

In the opinion of Bond Counsel, interest on the Bonds is not excludable from gross income for federal income tax purposes. See “TAX MATTERS” herein.



\$76,775,000
CITY OF TACOMA, WASHINGTON
Water System Revenue Bonds, 2009
(Taxable Build America Bonds – Direct Payment)

DATED: Date of Delivery

DUE: December 1, as shown below

The City of Tacoma, Washington (the “City”), Water System Revenue Bonds, 2009 (Taxable Build America Bonds – Direct Payment) (the “Bonds”), will be issued only as fully registered bonds under a book entry system, initially registered in the name of Cede & Co., as nominee for The Depository Trust Company (“DTC”), New York, New York, which will act as securities depository for the Bonds. Individual purchases of the Bonds will be made in the principal amount of \$5,000 each or any integral multiple thereof within a single maturity. Purchasers of the Bonds will not receive certificates representing their interest in the Bonds.

Both principal of and interest on the Bonds shall be payable in lawful money of the United States of America. Interest on the Bonds, payable each June 1 and December 1, commencing June 1, 2010, and principal of the Bonds are payable by the Bond Registrar (currently The Bank of New York Mellon, New York, New York) to DTC, which is obligated to remit such principal and interest to its broker-dealer Participants for subsequent disbursement to Beneficial Owners of the Bonds. See Appendix B—“BOOK-ENTRY SYSTEM.”

Maturity Schedule, Interest Rate, Price and Cusip Number

\$76,775,000 5.751% Term Bonds due December 1, 2039 @ 100%; CUSIP No.: 873547GW7

The Bonds are subject to redemption by the City prior to their stated maturities as described herein under “DESCRIPTION OF THE BONDS—Optional Redemption,” “—Mandatory Redemption” and “—Extraordinary Optional Redemption.”

The Bonds are being issued to finance capital improvements to the Water System, to provide a debt service reserve fund for the Bonds, and to pay costs of issuance. See “PURPOSE AND APPLICATION OF BOND PROCEEDS.”

The Bonds are payable solely from a special fund of the City known as the Water Revenue Bond Fund, and from the Net Revenue of the Water System pledged thereto on a parity with \$111,100,000 outstanding Water System revenue bonds and bonds hereafter issued on a parity therewith. See “SECURITY FOR THE BONDS” herein. The City has outstanding \$79,150,000 principal amount of Regional Water Supply System Revenue Bonds, 2002 (the “Regional System Bonds”), of which Tacoma Water is responsible for paying approximately 55% of the debt service as a Contract Resource Obligation payable from Gross Revenue of the Water System as an Operation and Maintenance Expense of the Water System. See “WATER SYSTEM—The Second Supply Project” and “SECURITY FOR THE BONDS.” The Bonds are not general obligations of the City, and neither the full faith and credit nor the taxing power of the City or of the State of Washington, nor any revenues of the City derived from sources other than the Water System, are pledged to the payment thereof.

This cover page includes certain information for reference only and is not a summary of matters set forth herein. Investors should read the entire Official Statement to obtain information essential to the making of an informed investment decision.

The Bonds are offered for delivery when, as, and if issued, subject to the approval of legality by Foster Pepper PLLC, Bond Counsel, Seattle, Washington. Certain legal matters will be passed upon for the Underwriter by K&L Gates LLP, Seattle, Washington. It is expected that the Bonds will be available for delivery at the facilities of The Depository Trust Company in New York, New York, by Fast Automated Securities Transfer (FAST) on or about November 4, 2009.

This Official Statement is provided by the City and not by the Underwriter of the Bonds. No dealer, broker, salesperson, or other person has been authorized to give any information or to make any representations other than those contained in this Official Statement in connection with the offering of the Bonds and, if given or made, such other information or representations must not be relied upon as having been authorized by any of the foregoing. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of the Bonds by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale.

Any statement made in this Official Statement involving any forecast or matter of estimates or opinion, whether or not expressly so stated, is intended solely as such and not as a representation of fact. The achievement of certain results or other expectations contained in such forward looking statements involves known and unknown risks, uncertainties, and other factors that may cause actual results, performance, or achievements described to be materially different from any future results, performance, or achievements expressed or implied by such forward looking statements. The City does not plan to issue any updates or revisions to those forward looking statements if and when its expectations or events, conditions, or circumstances on which such statements are based occur.

The information set forth herein has been obtained from the City and from other sources that are believed to be reliable, but it is not guaranteed as to accuracy or completeness. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale of the Bonds shall, under any circumstances, create any implication that there has been no change in the affairs of the City since the date hereof.

The CUSIP number provided in this Official Statement are included for convenience of the holders and potential holders of the Bonds. No assurance can be given that the CUSIP number for the Bonds will remain the same after the date of issuance and delivery of the Bonds.

The Underwriter has provided the following sentence for inclusion in this Official Statement. The Underwriter has reviewed the information in this Official Statement in accordance with, and as a part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information.

This Official Statement is not to be construed as a contract or agreement between the City and purchasers or owners of any of the Bonds.

The initial public offering price or yield set forth on the cover page hereof may be changed from time to time by the Underwriter. The Underwriter may offer and sell the Bonds to certain dealers, unit investment trusts or money market funds at prices lower than the public offering price stated on the cover page hereof.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITER MAY OVERALLOT OR EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICE OF THE BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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OFFICIAL STATEMENT

CITY OF TACOMA, WASHINGTON

\$76,775,000

Water System Revenue Bonds, 2009 (Taxable Build America Bonds – Direct Payment)

INTRODUCTION

The City of Tacoma, Washington (the “City” or “Tacoma”), a municipal corporation duly organized and existing under the laws of the State of Washington, furnishes this Official Statement in connection with the offering of \$76,775,000 principal amount of its Water System Revenue Bonds, 2009 (Taxable Build America Bonds – Direct Payment) (the “Bonds”). This Official Statement, which includes the cover page and appendices, provides information concerning the City, the Bonds, the City’s Water System (the “Water System”), and the City’s obligations with respect to the Second Supply Project.

The City is a municipal corporation under the constitution and laws of the State of Washington. The Water Division, doing business as Tacoma Water (“Tacoma Water”), of the City’s Department of Public Utilities (the “Department”) operates the Water System. Tacoma Water is one of the largest publicly owned water utilities in the Pacific Northwest and had 95,858 customers in 2008. See “THE WATER SYSTEM.”

The Bonds are issued pursuant to Substitute Ordinance No. 27837, passed by the Council on October 13, 2009, and Substitute Resolution No. 37890, adopted by the Council on October 20, 2009 (collectively, the “Bond Ordinance”), and under the authority of chapters 35.41 and 39.46 of the Revised Code of Washington (“RCW”). Certain provisions of the Bond Ordinance are summarized in Appendix A.

The Water System has outstanding \$30,460,000 principal amount of Water System Revenue Bonds, 2001 (the “2001 Bonds”), \$37,830,000 principal amount of Water System Revenue and Refunding Bonds, 2003 (the “2003 Bonds”), and \$42,810,000 principal amount of Water System Revenue and Refunding Bonds, 2005 (the “2005 Bonds”) (collectively the “Outstanding Parity Bonds”). The Bonds are issued on a parity with the Outstanding Parity Bonds. The Bonds, the Outstanding Parity Bonds, and any Future Parity Bonds are referred to as the “Parity Bonds.”

The City has outstanding \$79,150,000 principal amount of Regional Water Supply System Revenue Bonds, 2002 (the “Second Supply System Bonds”), of which Tacoma Water is responsible for paying approximately 55% of the debt service as a Contract Resource Obligation, payable as an Operation and Maintenance Expense from Gross Revenue of the Water System senior to the payment of debt service on the Parity Bonds. See “WATER SYSTEM—The Second Supply Project” and “SECURITY FOR THE BONDS—Additional Obligations—*Contract Resource Obligations*.”

The City has pledged in the Bond Ordinance that it will not issue any indebtedness which is secured by a lien on the Net Revenue of the Water System that is superior to the lien of the Parity Bonds. However, the City reserves the right under certain conditions to enter into additional Contract Resource Obligations, or issue additional debt of the Second Supply Project, under which amounts due are payable as Operation and Maintenance Expenses of the Water System. See “SECURITY FOR THE BONDS—Additional Obligations—*Contract Resource Obligations*.” The City reserves the right in the Bond Ordinance to issue additional bonds on a parity with the Parity Bonds (“Future Parity Bonds”). See “SECURITY FOR THE BONDS—Additional Obligations—*Future Parity Bonds*.”

The Bonds are being issued to provide funds to pay for certain capital improvements to the Water System, to provide a debt service reserve for the Bonds, and to pay the costs of issuance of the Bonds, as more fully described under “PURPOSE AND APPLICATION OF BOND PROCEEDS” herein.

In the preparation of the projections in this Official Statement, the City has made certain assumptions with respect to conditions that may occur in the future. While the City believes these assumptions are reasonable for the purpose of the projections, they are dependent upon future events, and actual conditions may differ from those assumed. To the extent actual future factors differ from those assumed or provided to the City by others, the actual results will vary from those forecast.

Certain capitalized words and phrases used in this Official Statement not defined herein have the meanings given in the Bond Ordinance, unless the context shall clearly indicate that another meaning is intended. See Appendix A for certain definitions.

DESCRIPTION OF THE BONDS

General

The Bonds will be dated the date of their delivery and will be issued in the principal amount of \$76,775,000. The Bonds will bear interest at the rate and mature on the date set forth on the cover page of this Official Statement. Interest on the Bonds shall be calculated on the basis of a 360 day year consisting of twelve 30 day months, and shall be payable each June 1 and December 1, commencing June 1, 2010.

The Bonds will be issued only as fully registered bonds under a book entry system, initially registered in the name of Cede & Co., as nominee for DTC, which will act as securities depository for the Bonds. Individual purchases of the Bonds will be made in the principal amount of \$5,000 each or any integral multiple thereof within a single maturity. Both principal of and interest on the Bonds shall be payable in lawful money of the United States of America. The fiscal agency of the State of Washington in New York, New York (currently The Bank of New York Mellon) will act as Bond Registrar for the Bonds. Purchasers will not receive certificates representing their interest in the Bonds. See Appendix B—"BOOK-ENTRY SYSTEM."

Designation of the Bonds as "Build America Bonds"

The City has made irrevocable elections to have Section 54AA of the Code apply to the Bonds so that the Bonds are treated as "Build America Bonds," and further to have Subsection 54AA(g) of the Code apply to the Bonds so that the Bonds are treated as "qualified bonds" with respect to which the City will be allowed a credit payable by the United States Treasury to the City pursuant to Section 6431 of the Code in an amount equal to 35% of the interest payable on the Bonds on each interest payment date. As a result of these elections, interest on the Bonds is not excludable from gross income of owners of the Bonds for federal income tax purposes, and owners of the Bonds will not be allowed any federal tax credits as a result of ownership of or receipt of interest payments on the Bonds. See "TAX MATTERS" herein. The obligation of the United States Treasury under Section 6431 of the Code to make direct payments to the City in respect of interest payments on the Bonds does not constitute a full faith and credit guarantee of the Bonds by the United States of America.

The City has authorized the Director of Finance to take such actions as are necessary or appropriate for the City to receive from the United States Treasury the applicable federal credit payments in respect of the Bonds, such as the timely filing with the Internal Revenue Service of Form 8038-CP – "Return for Credit Payments to Issuers of Qualified Bonds" in the manner prescribed by Internal Revenue Service Notice 2009-26. The City also has covenanted in the Bond Ordinance that it will not take or permit to be taken on its behalf any action that would adversely affect the entitlement of the City to receive from the United States Treasury the applicable federal credit payments in respect of any bonds, including the Bonds, sold and issued as Build America Bonds. Without limiting the generality of the foregoing, the City has covenanted to comply with the provisions of the Code compliance with which would result in the interest on such Bonds being excluded from gross income for federal tax purposes but for an irrevocable election to have Section 54AA of the Code apply to the Bonds.

Optional Redemption

The Bonds are subject to optional redemption by the City prior to their stated maturity date, in whole or in part (and if in part, pro rata), on any business day, at the “Make-Whole Redemption Price,” plus accrued and unpaid interest on the Parity Bonds to be redeemed on the date fixed for redemption.

