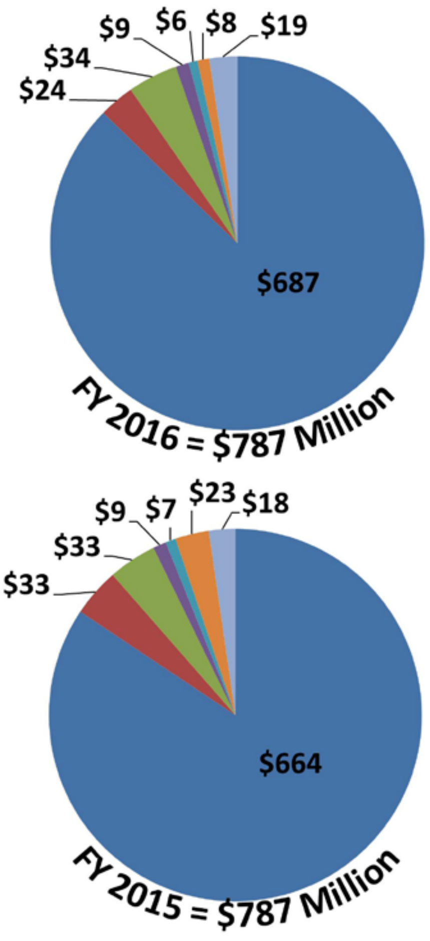
Deferred Outflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred outflows increased $0.8 million compared to the prior year, reflecting a $1.6 million increase in pension outflow and a $0.8 million decrease in unamortized bond refunding costs.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred outflows increased $8.5 million compared to the prior year, reflecting $7.9 million in unamortized bond refunding costs from fiscal year 2015 bond refinancing.



Wastewater Division Total Assets and Deferred Outflows of Resources (in Millions)

	FY16	FY15
🟦 Plant	87%	85%
🟥 General Fund	3%	4%
🟩 Contingency Fund	4%	4%
🟪 Accounts Receivable	1%	1%
🟦 Other Assets	1%	1%
🟧 Restricted Assets	1%	3%
🟦 Deferred Outflows of Resources	3%	2%

Current and Other Liabilities

Fiscal Year 2016 Compared to Fiscal Year 2015

Current and other liabilities were $2.6 million more than the prior fiscal year. This increase was primarily due to a $1.4 million increase in accounts payable and an actuarially determined net pension obligation of $1.1 million recognized in fiscal year 2016.

Fiscal Year 2015 Compared to Fiscal Year 2014

Current and other liabilities were consistent with the prior fiscal year.

Long-Term Debt

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division's outstanding long-term debt decreased $11.5 million or 2.3 percent primarily due to $10.9 million of long-term bond debt that shifted to current liabilities as payable within the next year.

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division's outstanding long-term debt increased $58.8 million or 13.2 percent. The Division issued $30 million in revenue bonds both in August 2014 and in April 2015. The increase was partially offset by the scheduled repayment of bond debt.

Deferred Inflows of Resources

Fiscal Year 2016 Compared to Fiscal Year 2015

Deferred inflows of resources were $1 million lower than the prior fiscal year due to differences in pension inflows.

Fiscal Year 2015 Compared to Fiscal Year 2014

Deferred inflows of resources were $1.3 million higher than the prior fiscal year due to the addition of pension inflow.

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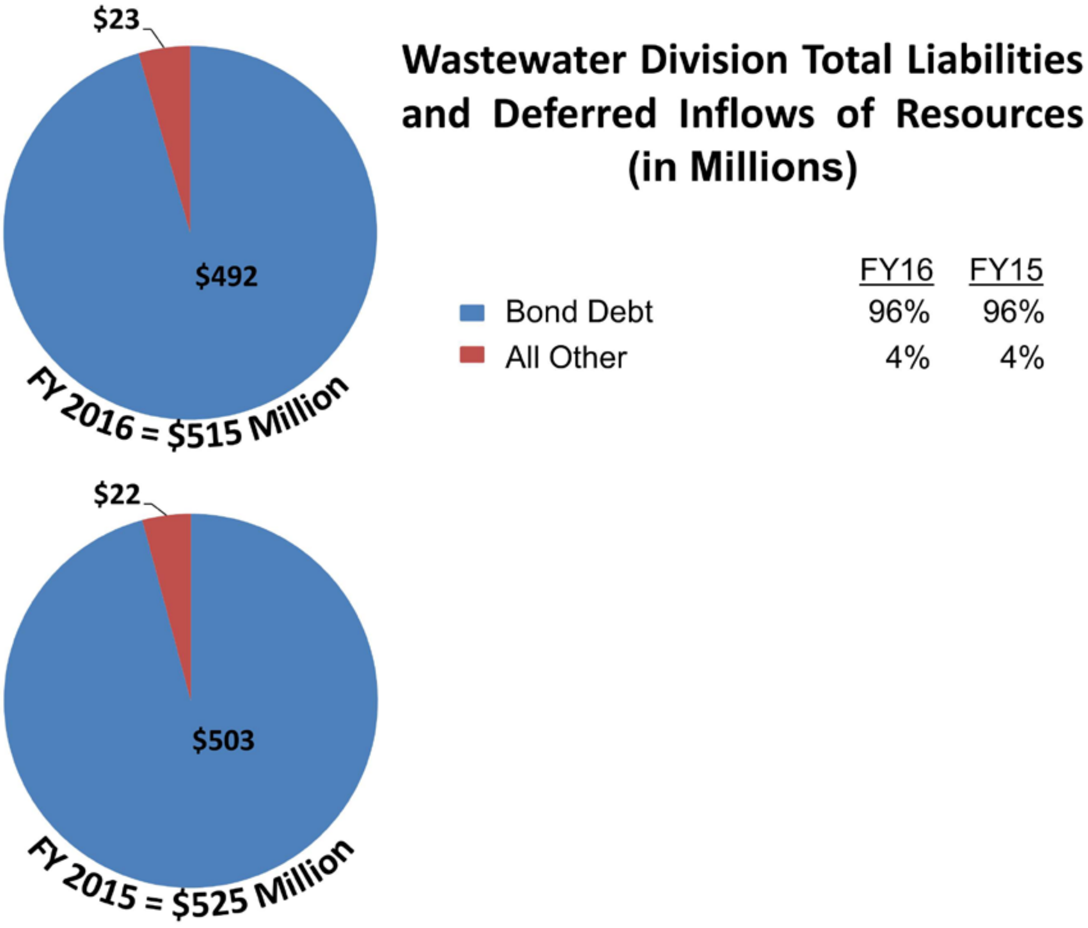

Wastewater Division Total Liabilities and Deferred Inflows of Resources (in Millions)

Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

Net investment in capital assets increased $33.6 million or 19.5 percent. The increase was the result of $22.9 million in net plant additions and a decrease in current and long term debt of $11 million, reflecting the scheduled repayment of bonds. Unrestricted assets decreased $24.2 million primarily due to the $24 million decrease in current and other assets compared to the prior year. Restricted net position was $0.1 million higher than the previous fiscal year, based on increases in debt service.

Fiscal Year 2015 Compared to Fiscal Year 2014

Net investment in capital assets decreased $29.8 million or 14.8 percent. The increase was the result of $21.9 million in net plant additions and an increase in current and long term debt of $53.2 million. Unrestricted assets increased $37 million primarily due to the $37.3 million increase in current and other assets compared to the prior year. Restricted net position was $0.4 million higher than the previous fiscal year, based on increases in debt service.

Statement of Revenues, Expenses and Changes in Net Position

The following table reflects the condensed Statement of Revenues, Expenses and Changes in Net Position for the Wastewater Division compared to the prior year and the year preceding the prior year.

Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended June 30

(in thousands of dollars)	**2016**	**2015**	**2014**
Operating revenues	$ 83,646	$ 79,206	$ 75,042
Operating expenses			
Treatment	12,516	11,597	10,769
Collection	7,462	8,609	7,795
Customer service	2,962	2,837	2,605
Administrative and general	8,572	7,846	8,484
Depreciation	18,343	17,131	16,086
Taxes and tax equivalents	4,537	4,301	4,092
Total operating expenses	54,392	52,321	49,831
Operating income	29,254	26,885	25,211
Interest income	462	301	292
Interest expense	(20,169)	(19,355)	(19,264)
Other income/(expense)	(717)	(433)	(837)
Change in net position before capital contributions	8,830	7,398	5,402
Capital contributions	690	358	272
Change in net position	$ 9,520	$ 7,756	$ 5,674

Normal Impacts on Statement of Revenues, Expenses and Changes in Net Position

The following is a description of activities which will normally impact the comparability of the Statement of Revenues, Expenses and Changes in Net Position presentation.

- Operating revenue is primarily determined by the amount of water usage billed during the fiscal year. KUB has certain commercial and industrial customers whose wastewater usage is metered separately from their water usage. Any change (increase/decrease) in wastewater rates would also cause a change in operating revenue.

- Operating expenses (treatment, collection system expense, customer service, administrative and general) are normally impacted by changes in areas including, but not limited to, labor cost (staffing, wage rates), active employee and retiree health insurance costs, chemicals, and wastewater system maintenance.

- Depreciation expense is impacted by plant additions and retirements during the fiscal year.

- Taxes and tax equivalents are impacted by plant additions/retirements and changes in property tax rates.

- Interest income is impacted by the level of interest rates and investments.

- Interest expense is impacted by the level of outstanding debt and interest rates on the outstanding debt.

- Other income/(expense) is impacted by miscellaneous non-operating revenues and expenses.

- Capital contributions are impacted by a donation of facilities/infrastructure to KUB by developers and governmental agencies. The contributions are recognized as revenue and recorded as plant in service based on the fair market value of the asset(s).

Impacts and Analysis

Change in Net Position

Fiscal Year 2016 Compared to Fiscal Year 2015

The Division’s net position during the year increased $9.5 million compared to a $7.8 million increase last fiscal year. A restatement to fiscal year 2014’s net position based on a change in method of accounting for pension expense reduced the total net position by $0.2 million during fiscal year 2015.

Fiscal Year 2015 Compared to Fiscal Year 2014

The Division’s net position during the year increased $7.8 million compared to a $5.7 million increase last fiscal year. A restatement to the prior fiscal year’s net position based on a change in method of accounting for pension expense reduced the total net position by $0.2 million during fiscal year 2015. This change resulted in a net increase of $7.6 million or 3 percent in the Division’s net position.

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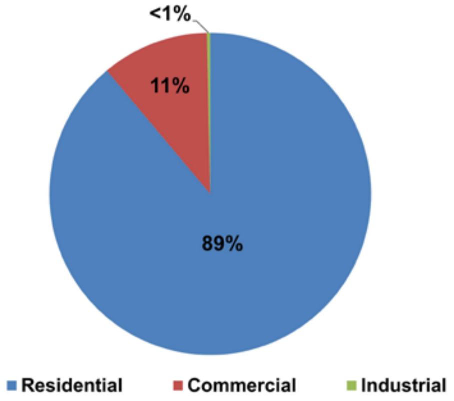
Margin from Sales

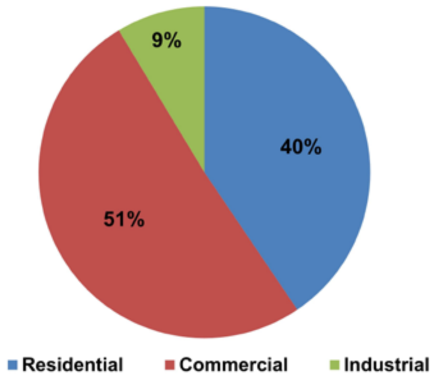
Fiscal Year 2016 Compared to Fiscal Year 2015

Operating revenue increased $4.4 million or 5.6 percent for the fiscal year ending June 30, 2016, the result of additional revenue generated during the fiscal year from the October 2015 rate increase as well as a 1.1 percent increase in wastewater sales volumes. Rebates on bond interest payments from the federal government for federally taxable Build America Bonds (BABs) are reported as revenue in accordance with GASB. KUB recognized $1.8 million in revenue for BABs rebates in fiscal year 2016.

FY 2016 Total Wastewater Customers = 70,265



FY 2016 Wastewater Sales = 6.5 Billion Gallons



Residential customers accounted for 89 percent of wastewater customers and 40 percent of total billed sales volumes for the year. Commercial customers accounted for the largest portion of total sales volumes for the year with 51 percent.

KUB's ten largest wastewater customers accounted for 11.1 percent of KUB's billed wastewater volumes. Those ten customers represent five industrial and five commercial customers, including four governmental customers.

KUB has added 737 wastewater customers over the past three years, representing annual growth of less than one percent.

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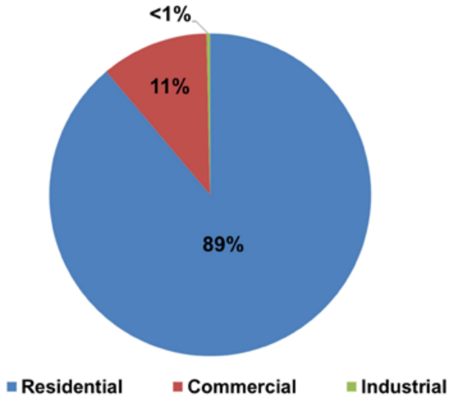
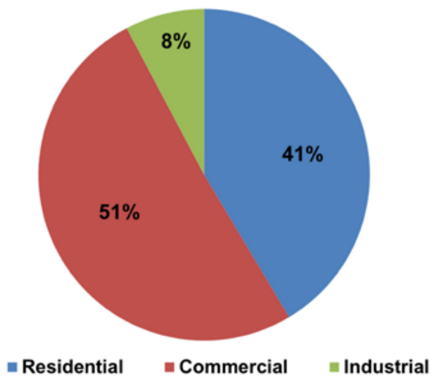
Fiscal Year 2015 Compared to Fiscal Year 2014

Operating revenue increased $4.2 million or 5.5 percent for the fiscal year ending June 30, 2015, the result of additional revenue generated during the fiscal year from the rate increase effective October 2014 and a 0.9 percent increase in wastewater sales volumes. Rebates on bond interest payments from the federal government for federally taxable Build America Bonds (BABs) are reported as revenue in accordance with GASB. KUB recognized $2.7 million in revenue for BABs rebates in fiscal year 2015.