The “Make-Whole Redemption Price” is the greater of (i) 100% of the principal amount of the Bonds to be redeemed and (ii) the sum of the present value of the remaining scheduled payments of principal and interest on the Bonds to be redeemed, not including any portion of those payments of interest accrued and unpaid as of the date on which such Bonds are to be redeemed, discounted to the date on which the Bonds are to be redeemed on a semi-annual basis, assuming a 360-day year consisting of twelve 30-day months, at the “Treasury Rate” (defined below) plus 30 basis points.

“Treasury Rate” means, with respect to any redemption date for a particular Bond, the rate per annum, expressed as a percentage of the principal amount, equal to the semi-annual equivalent yield to maturity or interpolated maturity of the Comparable Treasury Issue, assuming that the Comparable Treasury Issue is purchased on the redemption date for a price equal to the Comparable Treasury Price, as calculated by the Designated Investment Banker.

“Comparable Treasury Issue” means, with respect to any redemption date for a particular Bond, the United States Treasury security or securities selected by the Designated Investment Banker which has an actual or interpolated maturity comparable to the remaining average life of the Bond to be redeemed, and that would be utilized in accordance with customary financial practice in pricing new issues of debt securities of comparable maturity to the remaining average life of the Bond to be redeemed.

“Comparable Treasury Price” means, with respect to any redemption date for a particular Bond:

- (1) the most recent yield data for the applicable U.S. Treasury maturity index from the Federal Reserve Statistical Release H.15 Daily Update (or any comparable or successor publication) reported, as of 11:00 a.m. New York City time, on the Valuation Date; or
- (2) if the yield described in (1) above is not reported as of such time or the yield reported as of such time is not ascertainable, the average of four Reference Treasury Dealer Quotations for that redemption date, after excluding the highest and lowest of such Reference Treasury Dealer Quotations, or if the Designated Investment Banker obtains fewer than four Reference Treasury Dealer Quotations, the average of all quotations obtained by the Designated Investment Banker.

“Designated Investment Banker” means one of the Reference Treasury Dealers appointed by the City.

“Reference Treasury Dealer” means each of four firms, specified by the City from time to time, that are primary United States Government securities dealers in the City of New York (each, a “Primary Treasury Dealer”); provided, that if any of them ceases to be a Primary Treasury Dealer, the City will substitute another Primary Treasury Dealer.

“Reference Treasury Dealer Quotations” means, with respect to each Reference Treasury Dealer and any redemption date for a particular Bond, the average, as determined by the Designated Investment Banker, of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) quoted in writing to the Designated Investment Banker by such Reference Treasury Dealer at 3:30 p.m., New York City time, on the Valuation Date.

“Valuation Date” means the third business day preceding the redemption date.

Extraordinary Optional Redemption

The Bonds are subject to redemption prior to their stated maturity date at the option of the City, in whole or in part upon the occurrence of an Extraordinary Event (defined below), at a redemption price (the “Extraordinary

Redemption Price”) equal to the greater of: (i) the issue price set forth on the cover page hereof (but not less than 100%) of the principal amount of such Bonds to be redeemed; or (ii) the sum of the present value of the remaining scheduled payments of principal and interest to the maturity date of such Bonds to be redeemed, not including any portion of those payments of interest accrued and unpaid as of the date on which such Bonds are to be redeemed, discounted to the date on which such Bonds are to be redeemed on a semi-annual basis, assuming a 360-day year consisting of twelve 30-day months, at the Treasury Rate (described above) plus 100 basis points; plus, in each case, accrued interest on such Bonds to be redeemed to the redemption date.

An “Extraordinary Event” will have occurred if a material adverse change has occurred to Section 54AA or 6431 of the Internal Revenue Code of 1986, as amended (the “Code”) (as such Sections were added by Section 1531 of the Recovery Act, pertaining to “Build America Bonds”) pursuant to which the City’s 35% cash subsidy payment from the United States Treasury is reduced or eliminated.

Mandatory Redemption

The Bonds are Term Bonds and, if not optionally redeemed, purchased or defeased in accordance with the Bond Ordinance, are subject to mandatory redemption at a redemption price equal to 100% of the principal amount thereof, plus accrued interest to the date fixed for redemption, and without premium, on December 1 in the years and principal amounts as follows:

Year	Principal Amount
2033	\$ 9,800,000
2034	10,165,000
2035	10,545,000
2036	10,940,000
2037	11,345,000
2038	11,770,000
2039 ⁽¹⁾	12,210,000

(1) Final maturity.

If the City optionally redeems, purchases or defeases Term Bonds, the par amount of the Term Bonds so redeemed, purchased or defeased shall be credited against the scheduled mandatory redemption amounts pro rata for those Term Bonds.

Notice of Redemption

The City shall cause notice of any intended redemption of Bonds to be given not less than 30 nor more than 60 days prior to the date fixed for redemption by first class mail, postage prepaid, to the registered owner of any Bond to be redeemed at the address appearing on the Bond Register at the time the Bond Registrar prepares the notice, and this requirement shall be deemed to have been fulfilled when notice has been mailed, whether or not it is actually received by the owner of any Bond. Interest on Bonds called for redemption shall cease to accrue on the date fixed for redemption unless the Bond or Bonds called are not redeemed when presented pursuant to the call. Notwithstanding the foregoing, for so long as the Bonds are registered in the name of Cede & Co., as nominee of DTC, notice of redemption shall be given in accordance with the Letter of Representations (as it may be changed).

In the case of an optional redemption, the notice may state that the City retains the right to rescind the redemption notice and the related optional redemption of Bonds by giving a notice of rescission to the affected registered owners at any time prior to the scheduled optional redemption date. Any notice of optional redemption that is so rescinded shall be of no effect, and the Bonds for which the notice of optional redemption has been rescinded shall remain outstanding.

Purchase for Cancellation

The City reserves the right to purchase any of the Bonds for cancellation at any time at any price acceptable to the City.

Procedure in the Event of Revisions of Book Entry Transfer System

If the City is unable to retain a qualified successor to DTC or the City has determined that it is in the best interest of the City not to continue the book entry system of transfer or that interests of Beneficial Owners of the Bonds might be adversely affected if the book entry system of transfer is continued, the City shall execute, authenticate, and deliver at no cost to the Beneficial Owners of the Bonds or their nominees, Bonds in fully registered form, in the denomination of \$5,000 or any integral multiple thereof. Thereafter, the principal of the Bonds shall be payable upon due presentment and surrender thereof at the principal office of the Registrar, currently The Bank of New York Mellon in New York, New York; interest on the Bonds will be payable by check or draft mailed to the persons in whose names such Bonds are registered, at the address appearing upon the registration books on the 15th day of the month preceding an interest payment date, or, at the request of an owner of \$1,000,000 or more in aggregate principal amount of Bonds, by wire transfer to an account in the United States designated in writing by such owner prior to the record date; and the Bonds will be transferable as provided in the Bond Ordinance.

PURPOSE AND APPLICATION OF BOND PROCEEDS

The Bonds are being issued to provide funds to pay for certain capital improvements to the Water System, to fund a debt service reserve for the Bonds, and to pay the costs of issuance of the Bonds. For a description of the Water System's capital improvement program, see "CAPITAL IMPROVEMENT PROGRAM" herein.

The following table shows the estimated sources and uses of the Bond proceeds:

Sources of Funds	Total
Par Amount of the Bonds	\$ 76,775,000
Total	\$ 76,775,000
Uses of Funds	
Project Costs	\$ 71,634,231
Reserve Account Deposit	4,419,509
Issuance Expenses(1)	721,260
Total	\$ 76,775,000

- (1) Issuance expenses include underwriter's discount, legal fees, financial advisor's fees, rating fees, and other costs incurred in connection with the issuance of the Bonds.

SECURITY FOR THE BONDS

Pledge of Revenues

Under the Bond Ordinance and subject to its terms and conditions, the Bonds are special limited obligations of the City, payable from and secured solely by Net Revenue of the Water System and all money and investments held in the Bond Fund, the Rate Stabilization Account, and the Construction Fund (except for money or investments held for the purpose of compliance with rebate requirements under the Code).

THE BONDS ARE NOT GENERAL OBLIGATIONS OF THE CITY, AND NEITHER THE FULL FAITH AND CREDIT NOR THE TAXING POWER OF THE CITY OR OF THE STATE OF WASHINGTON, NOR ANY REVENUES OF THE CITY DERIVED FROM SOURCES OTHER THAN THE WATER SYSTEM OF THE CITY, ARE PLEDGED TO THE PAYMENT THEREOF.

The Bonds are being issued on a parity of lien with the \$111,100,000 Outstanding Parity Bonds. The City has obligated itself to set aside and pay into the Bond Fund certain amounts out of the Net Revenue of the Water System

sufficient to pay the principal of and interest on the Bonds, the Outstanding Parity Bonds, and any Future Parity Bonds.

The City has outstanding \$79,150,000 principal amount of Second Supply System Bonds and \$14,587,985 in junior lien State loans, of which Tacoma Water is responsible for paying approximately 55% of the debt service as a Contract Resource Obligation. The City also has certain step-up obligations in the event of a default by any other Participant in the Second Supply Project. See “Additional Obligations—Contract Resource Obligations” and “WATER SUPPLY SYSTEM—The Second Supply Project.” As a Contract Resource Obligation, Tacoma Water’s share of the City’s share of debt service on the Second Supply System Bonds and junior lien loans is payable as an Operation and Maintenance Expense of the Water System with a lien on Gross Revenue of the Water System prior to the lien thereon of the Bonds, Outstanding Parity Bonds, and Future Parity Bonds.

Washington State law provides that the owner of a bond, such as the Bonds, the payment of which is pledged from a special fund, such as the Bond Fund, has a claim only against that fund and proportionate amounts of revenue pledged to that fund. Under Washington State law, any bondowner may bring an action to compel a city to set aside and pay into the special fund the amount that a city is obligated to set aside and pay therein. See Appendix A—”SUMMARY OF THE BOND ORDINANCE—DEFAULTS AND REMEDIES.”

See Appendix A—”SUMMARY OF THE BOND ORDINANCE—PAYMENT OF AND SECURITY FOR THE BONDS.”

Flow of Funds

The Gross Revenue of the Water System shall be used for the following purposes only, and shall be applied in the following order of priority:

- (1) To pay the Operation and Maintenance Expenses, including payments for Contract Resource Obligations;
- (2) To pay interest on Parity Bonds and net payments on Parity Payment Agreements when due;
- (3) To pay the principal of Parity Bonds as it comes due at maturity or as the principal is required to be paid pursuant to mandatory redemption requirements applicable to Term Bonds, and to make payments due under any reimbursement agreement with a Bond Insurer for a series of Parity Bonds, which agreement requires those payments to be treated on a parity of lien with the Parity Bonds;
- (4) To make all payments required to be made into the Reserve Account, all payments required to be made under any agreement relating to the provision of Reserve Insurance, and payments due under any reimbursement agreement with a Bond Insurer, which agreement requires those payments to be treated on a parity of lien with the payments required to be made into the Reserve Account;
- (5) To make all payments required to be made into any revenue bond, note, warrant, or other revenue obligation redemption fund, debt service account, or reserve account created to pay or secure the payment of the principal of and interest on any revenue bonds, notes, warrants, or other obligations of the City having a lien upon the revenue of the Water System junior and inferior to the lien thereon for the payment of the principal of and interest on the Parity Bonds, including the Public Works Trust Fund Loans; and
- (6) To retire by redemption or purchase in the open market any outstanding revenue bonds or other revenue obligations of the Water System, to make necessary additional betterments, improvements, and repairs to or extensions and replacements of the Water System, to make deposits into the Rate Stabilization Account, or for any other lawful Water System purposes.

The City may transfer any money from any funds or accounts of the Water System legally available therefor, except bond redemption funds, refunding escrow funds, or defeasance funds, to meet the required payments to be made into the Bond Fund.

Rate Covenant

The City has pledged in the Bond Ordinance that it will establish, maintain, and collect rates and charges for services and facilities provided by the Water System, which will be fair and equitable, and will adjust those rates and charges from time to time so that:

- (1) The Gross Revenue will be sufficient to (i) pay all Operation and Maintenance Expenses, (ii) pay when due all amounts that the City is obligated to pay into the Bond Fund and the accounts therein, and (iii) pay all taxes, assessments, or other governmental charges lawfully imposed on the Water System or the revenue therefrom or payments in lieu thereof and any and all other amounts that the City may now or hereafter become obligated to pay from the Gross Revenue by law or contract; and
- (2) The Net Revenue of the Water System in each fiscal year will be at least equal to 1.25 times the Annual Debt Service that year on all Parity Bonds (the "Coverage Requirement").