FY 2015 Total Wastewater Customers = 69,847



FY 2015 Wastewater Sales = 6.5 Billion Gallons



Residential customers accounted for 89 percent of wastewater customers and 41 percent of total billed sales for the year. Commercial customers accounted for the largest portion of total sales for the year.

KUB's ten largest wastewater customers accounted for 9.1 percent of KUB's billed wastewater volumes. Those ten customers represent five industrial and five commercial customers, including four governmental customers.

The Division has added 664 customers over the past three years, representing annual growth of less than one percent. Billed wastewater volumes have slowed in recent years, reflecting declining water usage due to more efficient appliances and conservation efforts.

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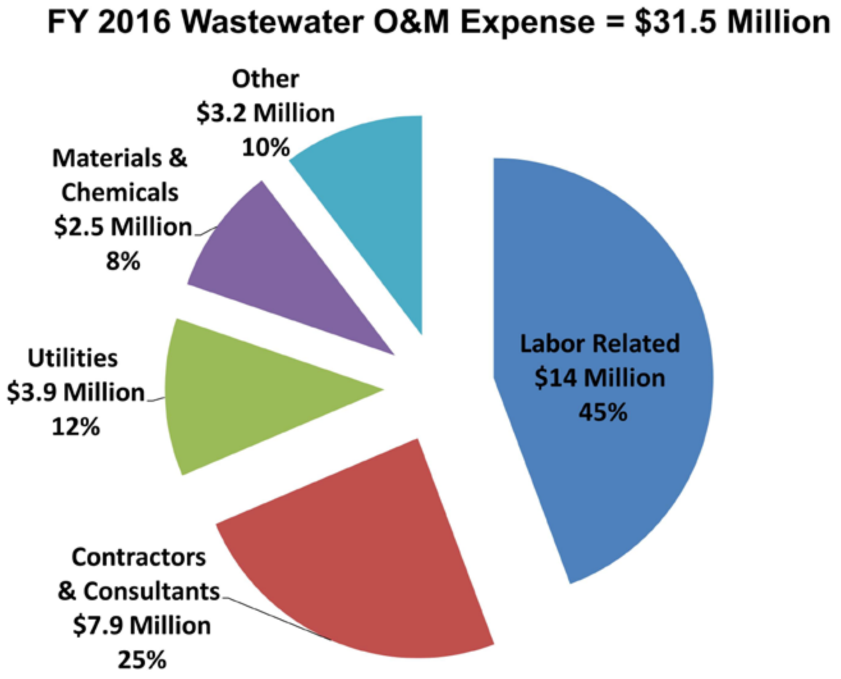
Operating Expenses

Fiscal Year 2016 Compared to Fiscal Year 2015

Operating expenses increased $2.1 million or 4 percent compared to fiscal year 2015. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as treatment, collection, customer service and administrative and general.

- Treatment expenses were up $0.9 million, primarily due to higher outside contractor expenses.
- Collection system expenses decreased $1.1 million, reflecting lower outside contractor expenses for Century II initiatives.
- Customer service expenses increased $0.1 million.
- Administrative and general expenses increased $0.7 million, due primarily to an increase in pension expense.



FY 2016 Wastewater O&M Expense = $31.5 Million

- Depreciation expense increased $1.2 million or 7.1 percent, the result of a full year of depreciation on $16.2 million of wastewater system assets placed in service during fiscal year 2015 and a partial year of depreciation of $53.6 million of wastewater system assets placed in service during fiscal year 2016. $12.1 million of wastewater system assets were retired during the fiscal year.
- Taxes and tax equivalents increased $0.2 million compared to the prior fiscal year, due to increased plant in service levels.

Fiscal Year 2015 Compared to Fiscal Year 2014

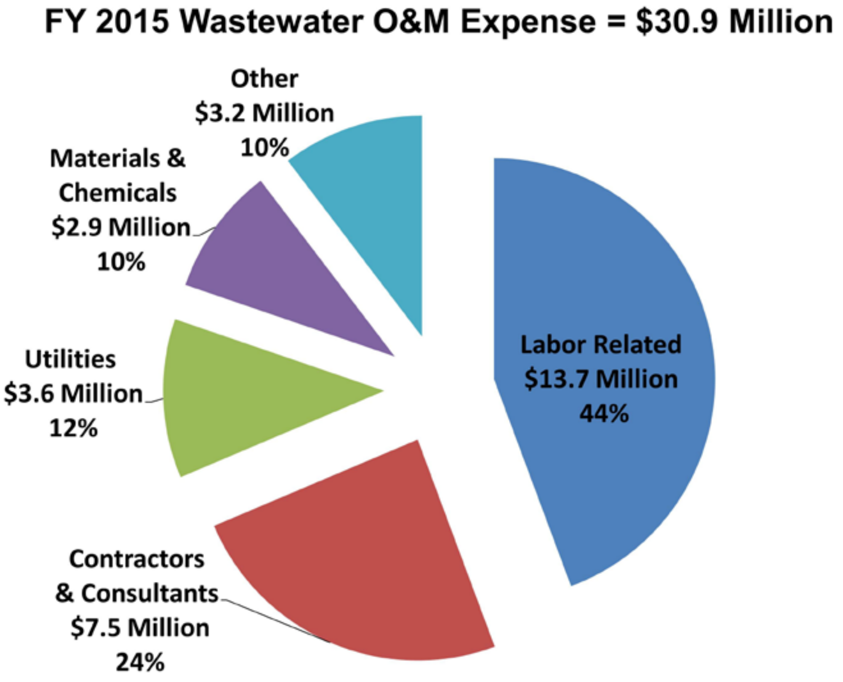
Operating expenses increased $2.5 million or 5 percent compared to fiscal year 2014. Operating expenses include operations and maintenance (O&M) expense, depreciation, and taxes/tax equivalents. O&M expenses can be further classified as treatment, collection, customer service and administrative and general.

- Treatment expenses were up $0.8 million, primarily due to higher consulting and contracting expenses.

- Collection system expenses increased $0.8 million, reflecting higher labor related expenses, outside contractor expenses for lift station maintenance and repairs, and outside consultant expenses for blockage abatement.

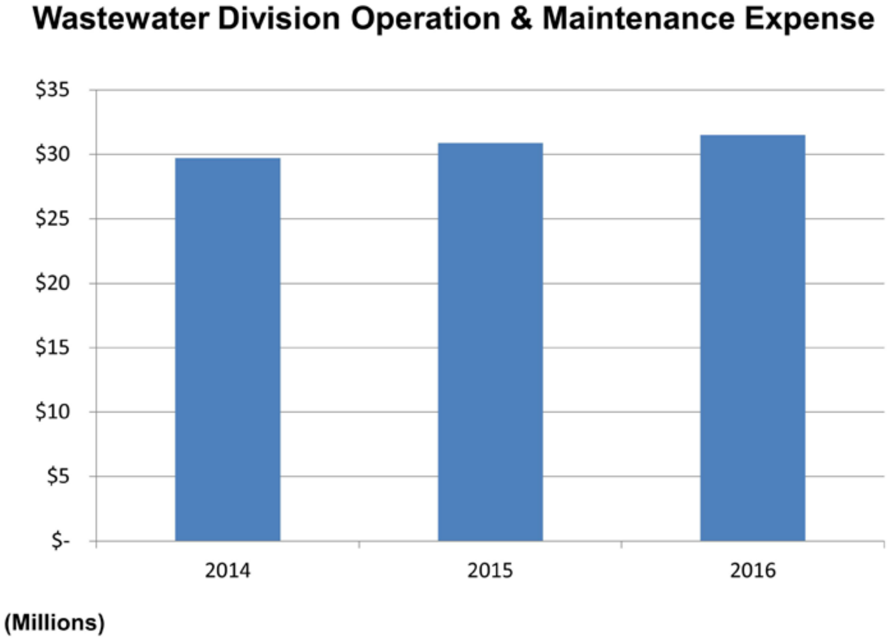
- Customer service expenses increased $0.2 million, reflecting the Division’s share of expenses for software licenses.

- Administrative and general expenses decreased $0.6 million, due to a decrease in pension expense.



- Depreciation expense increased $1 million or 6.5 percent, the result of a full year of depreciation on $72.3 million of wastewater system assets placed in service during fiscal year 2014, and a partial year of depreciation on $16.2 million placed in service during fiscal year 2015. $3.4 million of wastewater system assets were retired during the fiscal year.

- Taxes and tax equivalents increased $0.2 million. The City of Knoxville’s property tax rate increased this year and higher plant in service levels contributed to the growth in tax equivalent payments.



Other Income and Expense

Fiscal Year 2016 Compared to Fiscal Year 2015

Interest income was $0.2 million higher than the prior fiscal year.

Interest expense increased $0.8 million or 4.2 percent, the net effect of interest expense associated with bonds issued in fiscal year 2015 offset by debt interest savings from refinancing outstanding bonds at lower interest rates.

Other income (net) was $0.3 million lower, primarily due to a loss on disposition of wastewater system assets.

Capital contributions increased $0.3 million compared to last fiscal year as a result of additional assets received from developers and other governmental entities.

Fiscal Year 2015 Compared to Fiscal Year 2014

Interest income was consistent with the prior fiscal year.

Interest expense increased $0.1 million or less than one percent, the net effect of additional interest expense associated with $60 million in new bonds offset by debt interest savings from bond refinancing.

Other income (net) was $0.4 million lower primarily, due to a prior year loss on disposition of wastewater system assets.

Capital contributions increased $0.1 million compared to last fiscal year as a result of additional assets received from developers and other governmental entities.

Capital Assets

Capital Assets
As of June 30
(Net of Depreciation)

(in thousands of dollars)

	2016	2015	2014
Pumping & Treatment Plant	$ 144,383	$ 135,248	$ 136,055
Collection Plant			
Mains and Metering	416,102	390,454	389,515
Other Accounts	70,145	71,708	72,884
Total Collection Plant	486,247	462,162	462,399
Total General Plant	8,480	8,101	8,070
Total Wastewater Plant	$ 639,110	$ 605,511	$ 606,524
Work In Progress	47,946	58,667	35,778
Total Net Plant	$ 687,056	$ 664,178	$ 642,302

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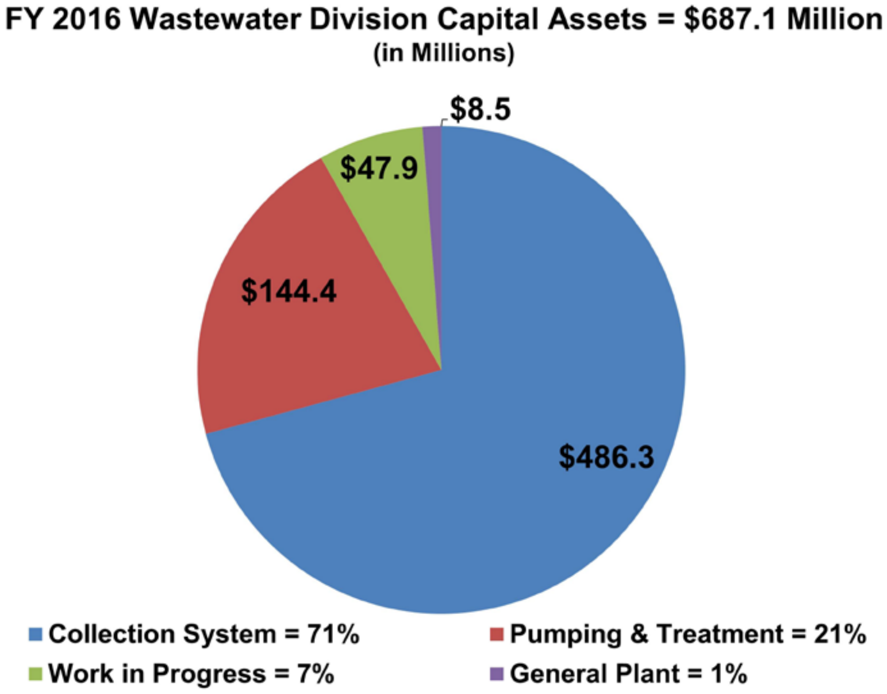
Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, the Division had $687.1 million invested in a variety of capital assets, as reflected in the schedule of capital assets, which represents a net increase (including additions, retirements, and depreciation) of $22.9 million or 3.4 percent over the end of the last fiscal year.



Major capital asset expenditures during the year were as follows:

- $32.6 million related to Century II projects
    - $15.8 million for sewer mini-basin rehabilitation and replacement
    - $7.7 million for sewer trunk line rehabilitation and replacement
    - $5.3 million for pump station design and construction
    - $3.8 million for wastewater treatment plant upgrades
- $1.8 million for upgrades to various information systems
- $1.3 million for replacement and relocation of wastewater system assets to accommodate TDOT highway improvement projects

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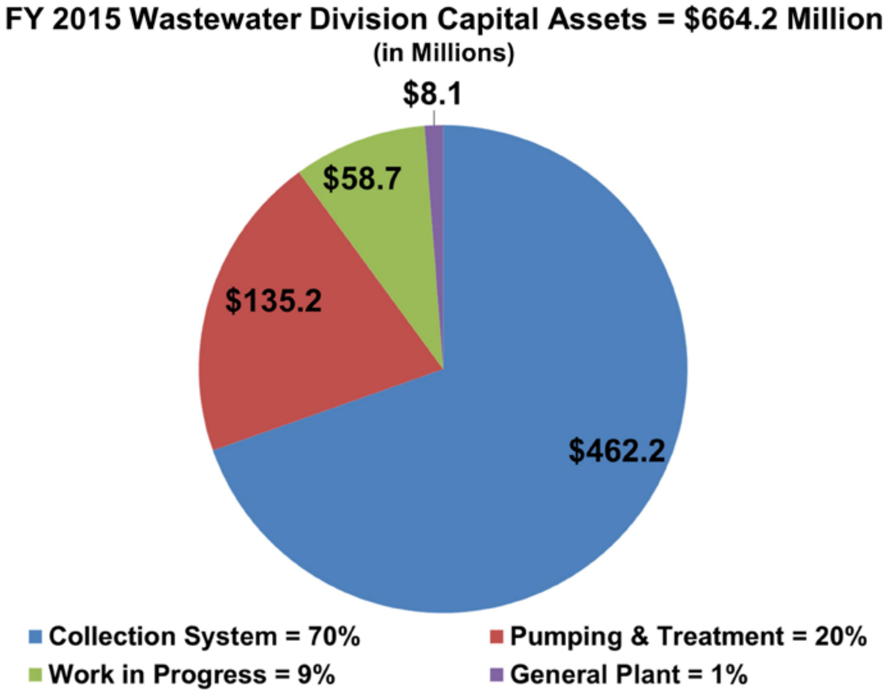
Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, the Division had $664.2 million invested in a variety of capital assets, as reflected in the schedule of capital assets, which represents a net increase (including additions, retirements, and depreciation) of $21.9 million or 3.4 percent over the end of the last fiscal year.



Major capital asset expenditures during the year were as follows:

- $25.3 million related to Century II projects
    - $20.4 million for sewer mini-basin rehabilitation and replacement
    - $2.6 million for pump station design and construction
    - $1.3 million for wastewater treatment plant upgrades
    - $1 million for sewer trunk line rehabilitation and replacement
- $7 million for system improvements
- $1.8 million for information system upgrades

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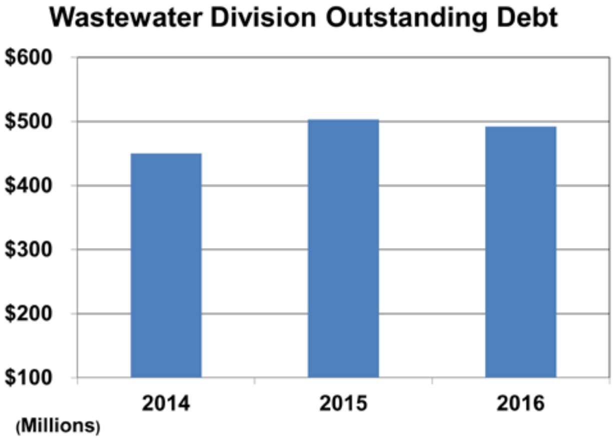
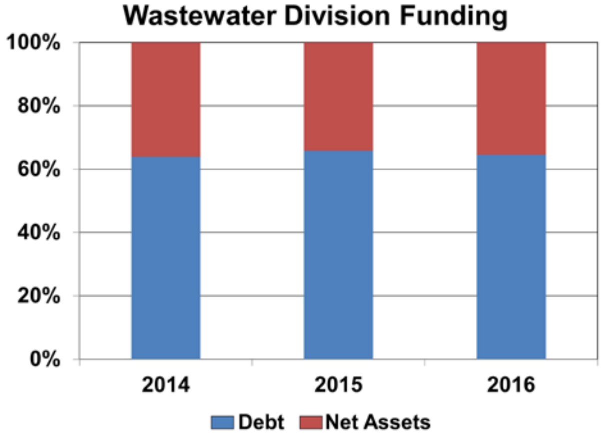
Debt Administration

As of June 30, 2016, the Wastewater Division had $492.3 million in outstanding wastewater system bonds. The Division's outstanding debt rose in fiscal year 2015 to $503.3 million due to $60 million in new bonds sold during the fiscal year. As part of the Century II Infrastructure Program, as well as PACE10 in previous years, bond proceeds were used to fund capital improvements for the wastewater system. The bonds are secured solely by revenues of the Wastewater Division. Debt as a percentage of the Division's capital structure was 64.5 percent in 2016, 65.8 percent in 2015 and 63.9 percent at the end of fiscal year 2014. KUB's Debt Management Policy limits the Division's debt ratio to 70 percent or less.

Outstanding Debt
As of June 30

(in thousands of dollars)	**2016**	**2015**	**2014**
Revenue bonds	$ 492,330	$ 503,260	$ 450,050
Total outstanding debt	$ 492,330	$ 503,260	$ 450,050





The Division will pay $129.9 million in principal payments over the next ten years, representing 26.4 percent of the outstanding bonds. KUB's Debt Management Policy requires a minimum of 20 percent of wastewater debt principal be repaid over the next ten years.

Fiscal Year 2016 Compared to Fiscal Year 2015

As of June 30, 2016, the Division had $492.3 million in outstanding debt (including the current portion of revenue bonds), representing a decrease of $11 million or 2.2 percent. The decrease is attributable to the scheduled repayments of bond debt. The Division's weighted average cost of debt as of June 30, 2016 was 4.03 percent.

The Division's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2016, the Division's revenue bonds were rated AA+ by Standard & Poor's and Aa2 by Moody's Investors Service.

Fiscal Year 2015 Compared to Fiscal Year 2014

As of June 30, 2015, the Division had $503.3 million in outstanding debt (including the current portion of revenue bonds), compared to $450.1 million last year, representing an increase of $53.2 million or 11.8 percent. The Division's weighted average cost of debt as of June 30, 2015 was 4.03 percent.

The increase is attributable to the issuance of revenue bonds during the fiscal year of $30 million in August 2014 and $30 million in April 2015. The increase was partially offset by scheduled repayments of bond debt.

In April 2015, KUB sold $129.8 million of revenue refunding bonds. The refunding of certain bonds at lower interest rates will provide debt service savings of $13.4 million over the life of the bonds.

The Division's outstanding debt is rated by Standard & Poor's and Moody's Investors Service. As of June 30, 2015, the Division's revenue bonds were rated AA+ by Standard & Poor's and Aa2 by Moody's Investors Service.

Impacts on Future Financial Position

KUB anticipates adding 250 wastewater customers in fiscal year 2017.

In June 2014, the KUB Board adopted three years of rate increases for all four Divisions to help fund the ongoing Century II infrastructure programs for each system. The first and second rate increases were effective October 2014 and October 2015. The remaining wastewater rate increase will be effective October 2016. The wastewater rate increases provide additional annual revenue of $4.7 million.

KUB sold $20 million in wastewater system revenue bonds in July 2016 for the purpose of funding wastewater system capital improvements. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.72 percent.

KUB long-term debt includes $94.5 million of Wastewater Division 2010 Build America Bonds (BABs). The BABs were sold on a taxable basis with the United States Treasury providing a rebate to KUB for a percentage of the interest cost. The interest rebates were subject to federal sequestration during the fiscal year and were reduced by 6.8 percent. Any future actions by Congress may also affect the anticipated rebates for future fiscal years.

GASB Statement No. 82, *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73* is effective for fiscal years beginning after June 15, 2016. GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* and GASB No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* are effective for periods beginning after June 15, 2017. KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

No other facts, decisions, or conditions are currently known which would have a significant impact on the Division's financial position or results of operations during fiscal year 2016.

Financial Contact

The Division's financial statements are designed to present users (citizens, customers, investors, and creditors) with a general overview of the Division's financial position and results of operations for the fiscal years ending June 30, 2016 and 2015. If you have questions about the statements or need additional financial information, contact KUB's Chief Financial Officer at 445 South Gay Street, Knoxville, Tennessee 37902.

Knoxville Utilities Board Wastewater Division
Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Assets and Deferred Outflows of Resources		
Current assets:		
Cash and cash equivalents	$ 23,725,645	$ 32,853,270
Short-term contingency fund investments	10,857,109	456,174
Other current assets	45,463	45,356
Accrued interest receivable	10,171	7,154
Accounts receivable, less allowance of uncollectible accounts of $106,528 in 2016 and $88,128 in 2015	9,176,445	8,848,535
Inventories	314,034	248,831
Prepaid expenses	85,397	64,592
Total current assets	44,214,264	42,523,912
Restricted assets:		
Wastewater bond fund	7,696,384	7,097,019
Other funds	4,712	9,218
Unused bond proceeds	-	15,605,921
Total restricted assets	7,701,096	22,712,158
Wastewater plant in service	812,426,671	770,902,707
Less accumulated depreciation	(173,316,844)	(165,391,520)
	639,109,827	605,511,187
Retirement in progress	185,012	187,702
Construction in progress	47,761,132	58,479,696
Net plant in service	687,055,971	664,178,585
Other assets:		
Net pension asset	-	1,264,542
Long-term contingency fund investments	23,110,075	32,373,560
Other	5,049,594	5,224,902
Total other assets	28,159,669	38,863,004
Total assets	767,131,000	768,277,659
Deferred outflows of resources:		
Pension outflow	2,278,604	663,012
Unamortized bond refunding costs	17,134,459	17,929,691
Total deferred outflows of resources	19,413,063	18,592,703
Total assets and deferred outflows of resources	$ 786,544,063	$ 786,870,362

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Wastewater Division
Statements of Net Position
June 30, 2016 and 2015

	2016	2015
Liabilities, Deferred Inflows, and Net Position		
Current liabilities:		
Current portion of revenue bonds	$ 10,930,000	$ 10,930,000
Accounts payable	2,340,915	899,476
Accrued expenses	716,125	579,027
Customer deposits plus accrued interest	917,734	1,037,256
Accrued interest on revenue bonds	4,963,784	4,482,373
Total current liabilities	19,868,558	17,928,132
Other liabilities:		
Accrued compensated absences	1,584,302	1,661,822
Customer advances for construction	-	306,000
Net pension liability	1,108,835	-
Other	67,881	85,069
Total other liabilities	2,761,018	2,052,891
Long-term debt:		
Wastewater revenue bonds	481,400,000	492,330,000
Unamortized premiums/discounts	11,066,224	11,625,190
Total long-term debt	492,466,224	503,955,190
Total liabilities	515,095,800	523,936,213
Deferred inflows of resources:		
Pension inflow	332,699	1,339,445
Total deferred inflows of resources	332,699	1,339,445
Total liabilities and deferred inflows of resources	515,428,499	525,275,658
Net position		
Net investment in capital assets	205,783,783	172,143,725
Restricted for:		
Debt service	2,732,600	2,614,646
Other	4,712	9,218
Unrestricted	62,594,469	86,827,115
Total net position	271,115,564	261,594,704
Total liabilities, deferred inflows, and net position	$ 786,544,063	$ 786,870,362

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Wastewater Division
Statements of Revenues, Expenses and Changes in Net Position
Years Ended June 30, 2016 and 2015

	2016	2015
Operating revenues	$ 83,645,509	$ 79,206,028
Operating expenses		
Treatment	12,515,728	11,596,638
Collection	7,462,333	8,608,980
Customer service	2,961,518	2,837,597
Administrative and general	8,571,620	7,845,973
Provision for depreciation	18,342,674	17,130,721
Taxes and tax equivalents	4,537,378	4,300,666
Total operating expenses	54,391,251	52,320,575
Operating income	29,254,258	26,885,453
Non-operating revenues (expenses)		
Contributions in aid of construction	652,525	394,551
Interest and dividend income	461,544	301,292
Interest expense	(20,168,993)	(19,355,169)
Amortization of debt costs	(473,327)	(405,039)
Write-down of plant for costs recovered through contributions	(652,525)	(394,551)
Other	(243,304)	(27,974)
Total non-operating revenues (expenses)	(20,424,080)	(19,486,890)
Change in net position before capital contributions	8,830,178	7,398,563
Capital contributions	690,682	357,246
Change in net position	9,520,860	7,755,809
Net position, beginning of year, as previously reported	261,594,704	253,999,330
Change in method of accounting for pension	-	(160,435)
Net position, beginning of year, as restated	261,594,704	253,838,895
Net position, end of year	$ 271,115,564	$ 261,594,704

The accompanying notes are an integral part of these financial statements.

Knoxville Utilities Board Wastewater Division
Statements of Cash Flows
Years Ended June 30, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Cash receipts from customers	$ 80,657,704	$ 76,288,189
Cash (payments to) receipts from other operations	2,243,560	1,399,282
Cash payments to suppliers of goods or services	(19,375,607)	(21,331,092)
Cash payments to employees for services	(11,216,903)	(10,185,046)
Payment in lieu of taxes	(3,789,989)	(3,575,461)
Net cash provided by operating activities	48,518,765	42,595,872
Cash flows from capital and related financing activities:		
Net proceeds from bond issuance	-	60,671,698
Principal paid on revenue bonds and notes payable	(10,930,000)	(9,390,000)
(Increase) decrease in unused bond proceeds	15,605,921	(15,605,921)
Interest paid on revenue bonds and notes payable	(19,687,582)	(19,633,440)
Acquisition and construction of wastewater plant	(41,981,738)	(39,310,006)
Changes in wastewater bond fund, restricted	(599,366)	(82,523)
Customer advances for construction	-	(6,000)
Proceeds received on disposal of plant	17,546	-
Cash received from developers and individuals for capital purposes	652,525	394,551
Net cash used in capital and related financing activities	(56,922,694)	(22,961,641)
Cash flows from investing activities:		
Purchase of investment securities	(1,458,958)	(7,241,807)
Maturities of investment securities	455,690	4,810,557
Interest received	458,527	297,004
Other property and investments	(178,955)	(60,634)
Net cash provided by (used in) investing activities	(723,696)	(2,194,880)
Net increase (decrease) in cash and cash equivalents	(9,127,625)	17,439,351
Cash and cash equivalents, beginning of year	32,853,270	15,413,919
Cash and cash equivalents, end of year	$ 23,725,645	$ 32,853,270
Reconciliation of operating income to net cash provided by operating activities		
Operating income	$ 29,254,258	$ 26,885,453
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	18,592,426	17,336,391
Changes in operating assets and liabilities:		
Accounts receivable	(327,909)	(647,772)
Inventories	(65,202)	(48,067)
Prepaid expenses	(20,805)	11,080
Other assets	(57,354)	(559,797)
Accounts payable and accrued expenses	1,280,061	(402,115)
Customer deposits plus accrued interest	(119,522)	19,006
Other liabilities	(17,188)	1,693
Net cash provided by operating activities	$ 48,518,765	$ 42,595,872
Noncash capital activities:		
Acquisition of plant assets through developer contributions	$ 690,682	$ 357,246

The accompanying notes are an integral part of these financial statements.