For purposes of the rate covenants, Tacoma Water's share of costs of the Second Supply Project are Operation and Maintenance Expenses and are not part of Annual Debt Service. The failure of the City to comply with paragraphs (1) and (2) above will not be an Event of Default as defined in the Bond Ordinance if the City promptly retains an Independent Consulting Engineer to recommend to the City Council adjustments in the rates of the Water System necessary to meet the requirements of those subparagraphs and if the City Council adopts the recommended modifications within 180 days of the date the failure became known to the City Council.

Reserve Account

The Bond Ordinance obligates the City to fund the Reserve Account. The Reserve Requirement, as of any date, is an amount equal to the lesser of Maximum Annual Debt Service or 125% of Average Annual Debt Service on all outstanding Parity Bonds. Once the 2001 Bonds are no longer outstanding, the Reserve Requirement for a series of Parity Bonds shall not exceed 10% of the net proceeds of such Parity Bonds. Upon the issuance of the Bonds, the City will use Bond proceeds in an amount that, together with the Reserve Insurance policies for the Outstanding Parity Bonds, will satisfy the Reserve Requirement for the Bonds.

Any deficiency created in the Reserve Account by reason of any withdrawal therefrom for payment into the Principal and Interest Account must be made up within 12 months from money in the Water Division Fund after payment of Operation and Maintenance Expenses and deposits to the Principal and Interest Account.

The City has retained the right under the Bond Ordinance to obtain Reserve Insurance in lieu of specific amounts required to be on deposit in the Reserve Account, which Reserve Insurance may not be subject to cancellation on less than three years' notice. Upon notice of cancellation, the City is obligated to fund the Reserve Account over a 36 month period from transfers from the Water Division Fund after making provision for payment of Operation and Maintenance Expenses and for required payments into the Bond Fund.

Once the Outstanding Parity Bonds are no longer outstanding, a supplemental ordinance may establish a separate reserve account for a series of Future Parity Bonds, in which case the Reserve Account shall not secure such Future Parity Bonds.

See Appendix A—"SUMMARY OF THE BOND ORDINANCE—PAYMENT OF AND SECURITY FOR THE BONDS."

The Reserve Insurance Policies

Financial Guaranty Insurance Company (“Financial Guaranty”) issued municipal bond debt service reserve fund policies relating to the City’s Water System Revenue Bonds, 1997 (the “1997 Bonds”) (which were refunded by the 2005 Bonds), the 2001 Bonds and the 2005 Bonds. The maximum amount of the reserve policy relating to the 2005 Bonds is \$3,675,596 and \$4,030,821 for the 1997 and 2001 Bonds. A reserve policy was obtained from Financial Security Assurance Inc. (“FSA”) in the maximum amount of \$2,778,351.56 to satisfy the Reserve Requirement of the 2003 Bonds. Moody’s Investors Service (“Moody’s”), Standard & Poor’s Ratings Services (“S&P”) and Fitch Ratings (“Fitch”) have all withdrawn their ratings for Financial Guaranty. FSA is currently rated Aa3, AAA and AA by Moody’s, S&P and Fitch, respectively. The ordinances authorizing the Outstanding Parity Bonds do not require that the Reserve Account be funded when the providers of reserve insurance are downgraded.

Rate Stabilization Account

The Bond Ordinance authorizes a Rate Stabilization Account in the Water Division Fund. The City is in the process of creating a Rate Stabilization Account and expects to deposit approximately \$20 million to \$25 million into such account. For purposes of calculating the Coverage Requirement described under “Rate Covenant,” Net Revenue excludes deposits into the Rate Stabilization Account and includes withdrawals from the Rate Stabilization Account. See Appendix A—“SUMMARY OF THE BOND ORDINANCE—PAYMENT OF AND SECURITY FOR THE BONDS.”

Additional Obligations

Future Parity Bonds. Pursuant to the Bond Ordinance, the City has reserved the right to issue Future Parity Bonds or to enter into Parity Payment Agreements for purposes related to the Water System or to refund a portion of the Parity Bonds upon satisfaction of certain conditions set forth in the Bond Ordinance. Before issuing Future Parity Bonds, among other things, there must be on file with the City either:

- (1) A certificate of the Director of Finance demonstrating that during any 12 consecutive calendar months out of the immediately preceding 24 calendar months Net Revenue was at least equal to 1.25 times the projected Maximum Annual Debt Service for all Parity Bonds plus the Future Parity Bonds proposed to be issued; or
- (2) A certificate of an Independent Consulting Engineer that in his or her opinion the Net Revenue will be at least equal to 1.25 times the projected Average Annual Debt Service for all Parity Bonds plus the Future Parity Bonds proposed to be issued. In providing that certificate, the Independent Consulting Engineer may take into account certain adjustments to Net Revenue as permitted by the Bond Ordinance.

If the Future Parity Bonds proposed to be issued are for the sole purpose of refunding outstanding bonds payable from the Bond Fund, no such coverage certification shall be required if the Annual Debt Service on the Parity Bonds after the issuance of the Future Parity Bonds is not, for any year in which Parity Bonds are outstanding, more than \$5,000 over the Annual Debt Service on the Parity Bonds prior to the issuance of those Future Parity Bonds.

See Appendix A—“SUMMARY OF THE BOND ORDINANCE—PROVISIONS FOR FUTURE PARITY BONDS.”

Parity Payment Agreements and Reimbursement Obligations. The Bond Ordinance permits the City to enter into a Payment Agreement for the purpose of managing the City’s exposure to fluctuations or levels of interest rates, currencies or commodities or other interest rate, investment, asset or liability management purposes. Upon satisfaction of the requirements for the issuance of Future Parity Bonds, a Payment Agreement may constitute a charge and lien on the Net Revenue of the Water System equal in rank with the charge and the lien of Parity Bonds. The City has not entered into any such Parity Payment Agreements and has no plans to do so at this time. See Appendix A—“SUMMARY OF THE BOND ORDINANCE—PAYMENT AGREEMENT AND PARITY PAYMENT AGREEMENTS.”

If the City elects to meet the Reserve Requirement or any portion thereof through the use of Reserve Insurance, the City may contract that payments to reimburse the provider of the Reserve Insurance shall be on a parity of lien with the payments required to be made into the Reserve Account. The reimbursement obligations for the debt service reserve fund policies for the Outstanding Parity Bonds are on a parity with the funds in the Reserve Account. See “—The Reserve Insurance Policies.”

Contract Resource Obligations. Pursuant to the Bond Ordinance, the City may at any time enter into one or more obligations for the acquisition, from facilities to be constructed, of water supply, transmission, treatment, or other commodity or service relating to the Water System. Upon compliance with certain requirements of the Bond Ordinance, the City may determine that such contract or obligation is a Contract Resource Obligation and may provide that all payments under that Contract Resource Obligation (including payments prior to the time that water supply, transmission, treatment, or other commodity or service is being provided, or during a suspension or after termination of supply or service) shall be Operation and Maintenance Expenses. The Regional System is a Contract Resource Obligation of the Water System. Before entering into a Contract Resource Obligation, among other things, there must be on file a certificate of an Independent Consulting Engineer stating that (i) the payments to be made by the City in connection with the Contract Resource Obligation are reasonable for the supply, transmission, treatment, or other service rendered; (ii) the source of any new supply, and any facilities to be constructed to provide the supply, transmission, treatment, or other service, are sound from a water or other commodity supply or transmission planning standpoint, are technically and economically feasible in accordance with prudent utility practice, and are likely to provide supply or transmission no later than a date set forth in the Independent Consulting Engineer’s Certification; and (iii) the Net Revenue (further adjusted by the Independent Consulting Engineer’s estimate of the payments to be made in accordance with the Contract Resource Obligation) for the five fiscal years following the year in which the Contract Resource Obligation is incurred, as such Net Revenue is estimated by the Independent Consulting Engineer (with such estimate based on such factors as he or she considers reasonable), will be at least equal to the Coverage Requirement. Payments required to be made under Contract Resource Obligations shall not be subject to acceleration. See Appendix A—”SUMMARY OF THE BOND ORDINANCE—SEPARATE UTILITY SYSTEMS; CONTRACT RESOURCE OBLIGATIONS.”

Junior Lien Obligations. Nothing in the Bond Ordinance prohibits the issuance of obligations of the Water System junior to the lien of the Parity Bonds. Tacoma Water currently has outstanding two low-interest loans from the State of Washington Public Works Trust Fund totaling \$11,102,439 and one low-interest loan from the State Revolving Fund totaling \$1,932,632, which are junior to the Bonds in their lien on the revenues and funds of the Water System.

Defeasance

In the event that the City, in order to effect the payment, retirement or redemption of any Bond, sets aside in the Bond Fund or in another special account, held in trust by the City or by a qualified trustee, advance refunding bond proceeds or other money lawfully available or Government Obligations or any combination of such proceeds, money and/or Government Obligations, in amounts which, together with known earned income from the investment thereof are sufficient to redeem, retire or pay such Bond in accordance with its terms and to pay when due the interest and redemption premium, if any, thereon, and such proceeds, money and/or Government Obligations are irrevocably set aside and pledged for such purpose, then no further payments need be made into the Bond Fund for the payment of the principal of and interest on such Bond, the Registered Owner of such Bond shall cease to be entitled to any lien, benefit or security of the Bond Ordinance except provisions regarding the transfer, exchange and replacement of Bonds, and the Registered Owner of such Bond shall be entitled to receive payment of principal, premium, if any, and interest only from such special account, and such Bond shall be deemed not otherwise to be outstanding hereunder.

The term “Government Obligations” has the meaning given in chapter 39.53 RCW, as amended, currently: (1) direct obligations of, or obligations the principal of and interest on which are unconditionally guaranteed by the United States of America and bank certificates of deposit secured by such obligations; (2) bonds, debentures, notes, participation certificates, or other obligations issued by the Banks for Cooperatives, the Federal Intermediate Credit Bank, the Federal Home Loan Bank system, the Export-Import Bank of the United States, Federal Land Banks, or the Federal National Mortgage Association; (3) public housing bonds and project notes fully secured by contracts with the United States; and (4) obligations of financial institutions insured by the Federal Deposit Insurance

Corporation or the Federal Savings and Loan Insurance Corporation, to the extent insured or to the extent guaranteed as permitted under any other provision of State law.

If the City defeases any Bonds, such Bonds may be deemed to be retired and “reissued” for federal income tax purposes as a result of the defeasance. See “TAX MATTERS—Disposition or Retirement.”

Additional Covenants

The Bond Ordinance also contains covenants regarding operation and maintenance of the Water System, sale, transfer, or disposition of the Water System, no free service, liens upon the Water System, books and accounts, collection of delinquent accounts, maintenance of insurance and condemnation awards and insurance proceeds. See Appendix A—“SUMMARY OF THE BOND ORDINANCE—COVENANTS WITH BONDOWNERS.”

Permitted Investments

Money held in the Bond Fund (and the accounts therein) and the Bond proceeds account may be invested in legal investments, and any earnings may be retained in such fund or account for the purpose of that fund or transferred to the Bond Fund. For a description of the funds and accounts created by the Bond Ordinance, see Appendix A—“SUMMARY OF THE BOND ORDINANCE—PAYMENT OF AND SECURITY FOR THE BONDS.”

No Acceleration

Neither a bondowner nor any bondowners’ trustee has the right under the Bond Ordinance to accelerate the payment of debt service on the Bonds upon the occurrence of an Event of Default.

DEBT SERVICE REQUIREMENTS AND ADDITIONAL BORROWING

The following table shows Tacoma Water's Contract Resource Obligation payments for its share of debt service on the Regional System Bonds and State loans, debt service on Tacoma Water's Outstanding Parity Bonds and the Bonds. The table does not show \$13,035,070 in junior lien Tacoma Water loans. See "SECURITY FOR THE BONDS—Additional Obligations."