1. Description of Business

Knoxville Utilities Board (KUB), comprised of the Electric Division, Gas Division, Water Division, and Wastewater Division (Divisions), is reported as a component unit enterprise fund in the financial statements of the City of Knoxville. KUB's responsibility is to oversee the purchase, production, distribution, and processing of electricity, natural gas, water, and wastewater services. A seven-member Board of Commissioners (Board) governs KUB. The Board has all powers to construct, acquire, expand, and operate the Divisions. It has full control and complete jurisdiction over the management and operation of the Divisions including setting rates. The Wastewater Division (Division) provides services to certain customers in Knox County and in two surrounding counties in East Tennessee. The Division's accounts are maintained in conformity with the Uniform System of Accounts of the National Association of Regulatory Utility Commissioners (NARUC) and the Governmental Accounting Standards Board (GASB), as applicable. The financial statements present only the Wastewater Division and do not purport to, and do not, present fairly the consolidated financial position of Knoxville Utilities Board at June 30, 2016 and 2015, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

2. Significant Accounting Policies

Basis of Accounting

In conformity with Generally Accepted Accounting Principles (GAAP), KUB follows the provisions of GASB Statement No. 34 (Statement No. 34), *Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* as amended by GASB Statement No. 63 (Statement No. 63), *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position.* Statement No. 34 established standards for external financial reporting for all state and local governmental entities. Under Statement No. 63, financial statements include deferred outflows of resources and deferred inflows of resources, in addition to assets and liabilities, and will report *net position* instead of net assets. In addition, KUB follows GASB Statement No. 62 (Statement No. 62), *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* as it relates to certain items for regulatory accounting. Regulatory accounting allows a regulated utility to defer a cost (a regulatory asset) or recognize an obligation (a regulatory liability) if it is probable that through the rate making process, there will be a corresponding increase or decrease in future revenues. Accordingly, KUB has recognized certain regulatory assets and regulatory liabilities in the accompanying Statements of Net Position.

The financial statements are prepared on the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred. The accounting and financial reporting treatment applied to the Division is determined by measurement focus. The transactions of the Division are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the Statement of Net Position. Net position (i.e., total assets and deferred outflows of resources net of total liabilities and deferred inflows of resources) is segregated into net investment in capital assets, restricted for capital activity and debt service, and unrestricted components.

Recently Adopted New Accounting Pronouncements

In February 2015, the Governmental Accounting Standards Board (GASB) issued Statement No. 72 (Statement No. 72), *Fair Value Measurement and Application.* Statement No. 72 is intended to provide guidance for determining a fair value measurement for financial reporting purposes and for applying fair value to certain investments and disclosures related to all fair value measurements.

In June 2015, the GASB issued GASB Statement No. 73 (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 Provision of GASB Statements 67 and 68.* The requirements of this Statement will improve financial reporting by establishing a single framework for the presentation of information about pensions and enhance comparability.

In June 2015, the GASB issued GASB Statement No. 76 (Statement No. 76), *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to simplify the hierarchy of generally accepted accounting principles (GAAP) used to prepare financial statements of state and local governmental entities. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments,* and amends Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, paragraphs 64, 74, and 82.

In December 2015, the GASB issued GASB Statement No. 79 (Statement No. 79), *Certain External Investment Pools and Pool Participants.* This statement establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes.

Statements No. 72, 73, 76, and 79 are effective for fiscal years beginning after June 15, 2015.

Wastewater Plant

Wastewater plant and other property are stated on the basis of original cost. The cost of current repairs and minor replacements is charged to operating expense. The cost of renewals and improvements is capitalized. The original cost of utility plant assets retired or otherwise disposed of and the cost of removal less salvage value is charged to accumulated depreciation. When other property is retired, the related asset and accumulated depreciation are removed from the accounts, and the gain or loss is included in the results of operations.

The provision for depreciation of wastewater plant in service is based on the estimated useful lives of the assets, which range from three to fifty years, and is computed using the straight-line method. Pursuant to NARUC, the caption "Provision for depreciation" in the Statements of Revenue, Expenses and Change in Net Position does not include depreciation for transportation equipment of $249,752 in fiscal year 2016 and $205,670 in fiscal year 2015. Under regulatory accounting, interest costs are expensed as incurred with construction of plant assets.

Operating Revenue

Operating revenue consists primarily of charges for services provided by the principal operations of the KUB Wastewater Division. Operating revenue is recorded when the service is rendered, on a cycle basis, and includes an estimate of unbilled revenue. Revenues are reported net of bad debt expense of $249,369 in fiscal year 2016 and $213,886 in fiscal year 2015.

Non-operating Revenue

Non-operating revenue consists of revenues that are related to financing and investing types of activities and result from non-exchange transactions or ancillary activities.

Expense

When an expense is incurred for purposes for which there are both restricted and unrestricted net assets available, it is KUB's policy to apply those expenses to restricted net assets to the extent such are available and then to unrestricted net assets.

Net Position

GASB Statement No. 63 requires the classification of net position into three components – net investment in capital assets; net position-restricted; and net position-unrestricted.

These classifications are defined as follows:

- Net investment in capital assets – This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt also should be included in this component of net position. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

- Net position-restricted – This component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported.

- Net position-unrestricted – This component of net position consists of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

Contributions in Aid of Construction and Capital Contributions

Contributions in aid of construction are cash collections from customers or others for a particular purpose, generally the construction of new facilities to serve new customers in excess of the investment KUB is willing to make for a particular incremental revenue source. KUB reduces the plant account balances to which contributions relate by the actual amount of the contribution and recognizes the contributions as non-operating revenue in accordance with Statement No. 62.

Capital contributions represent contributions of utility plant infrastructure constructed by developers and others in industrial parks and other developments, and transferred to KUB upon completion of construction and the initiation of utility service. In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, such contributions are recognized as revenues and capital assets upon receipt.

Inventories

Inventories, consisting of plant materials and operating supplies, are valued at the lower of average cost or replacement value.

Change in Method of Accounting for Pension

In June 2012, the Governmental Accounting Standards Board (GASB) issued Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, which revises existing standards of financial reporting for pensions. In addition, during November

2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, which requires deferred outflow of resources to be recognized for any contributions made subsequent to the measurement date of the beginning net pension liability. These standards were adopted by KUB in 2015 and resulted in a restatement of 2015 beginning net position of $763,975 (Division's share $160,435).

Pension Plan

KUB's employees are participants in the Knoxville Utilities Board Pension Plan as authorized by the Charter of the City of Knoxville §1107(J) (Note 10). KUB's policy is to fully fund the annual actuarially determined contributions. As required by GASB Statement No. 68, KUB measures net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30, 2016 and 2015 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 are based on a December 31, 2015 and 2014 measurement date, respectively.

Investments

Investments are carried at fair value as determined by quoted market prices at the reporting date.

Self-Insurance

KUB has established self-insurance programs covering portions of workers' compensation, employee health, environmental liability, general liability, property and casualty liability, and automobile liability claims. A liability is accrued for claims as they are incurred. When applicable, claims in excess of the self-insured risk are covered by KUB's insurance carrier. Additionally, KUB provides certain lifetime health benefits to eligible retired employees under a self-insurance plan administered by a third party.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates are based on historical experience and various other assumptions that KUB believes are reasonable under the circumstances. However, future events are subject to change and the best estimates and judgments routinely require adjustment. Estimates are used for, but not limited to, inventory valuation, allowance for uncollectible accounts, depreciable lives of plant assets, unbilled revenue volumes, pension trust valuations, OPEB trust valuations, insurance liability reserves, and potential losses from contingencies and litigation. Actual results could differ from those estimates.

Restricted and Designated Assets

Certain assets are restricted by bond resolutions for utility plant construction and debt repayment. Certain additional assets are designated by management for contingency purposes and economic development.

Cash Equivalents

For purposes of the Statements of Cash Flows, KUB considers all unrestricted and undesignated highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

Deferred Outflows and Inflows of Resources

Deferred outflows of resources are items previously reported as assets related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. Deferred inflows of resources are items previously reported as liabilities related to the acquisition of assets or related debt which are amortized over the life of the asset or debt. KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. Deferred outflows of resources also include employer pension contributions made subsequent to the measurement date of the net pension liability and before the end of the employer's reporting period in accordance with Statement No. 71. Deferred inflows and deferred outflows also include the net difference between projected and actual earnings on pension plan investments and differences between expected and actual experience in accordance with Statement No. 68.

Debt Premium/Discount

KUB records unamortized premium and discount on debt as a separate line item in the Long Term Debt section of the Financial Statements. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Debt Issuance Costs

In accordance with regulatory accounting, KUB records debt issuance costs as an Other Asset. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Deferred Gain/Loss on Refunding of Debt

KUB records costs associated with the gain or loss on refunding of debt as either a deferred outflow or inflow based on the parameters of Statement No. 65. Amortization of these amounts is recorded over the life of the applicable debt as amortization expense.

Compensated Absences

KUB accrues a liability for earned but unpaid paid-time off (PTO) days.

Subsequent Events

KUB has evaluated events and transactions through October 27, 2016, the date these financial statements were issued, for items that should potentially be recognized or disclosed. KUB sold $20 million in wastewater system revenue bonds in July 2016 for the purpose of funding wastewater system capital improvements in fiscal year 2017. The true interest cost of the bonds, which were sold through a competitive bidding process, was 2.72 percent.

Recently Issued Accounting Pronouncements

In June 2015, the GASB issued two related Statements that affect accounting and financial reporting by state and local governments for postemployment benefits other than pensions (OPEB). GASB Statement No. 74 (Statement No. 74), *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, addresses reporting by OPEB plans that administer benefits on behalf of governments. GASB Statement No. 75 (Statement No. 75), *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, addresses reporting by governments that provide OPEB to their employees. Statement No. 74 is effective for fiscal years beginning after June 15, 2016, and Statement No. 75 is effective for fiscal years beginning after June 15, 2017.

In March 2016, the GASB issued GASB Statement No. 82 (Statement No. 82), *Pension Issues – An amendment of GASB Statements No. 67, No. 68 and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to the presentation of payroll-related measures in required supplementary information, the selection of assumptions and treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes and the classification of payments made by employers to satisfy employee contribution obligations. Statement No. 82 is effective for fiscal years beginning after June 15, 2016.

KUB has not elected early implementation of these standards and has not completed the process of evaluating the impact of these statements on its financial statements.

3. Deposits and Investments

KUB follows the provisions of Statement No. 40 of the Governmental Accounting Standards Board, *Deposit and Investment Risk Disclosures an amendment of GASB Statement No. 3*. This Statement establishes and modifies disclosure requirements for state and local governments related to deposit and investment risks. KUB classifies its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*.

KUB's investment policy provides the framework for the administration and investment of cash deposits. The investment policy follows Tennessee State law and defines the parameters under which KUB funds should be invested. State law authorizes KUB to invest in obligations of the United States Treasury, its agencies and instrumentalities; certificates of deposit; repurchase agreements; money market funds; and the State Treasurer's Investment Pool.

Interest Rate Risk. KUB's primary investment objectives are to place investments in a manner to ensure the preservation of capital, remain sufficiently liquid to meet all operating requirements, and maximize yield of return. KUB minimizes its exposure to interest rate risk by adhering to Tennessee State law requirements for the investment of public funds. This includes limiting investments to those types described above and limiting maturity horizons. The maximum maturity is four years from the date of investment. KUB also limits its exposure by holding investments to maturity unless cash flow requirements dictate otherwise.

Credit Risk. KUB's investment policy, as required by state law, is to apply the prudent-person rule: Investments are made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable income to be derived, as well as the probable safety of their capital. KUB's Agency Bond investments are rated Aaa by Moody's Investors Service.

Custodial Credit Risk. KUB's investment policy limits exposure to custodial credit risk by restricting investments to a standard set forth by State law. All deposits in excess of federal depository insurance limits are collateralized with government securities held in KUB's name by a third-party custodian bank(s) acting as KUB's agent(s), or through the State of Tennessee's collateral pool. Financial institutions that participate in the collateral pool are subject to special assessment; therefore, the deposits are considered insured. A portion of KUB's investments are generally held in the State of Tennessee Local Government Investment Pool (LGIP). The LGIP is a part of the State Pooled Investment Fund and is sponsored by the State of Tennessee Treasury Department. Tennessee Code Annotated ¶9-4-701 *et seq*. authorizes local governments to invest in the LGIP. None of KUB's investments are exposed to custodial credit risk.

Classification of deposits and investments per Statement of Net Position:

	2016	2015
Current assets		
Cash and cash equivalents	$ 23,725,645	$ 32,853,270
Short-term contingency fund investments	10,857,109	456,174
Other assets		
Long-term contingency fund investments	23,006,967	32,306,048
Restricted assets		
Unused bond proceeds	-	15,605,874
Wastewater bond fund	7,696,384	7,097,019
Other funds	4,712	9,218
	$ 65,290,817	$ 88,327,603

The above amounts do not include accrued interest of $103,108 in fiscal year 2016 and $67,559 in fiscal year 2015. Interest income is recorded on an accrual basis.

Investments and maturities of KUB's deposits and investments as held by financial institutions as of June 30, 2016:

	Deposit and Investment Maturities (in Years)		
	Fair Value	Less Than 1	1-5
Supersweep NOW and Other Deposits	$ 29,749,540	$ 29,749,540	$ -
State Treasurer's Investment Pool	1,654,595	1,654,595	-
Agency Bonds	37,801,501	10,857,109	26,944,392
Certificates of Deposits	7,124,064	6,041,689	1,082,375
	$ 76,329,700	$ 48,302,933	$ 28,026,767

KUB categorizes its fair value measurements within the fair value hierarchy established by Statement No. 72 of the Governmental Accounting Standards Board, *Fair Value Measurement and Application*. The hierarchy is based on the valuation inputs used to measure the fair value of an asset with a maturity at purchase greater than one year. 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.

KUB has the following recurring fair value measurements as of June 30, 2016:

- U.S. Agency bonds of $26,944,392, which have a maturity at purchase of greater than one year, are valued using quoted market prices (Level 1 inputs)
- Certificates of deposits of $1,082,375, which have a maturity at purchase of greater than one year, are valued at interest rates and yield curves observable at commonly quoted intervals (Level 2 inputs)

KUB measures investments with a maturity at purchase of one year or less at amortized cost, which is considered a fair value equivalent due to their nature. Investments in the State Treasurer's Investment Pool are measured at net asset value (NAV) per share.