Summary of Debt and Debt Service Requirements

Year	Contract Resource Obligation (2)	Outstanding Parity Bonds	The Bonds		Total Parity Bond Debt Service
			Principal	Interest (1)	
2009	\$ 3,524,599	\$ 10,432,133	--	--	\$ 10,432,133
2010	3,526,676	10,432,583	--	\$ 4,746,480	15,179,063
2011	3,513,804	10,435,558	--	4,415,330	14,850,888
2012	3,502,296	10,434,170	--	4,415,330	14,849,500
2013	3,503,667	10,432,370	--	4,415,330	14,847,700
2014	3,503,261	10,436,770	--	4,415,330	14,852,100
2015	3,528,578	10,435,574	--	4,415,330	14,850,904
2016	3,549,048	10,432,606	--	4,415,330	14,847,936
2017	3,548,878	10,437,013	--	4,415,330	14,852,343
2018	3,554,325	10,482,438	--	4,415,330	14,897,768
2019	4,020,685	10,484,769	--	4,415,330	14,900,099
2020	4,030,481	10,478,194	--	4,415,330	14,893,524
2021	4,036,348	10,476,788	--	4,415,330	14,892,118
2022	3,760,800	10,480,113	--	4,415,330	14,895,443
2023	3,246,986	10,479,125	--	4,415,330	14,894,455
2024	--	2,420,000	--	4,415,330	6,835,330
2025	--	2,420,250	--	4,415,330	6,835,580
2026	--	--	--	4,415,330	4,415,330
2027	--	--	--	4,415,330	4,415,330
2028	--	--	--	4,415,330	4,415,330
2029	--	--	--	4,415,330	4,415,330
2030	--	--	--	4,415,330	4,415,330
2031	--	--	--	4,415,330	4,415,330
2032	--	--	--	4,415,330	4,415,330
2033	--	--	\$ 9,800,000	4,415,330	14,215,330
2034	--	--	10,165,000	3,851,732	14,016,732
2035	--	--	10,545,000	3,267,143	13,812,143
2036	--	--	10,940,000	2,660,700	13,600,700
2037	--	--	11,345,000	2,031,541	13,376,541
2038	--	--	11,770,000	1,379,090	13,149,090
2039	--	--	12,210,000	702,197	12,912,197
TOTAL (3)	\$ 54,350,433	\$161,630,454	\$ 76,775,000	\$ 120,191,479	\$ 358,596,933

(1) Before 35% federal credit payments.

(2) Payable as an Operation and Maintenance Expense. See "THE WATER SYSTEM – The Second Supply Project" herein.

(3) Totals may not foot due to rounding.

Additional Borrowing

Tacoma Water currently plans to issue additional Parity Bonds starting in 2011. These bonds will fund a large portion of the capital improvements in the 2009-2013 Capital Improvement Program (see "CAPITAL IMPROVEMENT PROGRAM"), including design and construction of Tacoma Water's preferred treatment option to meet Federal and State drinking water regulations. See "THE WATER SYSTEM – Water Quality and Treatment" for a discussion of the City's water treatment project. A portion of the bonds may be issued as Regional System Bonds.

THE CITY

The City of Tacoma was incorporated in 1884 and utilizes the Council Manager form of government, which is administered by a City Council under the Constitution and laws of the State of Washington and the City Charter. The Council is composed of a Mayor and eight Council members, five of whom are elected from districts which have been apportioned according to population. The three remaining positions are “at large” positions, nominated and elected City wide. The Councilmember positions are four year terms with overlapping terms to allow for the election of four new Councilmembers every two years. The Mayor is elected City wide for a four year term and is the presiding officer of the Council. Councilmembers, including the Mayor, can serve no more than ten consecutive years as a member of the Council, Mayor or combination thereof.

The City Council appoints a City Manager who is the chief executive officer of the City and who serves at the pleasure of the City Council. The City Manager is responsible to the Council for the administration of all departments of the City with the exception of the Department. The City Manager has the power to appoint department heads.

The City Manager appoints a Director of Finance who supervises the financial affairs of the City. The Director of Finance is responsible for operating a general accounting system for the City in conformity with generally accepted accounting principles and practices, supervising the purchasing activities of all departments and the receipt, custody, and disbursement of all City funds and money. Under the operating procedures of the City, the Director of Finance is responsible for the payment of principal and interest on all bonds issued by the City.

The City Manager appoints a City Treasurer who is responsible for the custody of all City funds, including funds of Tacoma Water. The City Treasurer receives all money due and belonging to the City, and keeps an accurate, detailed account of the same in the manner prescribed by the Director of Finance. A Finance Committee composed of the Mayor, Director of Finance, and City Treasurer controls the investment of City funds.

THE DEPARTMENT OF PUBLIC UTILITIES—TACOMA WATER

Department of Public Utilities

The City Charter provides for a Department of Public Utilities governed by a five member Public Utility Board (the “Board”). The Board is responsible for general utility policy, and its members are appointed by the Mayor and confirmed by the City Council. The Department’s budget is presented to the Board for review and approval and then forwarded to the City Council for approval and inclusion in the City’s budget. The Board meets bi-monthly.

The Department consists of the Light Division (“Tacoma Power”), Water Division (“Tacoma Water”), and Belt Line Railroad Division (“Tacoma Rail”). The Board serves as the sole policy board for the approval of most Department business. In the case of budgets, rates, bond issues, real property transactions, and system expansions, actions approved by the Board must also be approved by the City Council.

The Board appoints the Director of Utilities who is chief executive officer of the Department and serves at the pleasure of the Board. The Director, with the concurrence of the Board, has the power to appoint division superintendents.

Utility rates and charges initiated by the Board and adopted by the City Council are not subject to review or approval by any other governmental agency.

The City Charter provides that, except for a reasonable gross earnings tax imposed by the City Council for the benefit of the City’s general fund, the revenues of utilities owned and operated by the City may not be used for any purposes other than the ongoing operations of the utilities and payment of debt service on utility debt. The funds of any utility may not be used to make loans to or purchase the bonds of any other utility, department, or agency of the City.

Tacoma Water—General

Tacoma Water was formed in 1893 when the City purchased the water and light utility properties of the former Tacoma Water and Light Company. The City acquired rights for up to 73 million gallons per day (“MGD”) of water from the Green River and in 1912 began construction of the Green River gravity system, which includes the headworks dam facilities, 43 miles of pipeline and 110 million gallons (“MG”) of storage. Water was first delivered to the City in 1913. The City was awarded a second water right on the Green River in 1986 for 65 MGD. The present gravity system has a capacity of 165 MGD and delivers water to most of the City without the need for any pumping equipment.

As the City grew, a system of wells was developed in south Tacoma and on the North Fork of the Green River to meet summer peak use periods as well as the City’s needs during periods of turbidity in the Green River. Today, the system of wells has a capacity of approximately 59 MGD and on an annual basis supplies approximately 5% of the City’s water needs.

Tacoma Water is one of the largest publicly owned water utilities in the State of Washington. The following table displays selected operating and financial data regarding Tacoma Water as of December 31, 2008 and 2007.

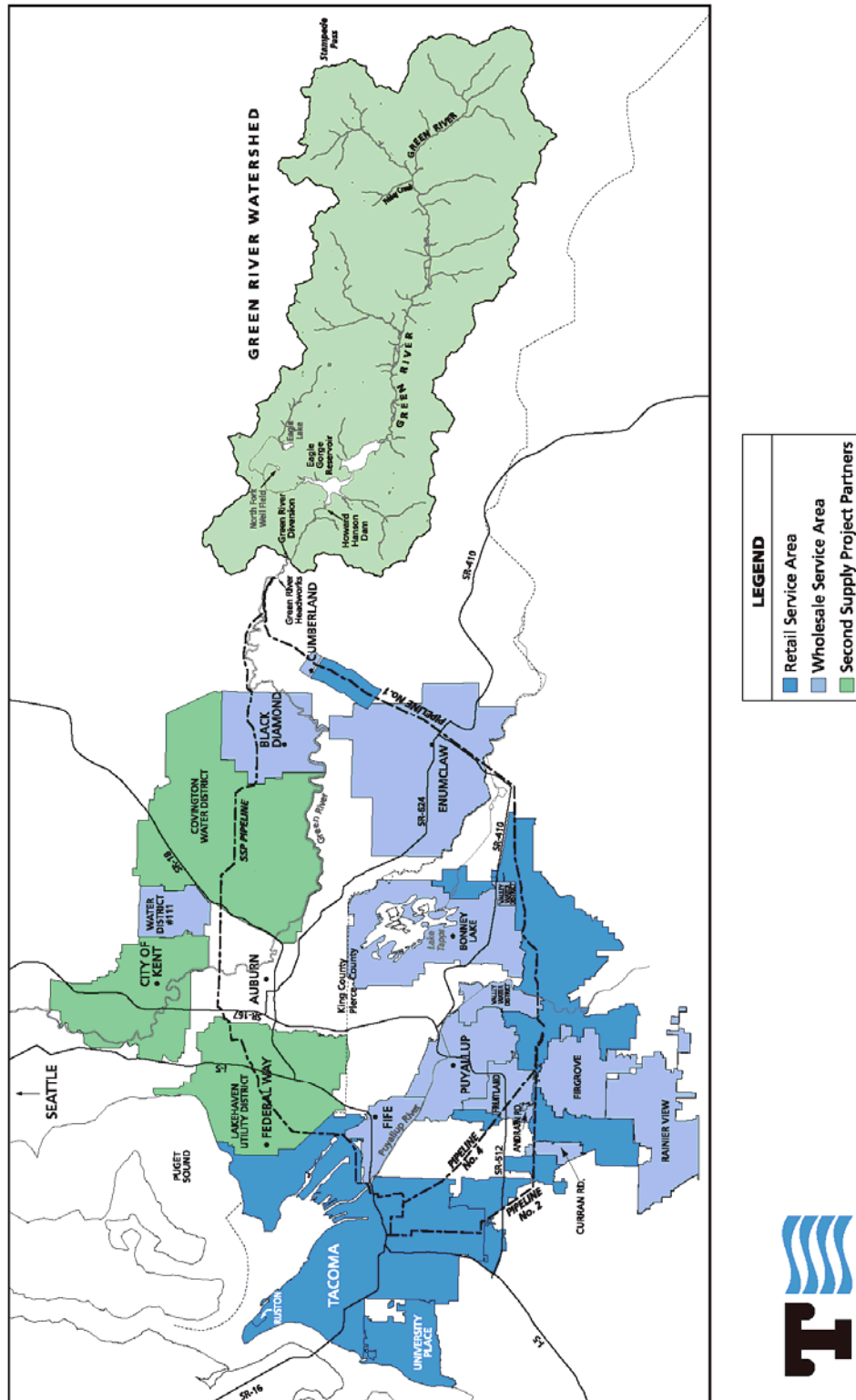
Selected Operating and Financial Data Calendar Years 2008 and 2007

	2008	2007
Average Number of Metered Customers	95,858	96,278
Operating Revenue	\$ 57,025,000	\$52,726,000
Net Operating Expenses(1)	\$ 49,286,000	\$45,365,000
Debt Service Coverage Ratio	1.81x	2.09x
Total Water Billed (Million Gallons)	18,252	18,487
Average Daily Use (Million Gallons)	54.4	56.6
Maximum Daily Use (Million Gallons)	86.6	90.6

(1) Excludes City gross earnings tax and depreciation.

Source: Water Division, 2008 and 2007 Financial Reports.

Service Area and Map



Tacoma Water's current service area consists of the City and the urbanized areas of Pierce and south King Counties. The area extends from the northerly boundary of Lakewood Water District and Parkland Light and Water Company in the south, northward to the City of Federal Way in King County. The eastern boundary is the foothills of the Cascade Mountains. The western boundary is Puget Sound. Water service outside the City limits is provided under franchises granted by both Pierce County and King County, and the cities of Puyallup, Federal Way and University Place. Approximately 39% of Tacoma Water's residential service is outside of the City limits.

Tacoma Water's service outside of the City limits began in 1912 when customers adjacent to the first transmission pipeline from the Green River were served from the transmission line and from distribution extensions from the pipeline. As a result, the Water System serves customers as far away as Palmer and Cumberland in King County.

Tacoma Water is the exclusive provider of water service within the City and is designated as a key provider of water service within Pierce County under the Pierce County Coordinated Water System Plan. Tacoma Water presently provides direct service to some customers within the city limits of several municipalities, including the cities of Federal Way, Puyallup, and University Place.

Historically, the Water System has expanded in order to meet City growth and to supply surrounding communities and water utilities. Over the years, the City has acquired water districts, water companies, and cooperatives as well as individual services outside the City limits. The City will continue such an acquisition program when requested, provided it is economically sound and consistent with growth management policy. Some examples are the acquisition of South East Tacoma Mutual, Hyada Water Company and Day Island.

The State of Washington has a Growth Management Act which directs growth to the urbanizing areas. Dense development in rural areas is generally discouraged. It is anticipated that the direction of growth to the urbanizing areas will most likely result in an increase in the demand for water in the City's service area in coming years.