4. Accounts Receivable

Accounts receivable consists of the following:

	2016	2015
Wholesale and retail customers		
Billed services	$ 5,053,928	$ 4,886,812
Unbilled services	3,529,053	3,206,393
Other	699,992	843,458
Allowance for uncollectible accounts	(106,528)	(88,128)
	$ 9,176,445	$ 8,848,535

5. Accounts Payable and Accruals

Accounts payable and accruals were composed of the following:

	2016	2015
Trade accounts	$ 2,340,915	$ 899,476
Salaries and wages	330,469	222,361
Self-insurance liabilities	385,656	356,666
	$ 3,057,040	$ 1,478,503

6. Long-Term Obligations

Long-term debt consists of the following:

	Balance June 30, 2015	Additions	Payments	Defeased	Balance June 30, 2016	Amounts Due Within One Year
2005 B - 3.0 - 5.0%	$ 16,045,000	$ -	$ 1,410,000	$ -	$ 14,635,000	$ 1,470,000
2008 - 4.0 - 6.0%	11,000,000	-	4,450,000	-	6,550,000	4,600,000
2010 - 6.3 - 6.5%	30,000,000	-	-	-	30,000,000	-
2010C - 1.18 - 6.1%	65,750,000	-	1,250,000	-	64,500,000	1,400,000
2012A - 2.0 - 4.0%	15,415,000	-	820,000	-	14,595,000	840,000
2012B - 1.25 - 5.0%	63,275,000	-	925,000	-	62,350,000	975,000
2013A - 2.0 - 4.0%	112,325,000	-	610,000	-	111,715,000	620,000
2014A - 2.0 - 4.0%	29,625,000	-	425,000	-	29,200,000	450,000
2015A - 3.0 - 5.0%	129,825,000	-	465,000	-	129,360,000	125,000
2015B - 3.0 - 5.0%	30,000,000	-	575,000	-	29,425,000	450,000
Total bonds	$ 503,260,000	$ -	$ 10,930,000	$ -	$ 492,330,000	$ 10,930,000
Unamortized Premium	11,625,190	-	558,966	-	11,066,224	-
Total long term debt	$ 514,885,190	$ -	$ 11,488,966	$ -	$ 503,396,224	$ 10,930,000

	Balance June 30, 2014	Additions	Payments	Defeased	Balance June 30, 2015	Amounts Due Within One Year
2005 A - 4.0 - 5.0%	$ 36,550,000	$ -	$ -	$ 36,550,000	$ -	$ -
2005 B - 3.0 - 5.0%	17,395,000	-	1,350,000	-	16,045,000	1,410,000
2007 - 4.0 - 5.0%	75,000,000	-	-	75,000,000	-	-
2008 - 4.0 - 6.0%	30,975,000	-	4,300,000	15,675,000	11,000,000	4,450,000
2010 - 6.3 - 6.5%	30,000,000	-	-	-	30,000,000	-
2010C - 1.18 - 6.1%	66,850,000	-	1,100,000	-	65,750,000	1,250,000
2012A - 2.0 - 4.0%	16,215,000	-	800,000	-	15,415,000	820,000
2012B - 1.25 - 5.0%	64,150,000	-	875,000	-	63,275,000	925,000
2013A - 2.0 - 4.0%	112,915,000	-	590,000	-	112,325,000	610,000
2014A - 2.0 - 4.0%	-	30,000,000	375,000	-	29,625,000	425,000
2015A - 3.0 - 5.0%	-	129,825,000	-	-	129,825,000	465,000
2015B - 3.0 - 5.0%	-	30,000,000	-	-	30,000,000	575,000
Total bonds	$ 450,050,000	$ 189,825,000	$ 9,390,000	$ 127,225,000	$ 503,260,000	$ 10,930,000
Unamortized Premium	4,154,409	8,539,211	312,636	755,794	11,625,190	-
Total long term debt	$ 454,204,409	$ 198,364,211	$ 9,702,636	$ 127,980,794	$ 514,885,190	$ 10,930,000

Debt service over remaining term of the debt is as follows:

Fiscal Year	Total Principal	Interest	Grand Total
2017	$ 10,930,000	$ 19,855,137	$ 30,785,137
2018	11,380,000	19,439,779	30,819,779
2019	11,810,000	18,969,000	30,779,000
2020	12,320,000	18,473,025	30,793,025
2021	12,830,000	17,958,645	30,788,645
2022-2026	70,625,000	80,921,305	151,546,305
2027-2031	76,135,000	67,260,745	143,395,745
2032-2036	91,580,000	52,086,863	143,666,863
2037-2041	105,745,000	32,888,520	138,633,520
2042-2046	74,600,000	11,970,575	86,570,575
2047-2050	14,375,000	1,076,675	15,451,675
Total	$ 492,330,000	$ 340,900,269	$ 833,230,269

The Division has pledged sufficient revenue, after deduction of all current operating expenses (exclusive of tax equivalents), to meet bond principal and interest payments when due. The bond covenants relating to the Wastewater Revenue Bonds require the establishment of a Wastewater Bond Fund for the payment of principal and interest requirements. As of June 30, 2016, those bond covenants had been satisfied.

During fiscal year 2006, KUB's Wastewater Division issued Series 2005B bonds in part to retire certain existing debt and fund wastewater system capital improvements. Concurrent with the issuance of these bonds, KUB transferred funds to an irrevocable trust to pay a portion of the Series 1998 bonds and Series 2001A bonds, as such amounts mature.

During fiscal year 2009, KUB's Wastewater Division issued Series 2008 bonds to fund wastewater system capital improvements.

During fiscal year 2010, KUB's Wastewater Division issued Series 2010 bonds to fund capital improvements. These bonds were issued as federally taxable Build America Bonds with a 35 percent interest payment rebate to be received from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8 percent reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change.

During fiscal year 2011, KUB's Wastewater Division issued Series 2010C bonds to fund wastewater system capital improvements. These bonds were issued as federally taxable Build America Bonds with a 35 percent interest payment rebate to be received from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8 percent reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change.

During fiscal year 2012, KUB's Wastewater Division issued Series 2012A bonds to retire Series 2004A bonds.

During fiscal year 2013, KUB's Wastewater Division issued Series 2012B bonds to fund wastewater system capital improvements. KUB's Wastewater Division also issued Series 2013A bonds to retire a portion of outstanding Series 2005A bonds.

During fiscal year 2015, KUB's Wastewater Division issued Series 2015A bonds to retire a portion of outstanding Series 2005A, Series 2007, and Series 2008 bonds. KUB's Wastewater Division also issued Series 2014A and Series 2015B bonds to fund wastewater system capital improvements.

In prior years, certain revenue bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the liability for the defeased bonds, $90.7 million at June 30, 2016, and the trust account assets are not included in the financial statements.

Other liabilities consist of the following:

	Balance June 30, 2015	**Increase**	**Decrease**	**Balance June 30, 2016**
Accrued compensated absences	$ 1,661,822	$ 3,192,415	$ (3,269,935)	$ 1,584,302
Customer advances for construction	306,000		(306,000)	-
Other	85,069	143,427	(160,615)	67,881
	$ 2,052,891	$ 3,335,842	$ (3,736,550)	$ 1,652,183

7. Lease Commitments

KUB has non-cancelable operating lease commitments for office equipment, property, and vehicles, summarized for the following fiscal years:

2017	$ 8,047
2018	4,749
2019	2,972
2020	1,801
Total operating minimum lease payments	$ 17,569

8. Capital Assets

Capital asset activity was as follows:

	Balance June 30, 2015	Increase	Decrease	Balance June 30, 2016
Pumping & Treatment Plant	$ 206,630,404	$ 14,986,965	$ (1,850,766)	$ 219,766,603
Collection Plant				
Mains and Metering	457,776,419	35,573,089	(9,665,081)	483,684,427
Other Accounts	80,547,995	3,357	(165,471)	80,385,881
Total Collection Plant	$ 538,324,414	$ 35,576,446	$ (9,830,552)	$ 564,070,308
Total General Plant	25,947,889	2,975,604	(333,733)	28,589,760
Total Wastewater Plant	$ 770,902,707	$ 53,539,015	$ (12,015,051)	$ 812,426,671
Less accumulated depreciation	(165,391,520)	(18,624,856)	10,699,532	(173,316,844)
Net Plant Assets	$ 605,511,187	$ 34,914,159	$ (1,315,519)	$ 639,109,827
Work In Progress	58,667,398	41,026,770	(51,748,024)	47,946,144
Total Net Plant	$ 664,178,585	$ 75,940,929	$ (53,063,543)	$ 687,055,971

	Balance June 30, 2014	Increase	Decrease	Balance June 30, 2015
Pumping & Treatment Plant	$ 202,877,753	$ 4,119,355	$ (366,704)	$ 206,630,404
Collection Plant				
Mains and Metering	450,538,908	9,876,536	(2,639,025)	457,776,419
Other	80,411,724	197,288	(61,017)	80,547,995
Total Collection Plant	$ 530,950,632	$ 10,073,824	$ (2,700,042)	$ 538,324,414
Total General Plant	24,303,876	1,974,951	(330,938)	25,947,889
Total Wastewater Plant	$ 758,132,261	$ 16,168,130	$ (3,397,684)	$ 770,902,707
Less accumulated depreciation	(151,608,595)	(17,196,280)	3,413,355	(165,391,520)
Net Plant Assets	$ 606,523,666	$ (1,028,150)	$ 15,671	$ 605,511,187
Work In Progress	35,777,951	39,146,048	(16,256,601)	58,667,398
Total Net Plant	$ 642,301,617	$ 38,117,898	$ (16,240,930)	$ 664,178,585

9. Risk Management

KUB is exposed to various risks of loss related to active and retiree medical claims; injuries to workers; theft of, damage to, and destruction of assets; environmental damages; and natural disasters. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported.

These liabilities are included in accrued expenses in the Statement of Net Position. The liability is KUB's best estimate based on available information. At June 30, 2016 and 2015, the amount of these liabilities was $385,656 and $356,666, respectively, resulting from the following changes:

	2016	2015
Balance, beginning of year	$ 356,666	$ 330,289
Current year claims and changes in estimates	3,104,281	2,971,832
Claims payments	(3,075,291)	(2,945,455)
Balance, end of year	$ 385,656	$ 356,666

10. Pension Plan

Description of Plan

The Knoxville Utilities Board Pension Plan (the Plan) is a governmental plan as defined by the Employee Retirement Income Security Act of 1974 ("ERISA" or the "Act"), is not subject to any of the provisions of the Act, and was revised January 1, 2014 to include all prior approved amendments. The Plan is a single-employer contributory, defined benefit pension plan established by Knoxville Utilities Board ("KUB") Resolution No. 980 dated February 18, 1999, effective July 1, 1999, as authorized by the Charter of the City of Knoxville §1107(J). The Plan is designed to provide retirement, disability and death benefits to KUB employees. KUB administers the Plan through an Administrative Committee consisting of seven KUB employees that are appointed by KUB's President and CEO. Any amendments to the Plan involving costs not approved in the operating budget must be adopted by KUB's Board of Commissioners, upon recommendation by KUB's President and CEO. All other amendments to the Plan may be approved by KUB's President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The Plan issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017. For purposes of this disclosure, presentation is on a consolidated basis unless division's share is specified.

Effective January 1, 2011, KUB closed the Plan such that persons employed or re-employed by KUB on or after January 1, 2011, are not eligible to participate, but that eligible employees hired prior to January 1, 2011, who have not separated from service, shall continue as Participants and to accrue benefits under the Plan.

Participants in the Plan consisted of the following as of December 31:

	2015	2014
Inactive plan members:		
Terminated vested participants	39	40
Retirees and beneficiaries	628	627
Active plan members	692	725
Total	1,359	1,392

Retirement Benefits

The Plan provides three benefit arrangements for KUB participants, retirees, and beneficiaries.

The Plan provides pension benefits through the Career Equity Program ("CEP") for eligible employees hired on or after January 1, 1999, and for eligible former "City System Plan A" participants who elected CEP coverage as of July 1, 1999. The guaranteed pension benefit payable to a participant who has completed five or more years of service (or reached the normal retirement date, if earlier) upon termination of KUB employment shall be a lump sum equal to the participant's average compensation times their benefit percentage, as defined in the Plan document, or an annuity may be chosen by the participant.

In addition, the Plan provided retirement benefits through "Plan A" for former City System Plan A participants who elected not to participate in the CEP. Plan A is a closed plan and is not available to KUB employees hired after July 1, 1999. Plan A provides for early retirement benefits with 25 years of service and normal retirement benefits at age 62 or later. Benefits provided to Plan A participants include several different forms of monthly annuity payments.

The Plan also provides retirement benefits through "Plan B" for former "City System Plan B" participants. Plan B is a closed plan providing benefits to participants not covered by Social Security. Benefits provided to Plan B participants include several different forms of monthly annuity payments available to participants.

Effective January 1, 2012, KUB began to provide for additional monthly supplements, which will not be subject to cost of living adjustments, to certain former employees and surviving dependents of former employees who are eligible for and have elected coverage under the KUB retiree medical plan and are eligible for Medicare. This was done to address the loss of drug coverage under the KUB retiree medical plan and to assist such individuals in obtaining prescription drug coverage under Medicare Part D.

Contributions

Participation in Plan A requires employee contributions of 3 percent of the first $4,800 of annual earnings and 5 percent of annual earnings in excess of $4,800. Plan B participants may not make contributions to the Plan. KUB contributions are determined by the enrolled actuary of the Plan and equal the amount necessary to provide the benefits under the Plan determined by the application of accepted actuarial methods and assumptions. The method of funding shall be consistent with Plan objectives.

Plan Funding

KUB maintains a Funding Policy for the Plan in accordance with Tennessee State Law. The primary goal of the Policy is to document the method KUB has adopted to provide assurance that future KUB and employee contributions and current Plan assets will be sufficient to fund all benefits expected to be paid to current active, inactive and retired Plan participants and their beneficiaries. Per the Funding Policy, KUB fully funds its annual Actuarially Determined Contribution.

Investments

The Plan's investments are held by State Street Bank and Trust Company (the "Trustee"). The Plan's policy in regard to the allocation of invested assets is established by the Investment Committee and approved by the KUB Board of Commissioners and may only be amended by the KUB Board of Commissioners. It is the policy of the Investment Committee to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes. The following was the Plan's adopted asset allocation policy as of December 31, 2015:

Asset Class	Target Allocation
Domestic equity – large cap	20% - 50%
Domestic equity – mid cap	0% - 15%
Domestic equity – small cap	0% - 15%
Domestic equity - convertible securities	0% - 10%
Non-U.S. equity	0% - 20%
Real estate equity	0% - 10%
Fixed income – aggregate bonds	5% - 25%
Fixed income – long-term bonds	10% - 25%
Cash and deposits	0% - 5%

Contributions of $5,669,380 and $6,314,399 for 2014 and 2013, respectively, were made during KUB's fiscal years ending June 30, 2016 and 2015, respectively. Of these amounts, $1,247,264 and $1,326,024 are attributable to the Wastewater Division. The contribution was determined as part of the January 1, 2014 valuation using the Individual Entry Age Normal funding method. The objective under this method is to fund each participant's benefits under the Plan as payments which are level as a percentage of salary, starting on the original participation date (employment date) and continuing until the assumed retirement, termination, disability or death. The actuarial valuation for the Plan year ending December 31, 2015 resulted in an actuarially determined contribution of $4,816,913 for the fiscal year ending June 30, 2017, based on the Plan's current funding policy. The Wastewater Division's portion of this contribution is $1,059,721.

Subsequent to June 30, 2016, the actuarial valuation for the Plan year ending December 31, 2016 was completed. The actuarial valuation resulted in an actuarially determined contribution of $3,756,283 for the fiscal year ending June 30, 2018, based on the Plan's current funding policy. The Wastewater Division's portion of this contribution is $826,382. For the Plan year ending December 31, 2016, the Plan's actuarial funded ratio was 103.04 percent.

The actuarial valuations for the Plan years ending December 31, 2015 and 2016, which determine the actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Implementation of GASB 68

In fiscal year 2015, KUB adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27* ("GASB 68"), which requires measurement of the net pension liability as total pension liability less the amount of the Plan's fiduciary net position. The amounts reported as of June 30 must be based upon a plan measurement date within the prior twelve months. Therefore, KUB's measurements as of June 30, 2016 and 2015 will be based on the December 31, 2015 and 2014 measurement date, respectively. The division's share of the net pension liability at June 30, 2016 is $1,108,835 and the net pension asset at June 30, 2015 is $1,264,542.

GASB 68 requires certain disclosures related to the net pension liability of the Plan as disclosed below:

		2015		**2014**
Total pension liability	$	204,502,350	$	202,773,764
Plan fiduciary net position		199,462,190		(208,795,394)
Plan's net pension liability (asset)	$	5,040,160	$	(6,021,630)
Plan fiduciary net position as a percentage of the total pension liability		97.54%		102.97%

Changes in Net Pension Liability are as follows:

		Total Pension Liability (a)		Increase (Decrease) Plan Fiduciary Net Position (b)		Net Pension Liability (a) - (b)
Balances at December 31, 2014	$	202,773,764	$	208,795,394	$	(6,021,630)
Changes for the year:						
Service cost		4,157,062		-		4,157,062
Interest		14,812,784		-		14,812,784
Differences between Expected and Actual Experience		(1,890,334)		-		(1,890,334)
Changes of Assumptions		-		-		-
Contributions - employer		-		5,991,887		(5,991,887)
Contributions - rollovers		-		482,060		(482,060)
Contributions - member		-		5,486		(5,486)
Net investment income		-		(64,551)		64,551
Benefit payments		(15,350,926)		(15,350,926)		-
Administrative expense		-		(397,160)		397,160
Net changes		1,728,586		(9,333,204)		11,061,790
Balances at December 31, 2015	$	204,502,350	$	199,462,190	$	5,040,160

Actuarial Assumptions

The total pension liability was determined by an actuarial valuation as of December 31, 2015 and 2014, using the following actuarial assumptions, applied to all periods included in the measurement:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.80% to

	5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the January 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation
Inflation	2.8 percent

The actuarial assumptions used in the December 31, 2015 valuation were based on the results of an actuarial experience study for the period January 1, 2009 through December 31, 2013.

The long-term expected rate of return on Plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of Plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the Plan's target asset allocation as of December 31, 2015 and 2014 are summarized in the following table. The real rate of return reported for fixed income is for aggregate fixed income. The Plan has both aggregate and long duration fixed income.

	Long Term Expected Real Rate of Return	
Asset Class	**2015**	**2014**
Domestic equity	7.2%	6.0%
Non-U.S. equity	7.4%	7.0%
Real estate equity	6.5%	5.7%
Fixed income	3.7%	1.8%
Cash and deposits	2.6%	0.5%

Discount rate
The discount rate used to measure the total pension liability was 7.5 percent as of January 1, 2015 and 2014. The projection of cash flows used to determine the discount rate assumed that participant contributions will be made at the current contribution rate and that KUB contributions will be made at rates equal to the actuarially determined contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the net pension liability to changes in the discount rate
The following presents the net pension liability of the Plan as of December 31, 2015, calculated using the discount rate of 7.5 percent, as well as what the Plan's net pension liability would be if it were calculated using a discount rate that is one percent lower (6.5 percent) or one percent higher (8.5 percent) than the current rate:

	1% Decrease (6.5%)	**Current Discount Rate (7.5%)**	**1% Increase (8.5%)**
Plan's net pension liability	$ 17,128,897	$ 5,040,160	$ (5,963,331)

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

For the year ended June 30, 2015, KUB recognized pension expense of $2,749,905 (Division’s share $577,480).

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in expense over the average expected remaining service life of all active and inactive members. As of the measurement date, this recognition period was 3.72 years. However, there were no experience gains or losses, and there were no assumption changes during the measurement year.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment gain of $7,972,887. $1,594,577 of that gain was recognized in the current year and an identical amount will be recognized in each of the next four years, resulting in a deferred inflow of resources of $6,378,310 (Division’s share $1,339,445). The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over the next five years. In addition, KUB recorded a deferred outflow of resources of $3,157,199 (Division’s share $663,012) at June 30, 2015 for employer contributions made between December 31, 2014 and June 30, 2015.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ -
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	-	6,378,310
Contributions subsequent to measurement date	3,157,199	-
Total	$ 3,157,199	$ 6,378,310

For the year ended June 30, 2016, KUB recognized pension expense of $4,665,035 (Division’s share $1,026,308).

The impact of experience gains or losses and assumption changes on the Total Pension Liability are recognized in the pension expense over the average expected remaining service life of all active and inactive members, determined as of the beginning of the measurement period. As of December 31, 2014, this average was 5.00 years. During the measurement year, there were no assumption or benefit changes. There was an experience gain of $1,890,334 with $378,067 of that recognized in the current year and in each of the next four years.

The impact of investment gains or losses is recognized over a period of five years. During the measurement year, there was an investment loss of $15,382,915. $3,076,583 of that loss was recognized in the current year and an identical amount will be recognized in each of the next four years. Unrecognized investment gains from prior periods were $6,378,310 of which $1,594,577 was recognized as a reduction in pension expense in the current year.

Experience gains this year created a deferred inflow of resources of $1,512,267 (Division's share $332,699). The combination of unrecognized investment losses this year along with unrecognized net investment gains from prior periods results in a deferred outflow of resources as of December 31, 2015 of $7,522,599 (Division's share $1,654,972). The table below summarizes the current balances of deferred outflows and deferred inflows of resources along with the net recognition over future years. In addition, KUB recorded a deferred outflow of resources of $2,834,692 (Division's share $623,632) at June 30, 2016 for employer contributions made between December 31, 2015 and June 30, 2016.

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ 1,512,267
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	7,522,599	-
Contributions subsequent to measurement date	2,834,692	-
Total	$ 10,357,291	$ 1,512,267

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

Year ended June 30:	
2017	$ 3,938,630
2018	1,103,939
2019	1,103,938
2020	2,698,517
Thereafter	-

11. Defined Contribution Plan

The KUB Asset Accumulation 401(k) Plan (the "401(k) Plan") is a defined contribution 401(k) employee retirement savings plan covering eligible KUB employees established by the KUB Board of Commissioners in accordance with the Charter of the City of Knoxville, Tennessee. The 401(k) Plan's assets are held in trust under an agreement between KUB and Fidelity Management Trust Company. Employees hired prior to January 1, 2011 may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. Employees hired on or after January 1, 2011 have an enhanced 401(k) due to the closure of the Defined Benefit Pension Plan. They may participate and receive a matching contribution of 50 percent of their own contribution up to a maximum match of 3 percent. They also receive a nonelective KUB contribution of from 3 percent to 6 percent, depending on years of service, whether they contribute or not.

Matching contributions were previously remitted to the KUB Pension Plan (a separate defined benefit plan) in the name of the participant for employees hired prior to January 1, 2011. As of December 9, 2015, these Pension match assets moved from the KUB Pension Plan to the 401(k) Plan. Effective December 9, 2015, all matching contributions are remitted to the 401(k) Plan. The match and nonelective contributions for employees hired on or after January 1, 2011 are paid directly by KUB. KUB funded 401(k) matching contributions and nonelective contributions of

$1,739,057 (Division's share $382,593) and $1,593,350 (Division's share $334,604), respectively, for the years ended June 30, 2016 and 2015.

12. Other Post-Employment Benefits (OPEB)

The Governmental Accounting Standards Board (GASB) established standards for the measurement, recognition, and reporting of other post-employment benefits (OPEB). OPEB includes post-employment benefits other than pension, which, for KUB, is presently limited to post-employment health care. GASB Statement No. 45 (Statement No. 45) requires the recognition of the accrued OPEB liability for the respective year, plus the disclosure of the total unfunded liability.

KUB currently provides post-employment health care benefits to 585 former employees and 593 covered dependents. The cost of coverage is shared with retirees and beneficiaries. KUB recognizes its share of the cost of post-employment health care benefits as an expense as claims are paid.

KUB amended its Group Health Plan in 1999, eliminating post-employment health care benefits for all employees hired on or after July 1, 1999. As of June 30, 2016, 356 active employees were eligible for individual and dependent coverage at separation. To qualify, the employee must meet the Rule of 80 (age plus years of service) with a minimum of 20 years of service, and be enrolled in medical coverage on their last day.

In May 2006, the State of Tennessee adopted Tennessee Code Annotated, Title 8, Chapter 50, Part 12 authorizing governmental entities to establish Trusts for the purpose of pre-funding their respective OPEB liabilities.

Although Statement No. 45 does not require pre-funding of the liability, KUB has determined that it is in the long-term economic interest of KUB and its ratepayers to establish a Trust to pre-fund KUB's OPEB liability.

Knoxville Utilities Board Other Post-Employment Benefits Trust (the "Trust") is a single-employer Other Post-Employment Benefits Plan established by the Knoxville Utilities Board (KUB) Board of Commissioners through Resolution No. 1168, as amended, dated October 18, 2007. The applicable documentation was submitted to the State Funding Board and, in December 2007, the State Funding Board approved the Trust. The Trust was also approved by the Internal Revenue Service in June 2008. KUB administers the Trust through a Board of Trustees consisting of seven KUB employees that are appointed by KUB's President and CEO. Any amendments to the Trust involving costs not approved in the operating budget must be approved by KUB's Board of Commissioners, upon recommendation by KUB's President and CEO. All other amendments to the Trust may be approved by KUB's President and CEO upon 60 days notification to the KUB Audit and Finance Committee. The investment of all deposits to the Trust is governed by an Investment Policy, which was adopted by the KUB Board and approved by the State Funding Board.

KUB makes annual contributions to the Trust at an actuarially determined rate. Based on the date of retirement, certain retired plan members are required to contribute specified amounts monthly to maintain health insurance. Those who retired prior to July 1983 have no required monthly premiums for themselves or dependents. The retirees, or their surviving dependents, who retired between August 1983 and January 1998 are required to pay $250 per month for pre-Medicare family health insurance. For individuals who retired after January 1998, the required monthly premium for pre-Medicare health insurance is $250 for single coverage and $500 for family coverage. There is currently no premium for Medicare eligible retirees or dependents.

An actuarial valuation of KUB's Postretirement Benefit Plan was performed for the Trust as of January 1, 2014 for fiscal year June 30, 2015 and January 1, 2015 for fiscal year June 30, 2016. The following table presents the OPEB cost for the year, the amount contributed to the Trust, and changes in the net OPEB obligation for fiscal year ending June 30:

	2016	**2015**
a) Net OPEB Obligation/(Asset) at beginning of fiscal year	$ (174,410)	$ (177,322)
b) Annual Required Contribution (ARC)	953,221	3,497,372
c) Interest on Net OPEB Obligation/(Asset)	(13,081)	(14,186)
d) Adjustment to ARC	(16,427)	(17,098)
e) Annual OPEB Cost **(b+c-d)**	956,567	3,500,284
f) Employer Contributions	953,221	3,497,372
g) Net OPEB Obligation/(Asset) at end of fiscal year **(a+e-f)**	$ (171,064)	$ (174,410)

KUB's annual OPEB cost, the percentage of annual OPEB cost contributed to the Trust, and the net OPEB obligation for fiscal year 2016 and the two preceding years were as follows:

Schedule of Employer Contributions

Actuarial Valuation Date	**Employer Fiscal Year**	**Annual Required Contribution**	**Fiscal Year Actual Contribution**	**Percentage Contributed**	**Net OPEB Obligation**
1/1/2012	6/30/2014	3,327,412	4,057,091	121.93%	(177,322)
1/1/2013	6/30/2015	3,497,372	3,497,372	100.00%	(174,410)
1/1/2014	6/30/2016	953,221	953,221	100.00%	(171,064)

Total contributions to the OPEB Trust for the fiscal year ended June 30, 2016 were $953,221 (Division's share $209,708). The contribution to the Trust was consistent with the annual required contribution, as determined by the Postretirement Benefit Plan's actuarial valuation as of January 1, 2014, which was $953,211 (Division's share $209,708). As of June 30, 2016, the employer's OPEB obligation has been exceeded by $171,064 (Division's share $37,634).