Currently, wholesale service is a small part of Tacoma Water's operations. Less than 5% of revenue is derived from that source but it is expected to grow substantially as additional water rights become more difficult to obtain by nearby growing communities that rely on limited ground water supplies.

Management

Brief descriptions of the backgrounds of key officials of the City, the Department, and Tacoma Water follow.

William A. Gaines, Director of Utilities, assumed his position in October 2007, after serving as Superintendent/Chief Operating Officer of Tacoma Power for a year. Mr. Gaines, an experienced executive with approximately 30 years in the utility industry, came to Tacoma from Seattle City Light, where he served as Power Supply and Environmental Affairs Officer and as Power Management Executive. He spent much of his career as an executive officer at Puget Sound Energy, where he served as Vice President for Engineering and Contracting and as Vice President for Energy Supply. Mr. Gaines is active in regional industry groups including the Public Power Council, Pacific Northwest Utilities Conference Committee and Western Systems Power Pool, and sits on the Board of the Tacoma/Pierce County Chamber of Commerce and the Pierce County Economic Development Board. Mr. Gaines received a B.S. degree in electrical engineering from Washington State University and an M.B.A. from the University of Puget Sound. He also attended the executive development program at Stanford University.

John Kirner, P.E., Superintendent, Water Division, was appointed in 2004. He joined the Department in 1983 and served as Assistant Water Superintendent for 18 years. Mr. Kirner earned his B.S. in civil engineering from Tufts University, an M.S. in engineering from University of Michigan at Ann Arbor, and a M.B.A. from the University of Puget Sound.

Linda McCrea, P.E., Deputy Water Superintendent, joined the City in 1980, became the Water Distribution Manager in 1993 and became Deputy Water Superintendent in 2006. She has a B.S. in civil engineering from the University of Washington.

Jane Evancho, P.E., Rates and Financial Analysis Manager, joined the City in 1987, became the Water Resource Planning Manager in 1993 and became the Rates and Financial Analysis Manager in July 2009. She has a B.S. and M.S. in agricultural engineering from Oregon State University.

Christopher Johnson, P.E., Water Distribution Engineering Manager, joined the City in 1997 as a Surface Water Engineer with Public Works, Environmental Services Engineering. He joined Tacoma Water in 2005 and became interim Distribution Engineering Manager in July 2009. He holds a B.S. in Civil Engineering and a minor in Mathematics from Washington State University.

Heather Pennington, P.E., Resource Planning Manager, joined Tacoma Water in 1994, and became Tacoma Water's interim Distribution Manager in 2006, Distribution Engineering Manager in 2007 and Resource Planning Manager in July 2009. She holds a M.B.A. from Pacific Lutheran University and a B.S. in environmental engineering from Northwestern University.

Chris McMeen, P.E., Water Quality Manager, joined the City in 2002 and became the Water Quality Manager in 2004. He has a B.S. and M.S. in civil engineering from the University of Washington.

Dave Sherman, P.E., Water Supply Manager, joined the City in 1977 and became the Water Supply Manager in 1993. He has a B.S. in civil engineering from Washington State University.

Raymond West, Water Distribution Operations Manager, joined Tacoma Water in 1975 and became Assistant Distribution Manager in 1998 and the Distribution Operations Manager in 2007. He has several certifications including electronics and a State of Washington Water Works Operator license.

Budgetary Policies

The Tacoma Water biennial budget is proposed by the Public Utility Board and adopted by the City Council with legal budgetary control at the fund level, i.e., expenditures may not exceed budgeted appropriations at the fund level. The City Manager and Director of Utilities may authorize transfers within funds; however, the Council must approve, by ordinance, any amendments that increase the total expenditures for the fund.

Auditing

Accounting systems and budgetary controls are prescribed by the Office of the State Auditor in accordance with RCW 43.09.200 and RCW 43.09.230. State statutes require audits for cities to be conducted by the Office of the State Auditor. The City complies with the systems and controls prescribed by the Office of the State Auditor and establishes procedures and records which reasonably assure safeguarding of assets and the reliability of financial reporting.

The State Auditor is required to examine the affairs of cities. The City is audited annually. The examination must include, among other things, the financial condition and resources of the City, whether the laws and constitution of the State are being complied with, and the methods and accuracy of the accounts and reports of the City. Reports of the auditor's examinations are required to be filed in the office of the State Auditor and in the finance department of the City. The City contracts with Moss Adams LLP to perform the annual audit of the financial statements of Tacoma Water. The 2008 audited financial statements of Tacoma Water prepared by Tacoma Water and audited by Moss Adams LLP are contained in Appendix C. Moss Adams has not performed any procedures related to this Official Statement.

Retirement System

Substantially all employees of Tacoma Water are covered by a contributory retirement plan administered by the City's Employee Retirement System. The Retirement System covers employees of the City other than law enforcement officers, fire fighters, and railroad employees, who are covered by retirement plans operated by other entities. Contributions by Tacoma Water in 2008 totaled approximately \$1,260,268. The contribution rate for Tacoma Water's covered payroll is currently set at 16.0% of gross wages (8.64% for Tacoma Water and 7.36% for

employees) and has been set at 18% of gross wages for 2010 (9.72% for Tacoma Water and 8.28% for employees). Tacoma Water is current in all payments to the Retirement System. Further details about the plan are provided in Note 9 in Appendix C—"2008 AND 2007 FINANCIAL STATEMENTS." Milliman performed an actuarial valuation of the Retirement System as of January 1, 2009, which found that due to the rapid decline of the investment markets in 2008, based on the actuarial value of assets, the contribution rates in effect for 2009 and approved for 2010 are sufficient to meet the actuarial costs of the Retirement System. However, based on the market value of the assets as of January 1, 2009, and the assumptions in the actuarial valuation, additional contribution rate increases may be needed in future years. The City will be actively monitoring the Retirement System.

Other Post-Employment Benefits

The Governmental Accounting Standards Board ("GASB") issued a standard concerning Accounting and Financial Reporting by Employers for Post-Employment Benefits Other than Pensions (GASB 45). In addition to pensions, many state and local governmental employers provide other post-employment benefits ("OPEB") as a part of total compensation to attract and retain the services of qualified employees. OPEB includes post employment health care as well as other forms of post-employment benefits when provided separately from a pension plan. The standard provides for the measurement, recognition and display of OPEB expenses/expenditures, related liabilities (assets), note disclosures, and, if applicable, required supplementary information in the financial reports.

The City allows retirees to participate in medical, dental and vision programs from the time retirement begins until they qualify for Federal funded programs. The City uses a pay as you go funding and the retiree is responsible for paying a blended premium, which prior to retirement was paid by the City. As of January 1, 2007, there were 4,834 members in the City's plan. As of December 31, 2008, the City's net OPEB obligation was \$10,430,277, of which \$495,507 related to the Water System. Further details about OPEB are provided in Note 10 in Appendix C—"2008 AND 2007 FINANCIAL STATEMENTS."

Taxation

Under the City Charter and State law, the City Council may impose a gross earnings tax not exceeding 8.0% upon the revenues of Tacoma Water. The current tax rate is 8.0%. The gross earnings tax is subordinate to the payments required to be made into any fund or funds previously or subsequently created for the payment of the principal of and interest on water revenue bonds of the City.

Tacoma Water pays an excise tax imposed by the State of Washington presently at the rate of 5.029% of gross revenues, with certain exceptions. Tacoma Water also pays miscellaneous fees, licenses, and sales and use taxes. Certain of these taxes and payments are Operation and Maintenance Expenses of the Water System and Operating Expenses of the Regional System.

Program of Insurance

Tacoma Water currently maintains insurance policies and a self insurance program. The insurance policies presently in effect include coverage on the Department's buildings and fleet vehicles as well as general liability and public officials liability. The current insurance policies have deductibles or self insured retention of \$250,000 for buildings and vehicles, and \$1,000,000 for general comprehensive liability. The public officials policy has a deductible of \$200,000 for employee practices liability and \$100,000 for all other issues. The general comprehensive liability policies provide \$20 million of coverage. The City has a policy to cover extraordinary worker's compensation claims with a limit of \$25 million and \$1 million per occurrence. Earthquake coverage has a 3% per building self-insured retention.

Tacoma Water participates in the Department's self insurance claim fund (the "Self Insurance Fund") for payment of third party claims. Assets in the Self Insurance Fund totaled \$4.8 million, which exceeds accrued and incurred but not reported liabilities. Tacoma Water's premium payments in both 2008 and 2007 totaled \$120,000. Contributions are routinely reviewed to determine their adequacy. The Self Insurance Fund is dedicated and requires a two thirds vote of the City Council before it can be used for anything except insurance or casualty losses.

The City and the other Second Supply Project Participants separately insure or self insure the Second Supply Project and potential liabilities arising from or related to the Second Supply Project.

Performance and fidelity bonds covering all employees are provided in amounts up to \$1 million (subject to a \$50,000 deductible per occurrence).

The City maintains a separate self insurance fund for payment of third party claims against the general fund and certain utilities (not including the Water System).

Financial Policies

Tacoma Water has formally adopted certain goals as a guide to financial management and rate setting. These goals are included in the Water Rate Policies and are periodically reviewed and approved by the Board and City Council after any modification. These goals include rates based on cost of service within a customer class, restrictions on the term of debt, a minimum of 50% of routine capital financed with current revenues, long term major projects are financed through debt, and maintenance of a minimum of 45 days of operating cash. The policies provide that water rates must be designed to adequately fund acquisition of new resources and conservation and that long-term capital projects will be financed through debt. The Board and City Council approved the amended Water Rate Policy in January 2003.

Tacoma Water operates under the guidance of a ten year business plan, which was most recently revised in 2008 to cover the period 2009 through 2018. This plan identifies key planning goals and customer, operational, and capital programs that the utility must address. The plan also addresses financing and rate requirements necessary to support the implementation of the operations and capital programs. This document serves as the basis for developing Tacoma Water's budget and is reviewed by the Board and City Council pursuant to budget and rate adjustment approval.

Labor Relations

Tacoma Water has approximately 280 employees, many of which are represented by Local 483-International Brotherhood of Electrical Workers ("IBEW"), one of the 11 labor organizations that represent City employees. Other units representing Tacoma Water employees include Local 117-Teamsters, Local 17-Professional and Technical Engineers, and Local 120-AFSCME. Negotiations with unions are done by a team chaired by a Human Resources Labor Relations staff member selected by the Human Resources Director who reports directly to the City Manager and Director of Utilities. Management of Tacoma Water strives to promote sound labor relations policies that are beneficial both to its operations and to its employees. This cooperative effort has precluded a significant work stoppage among utility employees for the last several decades, although there was an 11 day work stoppage by clerical members of IBEW, Local 483, in 1992.

As provided by state law, matters that are delegated by the City Charter to the City's Civil Service Board are established by law and are not negotiated at the bargaining table. Such matters include issues relating to tenure of employment, hiring, recruitment, and termination. Additionally, retirement benefits through the Tacoma City Employees' Retirement System historically have been set by the Tacoma Retirement Board, which includes representatives of City employees and retirees, as well as City management.

Investments

The investment of Tacoma Water's temporary excess funds is administered by the City Treasurer on behalf of the City's Finance Committee. The City has an investment policy that was last amended in August 2007 (the "Investment Policy"). The City Treasurer submits written reports of investment activity to the Finance Committee. The Finance Committee meets quarterly, and more often as needed.

In accordance with such Investment Policy, the City invests a portion of these excess funds in the Washington State Local Government Investment Pool (the "LGIP"). The Water System also currently invests its funds in the City's investment pool. The City Treasurer operates the investment portfolio as the Tacoma Treasury Investment Pool,

where each fund has an undivided interest in the pool and earnings are allocated daily to each fund. The City may invest in the following securities in accordance with State law: U.S. Treasury and Agency Obligations, Certificates of Deposits with qualified Washington State Public Depositories, Bankers Acceptances, Commercial Paper, Repurchase and Reverse Repurchase Agreements, and any other future investment authorized by State statute. The Investment Policy, which has been awarded the Certification for Excellence by the Municipal Treasurers' Association of the United States and Canada, establishes diversification requirements for each security type. The maturity of any individual security is limited to five years for operating funds and the average maturity of the portfolio may not exceed three years. Bond reserve accounts may be invested for longer periods. Reverse repurchase transactions are limited to 5% of the portfolio. The City does not borrow money for the primary purpose of investing.