The annual required contribution for the fiscal year ending June 30, 2017, as determined by the Plan's actuarial valuation as of January 1, 2015 is $620,015 (Division's share $136,403).

The actuarial valuation for the Plan as of January 1, 2016 has been completed. The valuation determined that the Plan's actuarial accrued liability was $45,118,624 (Division's share $9,926,097). The actuarial value of the Plan's assets was $48,510,796 (Division's share $10,672,375). As a result, the Plan's unfunded actuarial accrued liability was ($3,392,172) (Division's share ($746,278)). The Plan's actuarial funded ratio was 108 percent. Due to the future implementation of GASB 75, the contributions made for fiscal year ending June 30, 2018 will be the actuarially determined contribution instead of the annual required contribution and the actuarial cost method used to determine the contributions will change from the projected unit credit cost method to the entry age normal cost method. The actuarially determined contribution for fiscal year ending June 30, 2018 will be zero. See Required Supplementary Information for OPEB Schedule of Funding Progress.

The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution and actuarially determined contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

The required schedule of funding progress immediately following the notes to the financial statements presents multi-year trend information about whether the actuarial value of Trust assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point.

Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

Identification of actuarial methods and significant assumptions used to determine the annual required contribution for the fiscal year ending June 30, 2016:

I. Actuarial cost method	Projected unit credit cost method
II. Actuarial value of assets	Smoothed market value with phase-in method using a smoothing period of 5 years
III. Investment return	7.5%, based on the expected portfolio return
Projected salary increases	N/A
Healthcare cost Trend:	
Medicare	2014 - 2030+, ranging from 4.5% to 7.45%
Non-Medicare	2014 - 2030+, ranging from 4.5% to 8.75%
IV. Amortization method	Level dollar closed (30-year)
Remaining amortization period	22 years

The Trust issues a financial report, which includes financial statements and required supplementary information. The report may be obtained by writing the Knoxville Utilities Board Retirement System, P.O. Box 59017, Knoxville, TN 37950-9017.

13. Related Party Transactions

The Division, in the normal course of operations, is involved in transactions with the City of Knoxville and with other divisions of KUB. Such transactions for the years ended June 30, 2016 and 2015 are summarized as follows:

	2016	2015
City of Knoxville		
Amounts billed by the Division for utilities and related services	$ 1,111,067	$ 1,013,354
Payments by the Division in lieu of property tax	3,789,989	3,575,461
Payments by the Division for services provided	1,466,961	1,147,555
Other divisions of KUB		
Amounts billed to other divisions for utilities and related services provided	290,250	285,944
Interdivisional rental expense	306,304	306,769
Interdivisional rental income	114,197	96,075
Amounts billed to the Division by other divisions for utilities services provided	2,911,300	3,002,595

With respect to these transactions, accounts receivable from the City of Knoxville included in the balance sheet at year end were:

	2016	2015
Accounts receivable	$ 28,514	$ 29,056

14. Other Commitments and Contingencies

In the normal course of business, there are various lawsuits pending against KUB. Management has reviewed these lawsuits with counsel, who is vigorously defending KUB's position and is of the opinion that the ultimate disposition of these matters will not have a material adverse effect on KUB's financial position, results of operations or cash flows.

In February 2005, a Consent Decree was entered into federal court regarding the operation of KUB’s wastewater system. Under the terms of the Consent Decree, the remediation of identified sanitary sewer overflows (SSOs) on KUB’s wastewater system had to be completed by June 30, 2016. KUB completed all the requirements of the Consent Decree for the collection system two years in advance of the deadline.

The Consent Decree also required KUB to perform an evaluation of the wet weather performance and capacity of its wastewater treatment plants. In July 2007, KUB submitted a Composite Correction Plan (CCP) for its wastewater treatment plants to EPA for review. The development and filing of the CCP was a requirement of the federal order of February 2005. The CCP includes recommended improvements to KUB’s Kuwahee and Fourth Creek treatment plants to address wet weather capacity issues noted in prior assessments. The EPA approved the CCP in January 2009 including a recommended schedule of plant improvements that extends beyond the expiration date of the original Consent Decree. An amendment to the Consent Decree incorporating and establishing this schedule was agreed to by all parties and was entered on June 23, 2009. The purpose of the Amendment is to allow KUB to complete a portion of work outlined in the CCP after the Consent Decree deadline of June 30, 2016. The CCP provides for a biologically enhanced high-rate clarification (the BEHRC) secondary treatment system to be installed at the Fourth Creek treatment plant by June 30, 2018 and at the Kuwahee treatment plant by June 30, 2021. The total cost of such improvements is estimated to be approximately $120 million.

KUB's funding plan for the Consent Decree includes long-term bonds and a series of rate increases phased in over the term of the order. Bond proceeds fund all types of wastewater capital projects, the majority of which are related to the Consent Decree. As of June 30, 2016, the Wastewater Division had issued $485 million in bonds to fund system capital improvements since the inception of the Consent Decree. The Board previously approved two 50 percent rate increases, which went into effect in April 2005 and January 2007. The Board also approved an 8 percent rate increase, which was effective in September 2008, two 12 percent rate increases, which were effective in April 2011 and October 2012, and three 6 percent rate increases effective October 2014, October 2015 and October 2016. KUB anticipates additional bond issues and rate increases over the next decade to help fund wastewater capital improvements.

KUB successfully completed the first cycle of Maintenance Operation Management (MOM) requirements one year before the deadline by inspecting 99.5% of manholes and gravity mains, smoke testing 99.9% of gravity mains, performing required inspections of pump stations and the related force mains, and completing all Corrective Action Plan/Engineering Report (CAP/ER) projects. KUB initiated the second MOM cycle that continues to focus on the prevention of SSOs. As part of the Century II initiative, formally known as the PACE10 program, KUB has installed storage tanks providing 34 million gallons of wastewater storage to control wet weather overflows and rehabilitated or replaced approximately 334.9 miles of collection system pipe. KUB also continues to maintain a proactive operations and maintenance plan for the wastewater collection system including inspection, grease control, and private lateral enforcement. The result of the Pace10/Century II initiative has been an 82 percent reduction in SSOs.

As of June 30, 2016, the Wastewater Division had completed its twelfth full year under the Consent Decree, spending $529.5 million on capital investments to meet Consent Decree requirements. During fiscal year 2016, the Wastewater Division incurred $37.3 million in total expenditures related to Consent Decree requirements, including $3.3 million for operating costs and $34 million in capital improvements which included the rehabilitation or replacement of 28 miles of wastewater main. During the fiscal year, $26.5 million was spent on sewer mini-basin rehabilitation and replacement. Trunk line rehabilitation and replacement accounted for $2 million of capital expenditures, while pump station improvements accounted for $4.6 million.

Knoxville Utilities Board Wastewater Division
Required Supplementary Information – Schedule of Funding Progress
June 30, 2016
(Unaudited)

Other Post-Employment Benefits (OPEB)

	Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a)/(b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b)-(a)]/(c)
	January 1, 2008	$ -	$ 108,329,141	$ 108,329,141	0%	$ 31,234,509	346.8%
	January 1, 2009	14,593,487	100,726,738	86,133,251	14%	31,846,091	270.5%
	January 1, 2010	21,275,643	58,475,364	37,199,721	36%	30,069,028	123.7%
	January 1, 2011	40,749,815	64,289,254	23,539,439	63%	28,878,791	81.5%
	January 1, 2012	37,907,357	61,603,466	23,696,109	62%	28,269,123	83.8%
	January 1, 2013	38,571,803	63,341,531	24,769,728	61%	27,566,340	89.9%
	January 1, 2014	43,409,955	46,889,808	3,479,853	93%	26,724,154	13.0%
*	January 1, 2015	47,705,478	47,745,640	40,162	100%	25,816,884	0.2%
*	January 1, 2016	48,510,796	45,118,624	(3,392,172)	108%	25,243,127	(13.4%)

***** The actuarial valuations dated January 1, 2015 and 2016, which determine the annual required contribution for future fiscal years ending June 30, 2017 and 2018, have not been audited.

Knoxville Utilities Board Wastewater Division
Required Supplementary Information – Schedule of Changes in Net Pension Liability and Related Ratios
June 30, 2016
(Unaudited)

	Year ended December 31	
	2015	**2014**
Total pension liability		
Service cost	$ 4,157,062	$ 4,092,808
Interest	14,812,784	14,698,657
Differences between expected and actual experience	(1,890,334)	-
Benefit payments, including refunds of member contributions	(15,350,926)	(15,533,167)
Net change in total pension liability	1,728,586	3,258,298
Total pension liability - beginning	202,773,764	199,515,466
Total pension liability - ending (a)	$ 204,502,350	$ 202,773,764
Plan fiduciary net position		
Contributions - employer	$ 5,991,887	$ 5,908,541
Contributions - participants	487,546	475,854
Net investment income	(95,430)	22,292,369
Other additions	30,879	29,733
Benefit payments, including refunds of member contributions	(15,274,926)	(15,405,167)
Administrative expense	(397,160)	(378,085)
Death benefits	(76,000)	(128,000)
Net change in plan fiduciary net position**	(9,333,204)	12,795,245
Plan fiduciary net position - beginning**	208,795,394	196,000,149
Plan fiduciary net position - ending (b)**	$ 199,462,190	$ 208,795,394
Plan's net pension liability - ending (a) - (b)	$ 5,040,160	$ (6,021,630)
Plan fiduciary net position as a percentage of the total pension liability	97.54%	102.97%
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Plan's net pension liability as a percentage of covered-employee payroll	9.95%	(11.98%)

Notes to Schedule:

* Information not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented in 2014.

** Excludes amounts related to 401(k) matching contributions.

Knoxville Utilities Board Wastewater Division

Required Supplementary Information – Schedule of Employer Pension Contributions

June 30, 2016

(Unaudited)

	Year ended December 31 2015	 2014
Annual required contribution	$ 5,991,887	$ 5,908,541
Contribution in relation to the annual required contribution	5,991,887	5,908,541
Contribution deficiency	$ -	$ -
Covered-employee payroll	$ 50,679,585	$ 50,246,074
Contributions as a percentage of covered-employee payroll	11.82%	11.76%

Notes to Schedule:

Valuation Dates:	January 1, 2013 and January 1, 2014
Timing:	Actuarially determined contributions for a plan year are based upon 50% of the amounts determined at the actuarial valuations for each of the two prior plan years.

Key methods and assumptions used to determine contribution rates:

Actuarial cost method:	Individual entry age
Asset valuation method:	5-year smoothed market
Amortization method:	Level dollar closed period with 28 years remaining as of January 1, 2013 and 27 years remaining as of January 1, 2014.
Discount rate:	8% at January 1, 2013 and 7.5% at January 1, 2014
Salary increases:	From 2.58% to 7.92% for January 1, 2013 and from 2.8% to 5.15% for January 1, 2014, based on years of service
Mortality:	Sex distinct RP-2000 Combined Mortality projected to 2018 using Scale AA for the Janaury 1, 2013 valuation. Sex distinct RP-2000 Combined Mortality projected to 2024 using Scale AA for the January 1, 2014 valuation.
Inflation:	2.8 percent

* Schedule of Employer Contribution information is not reflected prior to 2014 due to changes in actuary methodologies required under GASB 67, which was implemented 2014.

Knoxville Utilities Board Wastewater Division

Supplemental Information - Schedule of Insurance in Force

June 30, 2016

(Unaudited) Schedule 1

Insurance coverage is for KUB as a consolidated entity.

Crime

Covers losses resulting from employee dishonesty, robbery, burglary, and computer fraud. Limits of coverage - $5,000,000; $250,000 retention.

Directors' and Officers' Liability Insurance

Covers KUB personnel appropriately authorized to make decisions on behalf of KUB (including but not limited to Commissioners, President and CEO, Senior Vice Presidents, Vice Presidents, and Directors) for wrongful acts. Limits of coverage - $20,000,000; $1,000,000 corporate deductible, $0 individual deductible.

Employment Practices Liability

Coverage for costs related to actual or alleged employment practices violations for amounts exceeding specified amount ($500,000). Limits of coverage - $10,000,000.

Fiduciary

Covers losses resulting from wrongful acts related to KUB's Pension, 401(k), and OPEB Trust funds. Limits of coverage - $10,000,000; $150,000 deductible.

Pollution Legal Liability

New conditions coverage for losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - $20,000,000.

Property Insurance

This coverage provides protection of KUB's property for fire, extended coverage, vandalism and malicious mischief, and coverage on boilers and machinery. Also included are flood and earthquake damage and mechanical failure. Limits of coverage - $250,000,000 per occurrence (subject to certain sublimits); $2,500,000 deductible per occurrence.

Travel Accident

Covers losses related to employees' business travel. Limits of coverage - $1,500,000 aggregate.

Excess Insurance for General Liability

As a government entity, KUB's liability is limited under the Tennessee Governmental Tort Liability Act (TCA §29-20-403). KUB is self-insured for up to the first $700,000 of any accident and has insurance of $1,000,000 above this retention.

Excess Insurance for Workers' Compensation

Covers all losses exceeding specified amount per occurrence ($1,000,000). Limits of coverage - Statutory; stop loss coverage applies for aggregate losses over $5,000,000.

Employee Health Plan Stop Loss Coverage

KUB's employee health plan is self-funded. KUB has purchased stop loss insurance, which covers KUB's exposure to annual expenses in excess of $400,000 per individual participant.

Knoxville Utilities Board Wastewater Division

Supplemental Information – Schedule of Debt Maturities by Fiscal Year

June 30, 2016

(Unaudited)

Schedule 2

Continued on Next Page

	2005B		2008		2010			2010C			2012A	
FY	**Principal**	**Interest**	**Principal**	**Interest**	**Principal**	**Interest**	**Rebate***	**Principal**	**Interest**	**Rebate***	**Principal**	**Interest**
16-17	1,470,000	620,185	4,600,000	327,500		1,910,000	668,500	1,400,000	3,634,545	1,272,090	840,000	551,425
17-18	1,525,000	561,385	1,950,000	97,500		1,910,000	668,500	1,500,000	3,584,425	1,254,548	985,000	528,325
18-19	1,595,000	498,860				1,910,000	668,500	1,550,000	3,525,625	1,233,968	970,000	498,775
19-20	1,655,000	433,066				1,910,000	668,500	1,600,000	3,460,990	1,211,346	950,000	467,250
20-21	1,725,000	363,556				1,910,000	668,500	1,650,000	3,394,270	1,187,994	1,085,000	434,000
21-22	1,800,000	290,244				1,910,000	668,500	1,700,000	3,325,465	1,163,912	1,175,000	390,600
22-23	1,880,000	212,844				1,910,000	668,500	1,750,000	3,246,925	1,136,424	1,165,000	343,600
23-24	695,000	130,594				1,910,000	668,500	1,850,000	3,162,575	1,106,902	1,250,000	297,000
24-25	730,000	100,188				1,910,000	668,500	1,950,000	3,065,450	1,072,908	1,140,000	247,000
25-26	765,000	68,250				1,910,000	668,500	2,375,000	2,961,125	1,036,394	1,190,000	201,400
26-27	795,000	34,781				1,910,000	668,500	2,500,000	2,830,738	990,758	1,235,000	153,800
27-28						1,910,000	668,500	2,600,000	2,688,488	940,970	1,280,000	104,400
28-29						1,910,000	668,500	2,725,000	2,536,388	887,736	1,330,000	53,200
29-30						1,910,000	668,500	2,850,000	2,376,975	831,942		
30-31						1,910,000	668,500	2,975,000	2,210,250	773,588		
31-32						1,910,000	668,500	3,100,000	2,031,750	711,112		
32-33						1,910,000	668,500	3,250,000	1,845,750	646,012		
33-34						1,910,000	668,500	3,375,000	1,650,750	577,762		
34-35						1,910,000	668,500	3,550,000	1,448,250	506,882		
35-36						1,910,000	668,500	3,700,000	1,235,250	432,338		
36-37						1,910,000	668,500	3,875,000	1,009,550	353,342		
37-38						1,910,000	668,500	4,050,000	773,175	270,612		
38-39						1,910,000	668,500	4,225,000	526,125	184,144		
39-40						1,910,000	668,500	4,400,000	268,400	93,940		
40-41						1,910,000	668,500					
41-42						1,910,000	668,500					
42-43					10,000,000	1,910,000	668,500					
43-44					10,000,000	1,260,000	441,000					
44-45					10,000,000	630,000	220,500					
45-46												
46-47												
47-48												
48-49												
49-50												
Total	$ 14,635,000	$ 3,313,953	$ 6,550,000	$ 425,000	$ 30,000,000	$ 53,460,000	$ 18,711,000	$ 64,500,000	$ 56,793,234	$ 19,877,624	$ 14,595,000	$ 4,270,775

*Series 2010 and 2010c bonds were issued as federally taxable Build America Bonds. KUB will receive a 35 percent interest rebate payment from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8% reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change.

Knoxville Utilities Board Wastewater Division
Supplemental Information – Schedule of Debt Maturities by Fiscal Year
June 30, 2016
(Unaudited)

Schedule 2

Continued from Previous Page

	2012B		2013A		2014A		2015A		2015B		TOTALS		Grand Total (P + I)	Grand Total (Less Rebates)
FY	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest		
16-17	975,000	1,916,563	620,000	3,551,100	450,000	1,086,119	125,000	5,115,762	450,000	1,141,938	10,930,000	19,855,137	30,785,137	28,844,547
17-18	1,000,000	1,904,375	635,000	3,538,700	475,000	1,077,119	2,835,000	5,109,512	475,000	1,128,438	11,380,000	19,439,779	30,819,779	28,896,731
18-19	1,050,000	1,891,871	660,000	3,513,300	475,000	1,058,119	5,010,000	4,967,762	500,000	1,104,688	11,810,000	18,969,000	30,779,000	28,876,532
19-20	1,100,000	1,878,750	685,000	3,486,900	500,000	1,039,119	5,305,000	4,717,262	525,000	1,079,688	12,320,000	18,473,025	30,793,025	28,913,179
20-21	1,150,000	1,862,250	710,000	3,459,500	525,000	1,019,119	5,460,000	4,452,012	525,000	1,063,938	12,830,000	17,958,645	30,788,645	28,932,151
21-22	1,200,000	1,804,750	740,000	3,431,100	550,000	998,119	5,675,000	4,179,012	550,000	1,042,938	13,390,000	17,372,228	30,762,228	28,929,816
22-23	1,250,000	1,744,750	770,000	3,401,500	575,000	981,619	6,005,000	3,895,262	575,000	1,020,936	13,970,000	16,757,436	30,727,436	28,922,512
23-24	1,300,000	1,694,750	4,600,000	3,370,700	600,000	964,369	3,720,000	3,595,012	600,000	997,938	14,615,000	16,122,938	30,737,938	28,962,536
24-25	1,375,000	1,642,750	4,900,000	3,232,700	625,000	946,369	3,785,000	3,483,412	625,000	973,938	15,130,000	15,601,807	30,731,807	28,990,399
25-26	1,425,000	1,587,750	5,040,000	3,085,700	650,000	927,619	1,425,000	3,369,864	650,000	955,188	13,520,000	15,066,896	28,586,896	26,882,002
26-27	1,500,000	1,530,750	5,200,000	2,934,500	700,000	908,119	1,490,000	3,323,550	675,000	935,688	14,095,000	14,561,926	28,656,926	26,997,668
27-28	1,575,000	1,470,750	6,305,000	2,778,500	725,000	880,119	1,405,000	3,271,400	700,000	915,438	14,590,000	14,019,095	28,609,095	26,999,625
28-29	1,625,000	1,423,500	6,535,000	2,573,588	750,000	851,119	1,450,000	3,222,226	725,000	887,438	15,140,000	13,457,459	28,597,459	27,041,223
29-30	1,700,000	1,374,750	8,315,000	2,377,538	775,000	821,119	1,455,000	3,178,726	775,000	858,438	15,870,000	12,897,546	28,767,546	27,267,104
30-31	1,775,000	1,323,750	8,550,000	2,128,088	825,000	790,119	1,515,000	3,135,076	800,000	827,436	16,440,000	12,324,719	28,764,719	27,322,631
31-32	1,875,000	1,270,500	8,840,000	1,871,588	850,000	757,119	1,520,000	3,089,626	825,000	795,436	17,010,000	11,726,019	28,736,019	27,356,407
32-33	1,950,000	1,214,250	9,120,000	1,606,388	900,000	723,119	1,580,000	3,042,125	850,000	762,436	17,650,000	11,104,068	28,754,068	27,439,556
33-34	2,025,000	1,155,750	9,390,000	1,332,788	925,000	687,119	1,635,000	2,992,750	900,000	733,750	18,250,000	10,462,907	28,712,907	27,466,645
34-35	2,125,000	1,095,000	9,705,000	1,015,875	975,000	650,119	1,690,000	2,939,612	925,000	703,375	18,970,000	9,762,231	28,732,231	27,556,849
35-36	2,225,000	1,031,250	10,025,000	688,331	1,025,000	611,119	1,750,000	2,884,688	975,000	671,000	19,700,000	9,031,638	28,731,638	27,630,800
36-37	2,325,000	964,500	10,370,000	349,988	1,075,000	570,119	1,825,000	2,827,812	1,000,000	632,000	20,470,000	8,263,969	28,733,969	27,712,127
37-38	2,425,000	894,750			500,000	527,119	13,420,000	2,768,500	500,000	592,000	20,895,000	7,465,544	28,360,544	27,421,432
38-39	2,550,000	822,000			500,000	507,119	13,895,000	2,298,800	500,000	572,000	21,670,000	6,636,044	28,306,044	27,453,400
39-40	2,650,000	745,500			500,000	488,994	14,480,000	1,743,000	500,000	552,000	22,530,000	5,707,894	28,237,894	27,475,454
40-41	2,775,000	666,000			1,175,000	470,869	15,130,000	1,236,200	1,100,000	532,000	20,180,000	4,815,069	24,995,069	24,326,569
41-42	2,900,000	582,750			1,225,000	428,275	15,775,000	631,000	1,150,000	488,000	21,050,000	4,040,025	25,090,025	24,421,525
42-43	3,025,000	495,750			1,300,000	382,950			1,200,000	442,000	15,525,000	3,230,700	18,755,700	18,087,200
43-44	3,150,000	405,000			1,350,000	334,850			1,250,000	394,000	15,750,000	2,393,850	18,143,850	17,702,850
44-45	3,300,000	310,500			1,400,000	284,900			1,300,000	344,000	16,000,000	1,569,400	17,569,400	17,348,900
45-46	3,450,000	211,500			1,475,000	233,100			1,350,000	292,000	6,275,000	736,600	7,011,600	7,011,600
46-47	3,600,000	108,000			1,550,000	178,525			1,400,000	238,000	6,550,000	524,525	7,074,525	7,074,525
47-48					1,600,000	121,175			1,450,000	182,000	3,050,000	303,175	3,353,175	3,353,175
48-49					1,675,000	61,975			1,525,000	124,000	3,200,000	185,975	3,385,975	3,385,975
49-50									1,575,000	63,000	1,575,000	63,000	1,638,000	1,638,000
Total	$ 62,350,000	$ 37,025,059	$ 111,715,000	$ 53,728,372	$ 29,200,000	$ 22,366,850	$ 129,360,000	$ 85,469,963	$ 29,425,000	$ 24,047,063	$ 492,330,000	$ 340,900,269	$ 833,230,269	$ 794,641,645

*Series 2010 and 2010c bonds were issued as federally taxable Build America Bonds. KUB will receive a 35 percent interest rebate payment from the United States Government for each interest payment. Effective October 1, 2015 these bonds became subject to a 6.8% reduction in rebate payment amounts due to the United States Government sequestration. The sequestration is effective until intervening Congressional action, at which time the sequestration rate is subject to change.

Knoxville Utilities Board Wastewater Division
Supplemental Information – Schedule of Current Rates in Force
June 30, 2016
(Unaudited)

Schedule 3

Rate Class	Base Charge	Number of Customers
Residential Inside City rate	For wastewater service furnished to premises entirely within the corporate limits of the City of Knoxville:	54,767

Commodity Charge

First	2	100 Cubic Feet Per Month at $0.70 Per 100 Cubic Feet
Over	2	100 Cubic Feet Per Month at $8.70 Per 100 Cubic Feet

Additional Monthly Customer Charge

5/8" meter	$ 26.00
1" meter	41.00
1 1/2" meter	53.00
2" meter	73.00

Rate Class	Base Charge	Number of Customers
Non-Residential Inside City rate	For wastewater service furnished to premises entirely within the corporate limits of the City of Knoxville:	8,441

Commodity Charge

First	2	100 Cubic Feet Per Month at $0.80 Per 100 Cubic Feet
Next	8	100 Cubic Feet Per Month at $10.45 Per 100 Cubic Feet
Next	90	100 Cubic Feet Per Month at $9.35 Per 100 Cubic Feet
Next	300	100 Cubic Feet Per Month at $8.00 Per 100 Cubic Feet
Next	4,600	100 Cubic Feet Per Month at $6.50 Per 100 Cubic Feet
Next	5,000	100 Cubic Feet Per Month at $4.30 Per 100 Cubic Feet

Knoxville Utilities Board Wastewater Division
Supplemental Information – Schedule of Current Rates in Force
June 30, 2016
(Unaudited)

Additional Monthly Customer Charge

5/8" meter	$ 26.00
1" meter	41.00
1 1/2" meter	53.00
2" meter	73.00
3" meter	130.00
4" meter	212.00
6" meter	453.00
8" meter	787.00
10" meter	1,193.00
12" meter	1,757.00

Knoxville Utilities Board Wastewater Division

Supplemental Information – Schedule of Current Rates in Force

June 30, 2016

(Unaudited)

Schedule 3

Rate Class	Base Charge	Number of Customers
Residential Outside City rate	For wastewater service furnished to premises entirely or partly outside the corporate limits of the City of Knoxville:	7,670

Commodity Charge

First	2	100 Cubic Feet Per Month at $0.85 Per 100 Cubic Feet
Over	2	100 Cubic Feet Per Month at $9.30 Per 100 Cubic Feet

Additional Monthly Customer Charge

5/8" meter	$	30.00
1" meter		44.00
1 1/2" meter		61.00
2" meter		81.00

Rate Class	Base Charge	Number of Customers
Non-Residential Outside City rate	For wastewater service furnished to premises entirely or partly outside the corporate limits of the City of Knoxville:	507

Commodity Charge

First	2	100 Cubic Feet Per Month at $0.95 Per 100 Cubic Feet
Next	8	100 Cubic Feet Per Month at $11.55 Per 100 Cubic Feet
Next	90	100 Cubic Feet Per Month at $10.25 Per 100 Cubic Feet
Next	300	100 Cubic Feet Per Month at $8.75 Per 100 Cubic Feet
Next	4,600	100 Cubic Feet Per Month at $7.30 Per 100 Cubic Feet
Next	5,000	100 Cubic Feet Per Month at $4.80 Per 100 Cubic Feet

Knoxville Utilities Board Wastewater Division

Supplemental Information – Schedule of Current Rates in Force

June 30, 2016

(Unaudited)

Schedule 3

Additional Monthly Customer Charge

5/8" meter	$ 30.00
1" meter	44.00
1 1/2" meter	61.00
2" meter	81.00
3" meter	147.00
4" meter	235.00
6" meter	497.00
8" meter	866.00
10" meter	1,308.00
12" meter	1,930.00

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

Board of Commissioners
Wastewater Division of the Knoxville Utilities Board
Knoxville, Tennessee

Report on the Financial Statements

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Wastewater Division (the Division) of the Knoxville Utilities Board, a component unit of the City of Knoxville, Tennessee, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Division's basic financial statements, and have issued our report thereon dated October 27, 2016.

Internal Control over Financial Reporting

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

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

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

Board of Commissioners
Wastewater Division of the Knoxville Utilities Board
Knoxville, Tennessee

Compliance and Other Matters

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

Purpose of Report

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

Coulter & Justus, P.C.

Knoxville, Tennessee
October 27, 2016