The State Treasurer's Office administers the LGIP, a \$6.7 billion fund that invests money on behalf of more than 632 participants (as of December 31, 2008). In its management of LGIP, the State Treasurer is required to adhere, at all times, to the principles appropriate for the prudent investment of public funds. These are, in priority order, (i) the safety of principal; (ii) the assurance of sufficient liquidity to meet cash flow demands; and (iii) to attain the highest possible yield within the constraints of the first two goals. Historically, the LGIP has had sufficient liquidity to meet all cash flow demands.

The LGIP, authorized by chapter 43.250 RCW, is a voluntary pool which provides its participants the opportunity to benefit from the economies of scale inherent in pooling. It is also intended to offer participants increased safety of principal and the ability to achieve a higher investment yield than would otherwise be available to them. The pool is restricted to investments with maturities of one year or less, and the average life typically is less than 90 days. Investments permitted under the pool's guidelines include U.S. government and agency securities, bankers' acceptances, high quality commercial paper, repurchase and reverse repurchase agreements, motor vehicle fund warrants, and certificates of deposit issued by qualified Washington State depositories.

As of December 31, 2008, the City's cash and investments, on a fair value basis, totaled \$919.8 million, of which a portion was Tacoma Water funds. The portfolio was distributed in various types of investment instruments in the following percentages:

Bank Interest-Bearing Accounts	14.15%
LGIP	10.23
Municipal Securities	7.61
Federal Home Loan Mortgage Assn (Freddie Mac)	14.82
Federal Farm Credit Bank (Farm Credit)	17.47
Federal Home Loan Bank (Home Loan)	14.94
Federal National Mortgage Ass'n (Fannie Mae)	18.28
U.S. Treasuries	0.38
Secured Repurchase Agreements	0.95
Commercial Paper	1.15
Total	100.00%

THE WATER SYSTEM

Sources of Supply

The primary current source of supply for the Water System is a headworks diversion on the Green River approximately 30 miles east of the City, which is capable of supplying up to 165 MGD to Tacoma Water. Water withdrawn at the headworks is chlorinated, fluoridated, treated with ozone, and pH adjusted before being introduced into Pipeline No. 1 and the Second Supply pipeline. Pipeline No. 1 transports the water through or near the cities of Enumclaw, Buckley, Bonney Lake, Puyallup, and other urbanized areas before discharging it into McMillin Reservoir. The Second Supply pipeline transports the water through the cities of Black Diamond, Auburn, Federal Way, and Tacoma before discharging into Pipeline No. 4. The Green River diversion and pipeline were originally constructed in 1913. Over the years nearly all of the original pipeline has been replaced. The Second Supply Project became operational in October 2005 and is capable of supplying up to 95 MGD of additional water from the Green River.

The watershed, located above the diversion, consists of approximately 230 square miles of timbered and mountainous terrain. The U.S. Army Corps of Engineers constructed Howard Hanson Dam and Reservoir about three miles above the diversion in 1961. The dam currently provides flood control to the Green River valley and provides low flow augmentation to the river in the summer and fall months. The Army Corps is responsible for managing flood control. The Army Corps currently is engaged in major rehabilitation of the Howard Hanson Dam to maintain the structural integrity of the dam and assure future flood control and is responsible for associated costs.

In the 1970s, Tacoma Water drilled seven wells on the North Fork of the Green River (the “North Fork Wells”) approximately six miles upstream from the headworks. The North Fork Wells have been effective in maintaining the quality of Tacoma Water’s main water supply during high turbidity in the Green River source. The well water either blends with the river water or replaces the river water depending on the level of turbidity.

In addition to the North Fork Wells, Tacoma Water has a number of wells within its service area that can be used to meet peak summer water demands. During a typical year, approximately 95% of the Water System’s water supply is from the Green River and 5% is from these wells. The following table summarizes the water supplied by source during 2008 to meet the peak and average water requirements.

Tacoma Water Division
2008 Sources of Supply of the Water System
(MGD)

<u>Source</u>	<u>Peak Capacity</u>	<u>Peak Day Production</u>	<u>Average Production</u>
Surface Water Sources:			
Green River (1)	111.00	70.57	53.06
Groundwater Sources:			
South Tacoma Wells	43.90	16.03	1.28
Other Wells	15.00	0.00	-
Sub-Total Groundwater	58.90	16.03	1.28
Total Sources	169.90	86.60	54.34

(1) Adjusted for McMillin reservoir storage.

With the Second Supply Project described below, the Water System has sufficient water supply to meet its current customers and expected growth until at least 2050.

The Second Supply Project

Description of the Project. To meet its own future water supply requirements as well as to increase regional supply, in 1968 Tacoma Water began developing the Second Supply Project, which includes a second supply pipeline from Tacoma Water’s Green River resource (the “Second Supply Pipeline”). The Second Supply Project consists of the following components: (i) water from the exercise of Tacoma Water’s Second Diversion Water Right (up to 100 cubic feet per second) (“cfs”); (ii) the Second Supply Pipeline; (iii) improvements made at the Headworks diversion dam and intake; (iv) Second Supply Project fisheries and environmental enhancements; (v) the right to store water as a result of the Howard Hanson Dam Additional Storage Project; and (vi) Treatment Facilities (disinfection, pH adjustment, fluoridation, and ozone). The Second Supply Pipeline is approximately 34 miles long and varies from 48 to 90 inches in diameter. Its route follows a more northerly route than Tacoma Water’s existing Pipeline No. 1, traversing south King County and thereby making water available to the urbanized areas north and east of Tacoma. In addition to increasing water supply, the Second Supply Project increases flexibility and reliability of water delivery in both Tacoma Water’s and the other Participants’ service areas. The Second Supply Project became operational in October 2005. All components of the Second Supply Project are complete, with the exception of the Howard Hanson Dam additional water storage project, which is expected to be completed in 2016.

Tacoma, the City of Kent, Covington Water District, and Lakehaven Utility District (the “Participants”) participate in the Second Supply Project under the terms of the Second Supply Project Agreement, which defines their rights and obligations with regard to the Second Supply Project. Tacoma has a 15/36 Participant Share and each of the City of Kent, Covington Water District, and Lakehaven Utility District has a 7/36 Participant Share in the Second Supply Project. Generally, a Participant Share represents a Participant’s proportional right to receive and obligation to pay for water delivered by the Second Supply Project.

Second Supply Project Agreement and Repayment Agreement. The term of the Second Supply Project Agreement extends through the operating life of the Second Supply Project, including all renewals and replacements thereof and additions thereto. The Second Supply Project Agreement provides that all obligations incurred during its term will survive its termination or expiration, and will survive until satisfied. The term of the Repayment Agreement among the Participants continues until no Second Supply System Bonds are outstanding.

The Second Supply Project Agreement confers rights and imposes obligations on all four Participants, including Tacoma Water, and on Tacoma Water as operator of the Second Supply Project (the “Project Operator”). Each Participant has contractual rights under the Second Supply Project Agreement (i) to use an undivided share of the Second Supply Project equal to its project capacity share and to use available excess project capacity; (ii) to schedule for delivery and receive its Participant Share of Second Diversion Water at its points of delivery; (iii) to schedule for delivery and receive additional water at its points of delivery; and (iv) to provide its Participant share of storage. Each Participant has a contractual obligation (i) to receive Second Diversion Water and additional water scheduled for delivery by and delivered to it; and (ii) to pay its Participant Share of Project Costs as shown above.

As Project Owner and Operator, Tacoma Water is responsible for the day to day operation of the Second Supply Project and is obligated, consistent with the approved Project Annual Budget then in effect, to operate and maintain the Second Supply Project in a manner that is consistent with prudent utility practice. Tacoma Water also is responsible as Project Operator for, among other things, (i) monitoring the delivery of Project water to each Participant, and (ii) calibrating and testing for accuracy no less than once each year the master meter and all delivery meters.

Under the Second Supply Project Agreement, the Participant Share of a Participant that has been in default for a period of 60 days or more on any payment obligation under the Project Agreement (if that payment obligation includes amounts necessary for the City to make payments on any Project bonds) will be offered for assignment to the non defaulting Participants. In the event that other non defaulting Participants decline any or all of the defaulting Participant’s Participant Share, Tacoma Water will increase its Participant Share in an amount equal to the defaulting Participant’s Participant Share then remaining unassigned.

Financing. In October 2002, the City sold the Second Supply System Bonds in the principal amount of \$82,700,000. Tacoma Water is responsible for paying approximately 55% of the debt service on these bonds. The Second Supply Project is a separate utility system of the City. The City’s obligation to pay its share of costs of the Second Supply System is a Contract Reserve Obligation payable from Gross Revenues of the Water System as an Operation and Maintenance Expense of the Water System. The total project cost was approximately \$232 million, including financing costs. The remaining costs were paid for by the individual Participants through a combination of cash contributions and low interest loans. As discussed under “Water Quality and Treatment,” the City expects to issue debt beginning in 2011 to finance a water filtration project. Some of the bonds may be issued as Regional System Bonds. Currently, the Second Supply Project Participants are evaluating financing options for funding of future Regional Water Supply System capital projects.

Agreement with Cascade Water Alliance

Tacoma Water entered into an agreement with the Cascade Water Alliance (“Cascade”) that entitles Cascade to a permanent supply of four MGD of water (average daily demand) each year, and an additional guaranteed reserved supply of six MGD (average daily demand) through 2026, declining to one MGD (average daily demand) in 2030 (the “Additional Supply”), and discontinuing thereafter. Increased deliveries are available during peak season. The agreement includes minimum purchase requirements from 2009 through 2025, and entitles Cascade to additional temporary water, based on availability. The agreement required that Cascade pay system development charges and capacity reservation fees to Tacoma, in addition to paying for the metered water based on wholesale water rates.

Cascade is obligated to provide Tacoma with a plan by December 1, 2015 that demonstrates Cascade's ability to provide for the long term water needs of its Members; if Cascade does not do so, Tacoma may terminate its obligation to provide the Additional Supply. Termination for the reasons described in the previous sentence applies only to Additional Supply, and not to the permanent supply of four MGD (average daily demand).

Water Rights

Tacoma Water has water rights on the Green River in excess of its current needs, which include a Water Right Claim for 73 MGD (the "First Diversion Water Right") plus a Water Permit for the Second Diversion Water Right of up to 65 MGD. Second Diversion Water is available approximately 60% of the time because of the requirement to maintain minimum flows in the Green River. Water rights for the Water System's 30 wells, most of which are located within its water service area, total 87 MGD.

During the last decade it has become increasingly difficult for Washington State water systems to obtain new water rights because of uncertainties in the administration of these rights. Major concerns include legal challenges to the Washington State Department of Ecology's ("Ecology") authority to administer water rights and concern that the additional appropriation of water in many areas might deplete limited resources. At this time, there is no foreseeable near term resolution of this issue. Some water systems in King and Pierce counties have had a water moratorium in the recent past, restricting development. These circumstances make Tacoma Water's Second Diversion Water Right on the Green River for 65 MGD particularly valuable and attractive to the Participants in the Second Supply Project as well as potentially to other systems in the vicinity of Tacoma Water's existing transmission pipelines. These other systems have experienced occasional water shortages due to increased demands resulting from customer growth.

Endangered Species Act Compliance

In 1998, the National Marine Fisheries Service ("NMFS") listed Puget Sound Chinook salmon as a threatened species. Subsequently, the U.S. Fisheries & Wildlife Service ("USFWS") listed bull trout as a threatened species. Pursuant to regulations, NMFS and USFWS have extended to these threatened species the same level of protection the Endangered Species Act ("ESA") provides for endangered species. This level of protection includes a prohibition on "taking" the species, which may include not only harm to members of the species, but also adverse effects or destruction of habitat. This caused water utilities throughout the region to assess their potential liability under the ESA. Tacoma Water has approached these issues within a multi faceted response strategy. First, it developed a Habitat Conservation Plan under Section 10 of the ESA, which was approved by the NMFS and USFWS in 2001, to protect its source of supply operations on the Green River. The Habitat Conservation Plan provides authorization under the ESA for Tacoma's water supply operations on the Green River. Although the protection of the threatened Chinook salmon was the incentive for plan development, the Habitat Conservation Plan eventually was approved to provide coverage for 32 aquatic and terrestrial species. This significantly reduces the risk to Tacoma Water that future water supply operations may be disrupted due to ESA issues. Second, Tacoma Water has adopted a "take" avoidance strategy for its field operations on the water distribution system. Section 4(d) of the ESA allows certain categories of activities defined by federal rule to be conducted without "take" liability. In 2001, Tacoma Public Utilities obtained coverage under this provision for a wide variety of its utility maintenance activities by adopting and implementing the federally approved "Regional Road Maintenance Endangered Species Act Program Guidelines." Tacoma Water has modified its operation to obtain coverage under this program for many of its day to day operations.

Water Quality and Treatment

Watershed monitoring and protection programs are critical to ensuring high water quality. Well managed, unpopulated watersheds minimize potential adverse effects on the water supply. Tacoma Water has a well organized watershed control program with inspectors who patrol the watershed to protect against any unauthorized entry. Tacoma Water owns approximately 12% of the watershed area including much of the land adjacent to the Green River and the Howard Hanson Reservoir located approximately three miles upstream from the Green River Headworks. The land that is not owned by Tacoma Water is either U.S. Forest Service property or is owned by timber companies or the State Department of Natural Resources. There are no permanent residents living within the watershed boundaries. Tacoma Water, the timber companies, and the State Department of Natural Resources work

cooperatively to ensure that timber harvesting and other activities comply with watershed control best management practices, thereby minimizing any potential adverse impacts on water quality. Tacoma Water has in place agreements with all of the timber companies to document their commitment to use these best management practices.

Tacoma Water's Watershed Control Program has been approved by the Washington State Department of Health ("WSDOH") and allows the Water System's Green River supply to remain unfiltered, provided that Tacoma Water implements this program, submits regular monitoring reports, and meets the established water quality standards at all times. Tacoma Water meets all current requirements for the avoidance of filtration.

Tacoma Water adds chlorine, fluoride, ozone and sodium hydroxide (to raise the pH of the water) at the Green River Headworks. The water is slightly acidic, which tends to accelerate pipe corrosion, and could lead to unacceptable levels of lead and copper in the water without the corrosion control plant.

The water from most of Tacoma Water's wells is chlorinated before being introduced into the distribution system. The water quality is monitored on a regular basis in accordance with the requirements of the WSDOH and the U.S. Environmental Protection Agency ("U.S. EPA"). One of Tacoma Water's 30 wells is equipped with an air stripping tower to remove organic compound contamination, which was discovered during the early 1980s. This treatment maintains water quality by keeping contaminants in this water below the detectable limits. Contaminant levels in this groundwater source have also decreased as a result of the cleanup of the pollution source.

Tacoma Water meets or exceeds all current drinking water standards and regulatory obligations. Significant new regulations covering a variety of public health concerns have been issued. In addition to the treatment process improvements currently underway, the most significant new requirement affecting Tacoma Water will be the mandatory removal or disinfection of an organism called "Cryptosporidium." Tacoma Water and the Participants are evaluating whether to implement an ultraviolet light or filtration treatment project. The project is expected to commence in 2010 and be operational by 2016 at an estimated cost to Tacoma Water of \$47 million to \$94 million depending on the project chosen. The Participants in the Second Supply Project, including Tacoma Water, will be responsible for a share of the cost of the treatment project. The Water System expects to issue Parity Bonds beginning in 2011 to finance such treatment project.

Water System Security

Tacoma Water, along with many other major water utilities, is taking increased steps to protect its water supply facilities and to prevent contamination of the water supply. Tacoma Water has taken actions to secure the source of supply on the Green River through increased surveillance of watershed activities and closing additional areas to access. Security has been tightened regarding chemical deliveries to Tacoma Water facilities, additional monitoring of water quality has been initiated, and security provisions are reviewed on an ongoing basis to assure adaptive reaction to any changes in threat status. A system wide analysis was completed in early 2003 with the support of a U. S. EPA grant.

Water System Operations

Water Quality Section. The Water Quality Section of Tacoma Water is responsible for the development, operation, and maintenance of source water protection and treatment, monitoring, and regulatory reporting. The section must assure compliance with the federal Safe Drinking Water Act, as implemented through WSDOH regulations.

The Water Quality Section operates the Green River Intake for both water supplies and a new fish trap and sort facility. Major water quality and regulatory drivers have led to initiatives for significant investments in water treatment infrastructure. A new chemical treatment plant began operation in 2005, providing capacity for the Second Supply Project, and significantly improved safety and reliability for the addition of chlorine, fluoride, and sodium hydroxide. In 2007 ozone treatment was added to enhance system disinfection, eliminate seasonal poor taste and odor in the natural water, and reduce the levels of regulated chlorinated organic compounds that form after chlorine disinfection. The cost of this treatment was included in the Second Supply Project partnership agreement.

In addition to the Watershed and Treatment operations associated with the Green River supply, the Water Quality Section operates and maintains disinfection treatment equipment for the groundwater supplies and three reservoir locations.

Water Supply Section. The Water Supply Section has responsibility for water supply resources, water transmission lines larger than 24 inches in diameter, reservoirs within the distribution system, pumping stations, and pressure reducing valves. The Water Supply Section also has responsibility for overall Water System operations and it controls all elements of the Water System that are integral to Water System operations. Water System operations are managed from the Water Control Center, located in the Tacoma Water Distribution Center, which is staffed 24 hours a day.

Tacoma Water's water transmission and distribution system consists of 106 miles of transmission pipelines ranging in size from 28 to 96 inches in diameter, 23 booster pump stations, 188 million gallons of reservoir storage, and 1,006 miles of distribution pipeline ranging in size from 2 to 24 inches in diameter. The distribution system includes a number of pressure zones; most are supplied by reducing the pressure gradient from the McMillin Reservoir and the remainder require additional pumping of water to serve higher areas.

Tacoma Water's pipeline system delivers adequate supply for municipal use and fire protection throughout its service area. An independent evaluation conducted by the Washington Survey and Rating Bureau in 1997 found the condition of Tacoma Water's water facilities and the City's fire fighting capabilities to be very good. The Bureau makes the results of its evaluations available to the insurance industry which uses the information to determine, among other things, insurance rates for water systems. The overall score of the most recent evaluation, which included a survey of the City's fire department, was Class 2 on a scale of 1 to 10, with Class 1 being the highest or best score. Also, the evaluation indicated a significant improvement in the water supply sections of the review as compared to the previous evaluation conducted in 1976. Only four cities in the state received a score of Class 2; no cities received a Class 1 designation.

The storage available in the Water System is capable of supplying approximately three days at the average daily usage rate. To maintain better water quality within the Water System, storage was reduced by approximately 100 MG when the Second Supply Pipeline was placed in service.

Tacoma Water also has approximately 22 interties with 14 wholesale purveyor systems. Some of these interties are used to supply wholesale water to the systems on a regular basis and others are available for peak or emergency demands of these systems. In several instances, these interties are capable of providing Tacoma Water with a limited amount of emergency water supply.

Water Distribution Section. The Water Distribution Section is responsible for the maintenance of the distribution system, which includes all of the distribution mains, hydrants, valves, service connections, meters, and other distribution system features. Tacoma Water has made significant improvements during the last few years in its operations and maintenance programs. Starting with an emergency repair crew to address old hydrants and valves, Tacoma Water has created a permanent staff of 13 positions that constitute the Systematic Maintenance and Renewal Team ("SMART") program for replacing hydrants and valves and providing customer services in the older neighborhoods of the City.

Tacoma Water has implemented maintenance plans for all components of the water distribution system. Crews are scheduled to do routine and preventive maintenance activities for the system based on various operational criteria and customer concerns. This assures that resources are allocated cost effectively and based on objective priorities.

The Water Distribution Section has implemented a major water main replacement program. Beginning in 1995, Tacoma Water formalized this program and is currently funding it with \$4.0 million annually, which represents a significant increase over previous levels of expenditures. This program is addressing the replacement of the oldest pipelines in the Water System. The initial goal of the program was to achieve a replacement cycle for mains that averaged 100-years, while recognizing that the life of individual mains could be more or less. Subsequent cycles of evaluation of the program continue to refine the criteria for main replacement based on an evolving asset management structure.

The Water Distribution Section engineering staff also supports the operation and maintenance crews. This staff evaluates and approves permits for Water System extensions including developer installed systems. The section prepares the design of developer systems rather than simply approving a system designed by the developer's engineer, which is the more common approach taken by water utilities. Past benchmarking and cost analysis has shown that this approach not only assures a timely response and quality design for the developer but is less expensive than hiring a private engineering firm.

Washington State Department of Health/U.S. Environmental Protection Agency Requirements. Tacoma Water must comply with the requirements of the rules and regulations promulgated by the U.S. EPA pursuant to the Safe Drinking Water Act. WSDOH is delegated by U.S. EPA to administer these regulations in the State of Washington. In addition, WSDOH has rules and regulations for the design and operation of water systems. WSDOH provides oversight of water systems including reviews, approvals, and monitoring of performance.

Tacoma Water has a Comprehensive Water Plan (the "Plan"), which was approved by WSDOH in 2006. The Plan includes projections of future water demand requirements for several scenarios and presents an Integrated Resource Development Strategy for meeting future water demands. The Plan sets forth Tacoma Water's proposed program of supply development and system capital improvements. It also describes the financial plan for funding these improvements and includes required sections on emergency response and routine operations. This plan must be developed and resubmitted for approval every six years.

Customers, Water Sales, and Rates

Tacoma Water serves residential, commercial, and industrial customers, a special rate large industrial customer, municipal and other governmental customers, and wholesale customers. In 2008, revenues were attributed 67% to residential and domestic service, and 25% to commercial and industrial service, including the Simpson Tacoma Kraft Company ("Simpson"). The remaining approximately 8% was accounted for by service to municipal and other governmental customers and to wholesale customers.

Simpson is the largest customer of Tacoma Water and accounted for approximately 9% of total water billings in 2008. In 2008, the 10 largest customers combined accounted for 14.5% of the total billing.

Special Contract

In order to protect the interests of both the City and Simpson, a 10 year contract was finalized in 2006 and expires in 2015. The contract currently provides that the City will furnish 15.9 MGD to Simpson on a uniform basis, 24 hours a day. Tacoma Water encouraged conservation at the Simpson facility, and the current use rate of 15.9 MGD represents a significant improvement in water use efficiency over the 30 MGD used by the mill in previous years. Overall reduction in water use by the mill has been supported by Tacoma Water through the development of a contract amendment to provide rate incentives for conservation.

Water Rates

Washington State law provides that municipalities may establish water rates by action of the City Council, independent from review or approval by any state board or commission.

Tacoma Water's rate structure consists of two basic components, a monthly minimum and a monthly consumption charge. In addition, the City charges a one time system development charge on new services to more equitably distribute the costs associated with growth. As described under "Financial Policies," the Board has adopted a water rate policy that, among other provisions, provides that rates be set based on cost of service within a customer class.

The current water rates were implemented on January 19, 2009. The changes resulted in an average annual increase in water charges of approximately 4%. Rate increases since 2001 are summarized in the following table.

**Tacoma Water
Rate Increases**

Year	Average Annual Increase
2001	9.5%
2002	9.5
2003	8.2
2004	8.2
2005	8.0
2006	8.0
2007	7.5
2008	7.5
2009	3.9

In addition, the Board and City Council have approved a rate increase of 2.9% effective January 1, 2010.

Tacoma Water's current water rates are summarized in the table below.

**Tacoma Water
Current Water Rates and Charges**

Size of Meter (inches)	Customer Charge Per Month	
	Inside Tacoma	Outside Tacoma
5/8	\$ 15.07	\$ 18.08
3/4	22.61	27.13
1	37.68	45.22
1-1/2	75.35	90.42
2	120.56	144.67
3	226.05	271.26
4	376.75	452.10
6	753.50	904.20
8	1,205.60	1,446.72
10	1,733.05	2,079.66
12	2,543.06	3,051.67

Consumption Up to and Including:	Charge for Water Used per Month	
	Inside Tacoma	Outside Tacoma
Residential		
Each 100 cubic feet of consumption		
October through May	\$ 1.230	\$ 1.251
First 500 cubic feet of consumption		
June through September	1.230	1.251
Each 100 cubic feet of consumption over 500		
cubic feet June through September	1.538	1.564
Commercial and Industrial		
General	1.275	1.360
Large Volume (over 65,000 cubic feet		
annually)	1.094	1.206
Parks and Irrigation		
For each 100 cubic feet	1.547	1.698

Tacoma Water's charges for water service are competitive with those of other major water utilities in the Pacific Northwest as well as other regional water utilities. The results of a comparison of Tacoma Water's current rates with those of other water utilities located both in major metropolitan areas in the Pacific Northwest and in the greater Pierce County area are set forth in the following table.

Comparison of Average Monthly Water Bills

UTILITY	5/8" RESIDENTIAL (10 ccf/month)	2" COMMERCIAL (134 ccf/month)
Tacoma Water	\$ 27.37	\$ 285.38
Major Regional Water Systems:		
City of Bellevue, WA	38.74	411.93
City of Everett, WA	22.00	222.48
Eugene Water & Electric Board, OR	23.70	216.21
Portland, OR Water Bureau	46.53	373.32
Seattle Public Utilities	27.93	460.30
Neighboring Water Systems:		
City of Kent, WA	29.63	412.72
City of Puyallup, WA	22.29	308.25
Covington Water District, WA	39.49	459.19
Lakehaven Utility District, WA	15.32	164.55

Source: Individual Utilities. Off-peak season rates.

In 1990, Tacoma Water implemented a system development charge ("SDC"), which is a one time charge on new services. The charge is calculated for meters 3 inches or larger, based upon water use projections. The result of this new fee structure was an increase in SDC revenues. The SDC fees were developed to pay for approximately 50% of growth related capital costs. In addition, Tacoma Water periodically collects contributions from property owners that are restricted to specific capital projects. The table below does not include these contributions.

The following table shows annual funds collected from SDCs from 2004 through 2008.

Tacoma Water Annual SDC Revenue

Year	SDC Revenue
2004	\$5,039,355
2005	5,769,592
2006	12,688,488
2007	2,953,984
2008	1,754,475

CAPITAL IMPROVEMENT PROGRAM

Tacoma Water biennially prepares a ten-year business plan, which includes capital improvements, additions and renovations to the Water System necessary to address engineering recommendations, regulatory requirements and water quality standards and to provide for present and projected future customer needs. From this projection of need, Tacoma Water derives its Capital Improvement Program for the Water System. This program is an element of the City's Growth Management Act ("GMA") Comprehensive Plan, which contains a six-year projection of projects and is updated annually. The following table summarizes Tacoma Water's 2009-2014 Capital Improvement Program.

Tacoma Water
2009-2014 Capital Improvement Program
(\$000)

	2009	2010	2011	2012	2013	2014
Uses of Funds						
General Plant	\$ 1,403	\$ 1,343	\$ 569	\$ 569	\$ 569	\$ 569
Water Supply(1)	22,066	22,066	12,120	10,617	7,694	11,837
Water Quality	2,251	1,940	2,420	2,000	750	690
Water Distribution	15,590	15,590	17,454	17,454	17,954	17,954
Second Supply System Projects(2)	745	3,073	7,918	25,432	24,829	24,810
Environmental Stewardship	650	200	200	200	1,000	250
Total Uses	\$ 42,705	\$ 44,212	\$ 40,681	\$ 56,272	\$ 52,796	\$ 56,110

(1) Water supply numbers have been reduced based on received bids for the McMillin Reservoir project.

(2) Includes Tacoma Water's First Diversion and Second Supply System funding obligations with Treatment modeled at \$122 million.

Source: Water Division Capital Projects plan published in the 2009-2018 Business Plan.

The Water System plans to fund these improvements with a combination of revenues from operations, Water System development funds, proceeds from the Bonds and Future Parity Bonds, and other miscellaneous revenue. See "Water Quality and Treatment."

HISTORICAL OPERATING RESULTS

The following table shows Tacoma Water's customer accounts and water sales for the years 2004 through 2008.

Tacoma Water
Historical Number of Customers and Water Sales

	2004	2005	2006	2007	2008
Customer Accounts (Average)					
Residential	87,819	87,991	89,047	90,092	89,680
Commercial & Industrial Service	5,347	5,345	5,386	5,494	5,466
Simpson Tacoma Kraft(1)	1	1	1	1	1
Municipal	195	204	215	219	251
Other Public Buildings	511	472	437	454	442
Other Utilities	18	20	17	18	18
Total Customer Accounts	93,906	94,033	95,103	96,278	95,858
Water Sales (ccf)(1)					
Residential	12,476,513	11,351,952	12,140,488	11,409,873	11,018,505
Commercial & Industrial Service	4,079,709	4,049,305	4,097,122	4,043,797	3,963,159
Simpson Tacoma Kraft(2)	8,047,059	7,273,997	6,711,163	7,307,367	7,777,754
Municipal	150,459	120,495	129,879	134,007	97,056
Other Public Buildings	833,723	669,291	835,497	752,170	692,616
Other Utilities	1,631,807	1,464,800	1,379,466	1,112,968	851,377
Total Potable Water Sales	27,219,270	24,929,840	25,293,615	24,760,182	24,400,467

(1) ccf = 100 cubic feet.

(2) Simpson Tacoma Kraft is a pulp and paper mill with contracted annual usage of 15.9 MGD. See "THE WATER SYSTEM—Special Contract."

Source: Annual Tacoma Water financial reports.

Historical Revenue and Expenses

The following table shows selected historical revenues and expenses for the years 2004 through 2008. The following table is based on consolidated financial statements that include Tacoma Water and the Second Supply System.

Tacoma Water Historical Operating Results					
	2004	2005	2006	2007	2008
Operating Revenues					
Residential and Domestic	\$ 26,589,163	\$ 27,611,024	\$ 31,216,429	\$ 32,645,594	\$ 34,592,712
Commercial & Industrial	6,619,432	7,174,647	7,751,215	8,298,263	8,978,703
Special Rate—Simpson	3,293,335	3,511,199	3,222,324	3,917,760	4,371,527
Municipal	308,884	316,562	363,455	396,131	349,722
Other Public Bldgs. & Grounds	1,523,562	1,409,107	1,596,360	1,644,166	1,680,603
Unbilled	(903,969)	0	1,067,323	37,113	417,145
Sales to Other Water Utilities	1,622,206	1,599,919	1,640,803	1,433,705	1,251,815
Total Water Sales	\$ 39,052,613	\$ 41,622,458	\$ 46,857,909	\$ 48,372,732	\$ 51,642,227
Other Operating Revenues	792,302	1,428,135	1,919,802	4,353,478	5,382,313
Total Operating Revenue	\$ 39,844,915	\$ 43,050,593	\$ 48,777,711	\$ 52,726,210	\$ 57,024,540
Operating Expenses					
Operating & Maintenance (1)	\$ 25,590,407	\$ 26,448,761	\$ 29,165,168	\$ 31,076,515	\$ 33,387,663
Depreciation	8,934,860	9,386,363	11,556,821	11,363,970	13,016,544
Taxes	2,480,667	2,995,424	3,407,187	2,924,930	2,881,877
Total	\$ 37,005,934	\$ 38,830,548	\$ 44,129,176	\$ 45,365,415	\$ 49,286,084
Net Operating Income (Loss)	\$ 2,838,981	\$ 4,220,045	\$ 4,648,535	\$ 7,360,795	\$ 7,738,456
Non-Operating Revenue (Expenses)	\$ 1,190,100	\$ 2,841,371	\$ 2,293,477	\$ 306,680	\$ 61,265
Interest Income	1,484,779	1,695,578	4,603,137	5,255,881	3,730,407
Gain from Disposition of Property	4,500	4,622,927	0	4,199,382	0
Interest Charges (Net)	(6,253,392)	(7,185,197)	(8,403,448)	(8,484,405)	(8,406,264)
Total Non-Operating Income (Expense)	\$ (3,574,013)	\$ 1,974,679	\$ (1,506,834)	\$ 1,277,538	\$ (4,614,592)
Net Income (Loss) Before Capital Contributions	\$ (735,032)	\$ 6,194,724	\$ 3,141,701	\$ 8,638,333	\$ 3,123,864
Less: Regional Water Supply System Net Income (Loss) Before Capital Contributions	(1,255,530)	(484,221)	(3,302,056)	(2,928,543)	(2,115,659)
Net Tacoma Water Net Income (Loss) Before Capital Contributions	\$ 520,498	\$ 6,678,945	\$ 6,443,757	\$ 11,566,876	\$ 5,239,523
Debt Service Calculation Adjustments					
Less: Restricted Income	\$ (115,043)	\$ (138,874)	\$ (288,349)	\$ (784,445)	\$ (623,867)
Less: Restricted Sale of Land, Surplus	0	(4,622,927)	0	(4,200,000)	0
Add: Depreciation	8,934,860	6,455,591	8,143,480	7,850,529	8,212,995
Add: Interest Charges (Net)	3,314,830	3,411,166	4,220,331	4,399,711	4,323,860
Add: SDC Revenues (2)	5,039,355	5,769,592	12,688,488	2,953,984	1,754,475
Net Tacoma Water Revenue Available for Debt Service	\$ 17,694,500	\$ 17,553,493	\$ 31,207,707	\$ 21,786,655	\$ 18,906,986
Debt Service on Outstanding Bonds (3)	\$ 8,061,967	\$ 8,148,638	\$ 10,433,329	\$ 10,434,324	\$ 10,438,952
Debt Service Coverage	2.19x	2.15x	2.99x	2.09x	1.81x

(1) Regional Water Supply System debt service is included in operation and maintenance expenses and is not included in Debt Service below.

(2) Excludes contributions restricted to specific capital projects.

(3) Includes debt service on Tacoma Water Parity Bonds. Does not include debt service on Regional Water Supply System debt, which is included in Operation and Maintenance Expenses above.

The financial statements of Tacoma Water as of and for the years ended December 31, 2008 and 2007 are included as Appendix C to this Official Statement.

Recent Developments

Given the economic downturn in the region, Tacoma Water has instituted monthly and quarterly reporting on budget to actual water sales and billed revenue. Sales and revenues for the first six months of 2009 are tracking closely to projections for all customer classes. System development charge revenues have declined in 2008 through mid-2009 due to slower housing and commercial construction activity.

GENERAL AND ECONOMIC INFORMATION

Tacoma, the county seat of Pierce County (the “County”), is located in the west central part of Washington State near the southern tip of Puget Sound. It is the third largest city in the State with 2009 estimated population of 203,400. The City is located 32 miles south of Seattle and 28 miles northeast of Olympia, the State capital. The historical population of the City and Pierce County is shown in the following table.

POPULATION CITY OF TACOMA AND PIERCE COUNTY

<u>Year</u>	<u>Tacoma</u>	<u>Pierce County</u>
2009	203,400	813,600
2008	202,700	805,400
2007	201,700	790,500
2006	199,600	773,500
2005	198,100	755,900
2004	196,800	744,000
2003	196,300	733,700
2002	194,900	724,998
2001	194,500	713,398
2000	193,556	700,818

Source: Washington State Office of Financial Management estimates; U.S. Census for 2000 figure.

Following are economic indicators for the City and Pierce County.

PIERCE COUNTY MAJOR EMPLOYERS

Employer	Type of Business	Number of Employees
US Army Fort Lewis (Total)	Military	42,231
US Army Fort Lewis (Military)	Military	30,800
US Army Fort Lewis (Civilian)	Military	11,431
Local Public School Districts (K-12)	Education	13,736
US Air Force McChord (Total)	Military	10,301
US Air Force McChord (Civilian & Res.)	Military	6,818
US Air Force McChord (Military)	Military	3,483
Washington State Government	Government/Public Offices	7,889
Multicare Health System	Health Services	6,204
Franciscan Health System	Health Services	4,406
US Army Madigan Hospital (Total)	Military Health Care	4,023
US Army Madigan Hospital (Civilian)	Military Health Care	2,752
US Army Madigan Hospital (Military)	Military Health Care	1,271
Pierce County Government	Government/Public Offices	3,299
Washington State Higher Education	Education	2,912
Washington State National Guard	Military	2,476
City of Tacoma (excluding Tacoma Public Utilities)	Government/Public Offices	2,394
Fred Meyer Stores (includes part time employees)	Retail Store	2,321
Emerald Queen Casino	Casino Gambling	1,915
Wal-Mart	Retail	1,820
The Boeing Company (Frederickson Site)	Aerospace	1,537
US Postal Service	Government/Public Offices	1,482
Tacoma Public Utilities	Public Utility	1,313
Safeway Stores, Inc.	Grocery	1,261
Costco	Wholesale	1,134
State Farm Insurance Companies	Insurance	1,124
Russell Investments ⁽¹⁾	Investment Management	1,042
Intel Corporation	Computer Electronics	1,000

(1) Russell recently announced it is moving its headquarters to Seattle at the end of 2010.

Source: Economic Development Board of Tacoma-Pierce County, 2009.

CITY OF TACOMA BUILDING PERMIT ACTIVITY

Year	City of Tacoma	
	Total Number	Value
2009*	785	\$ 97,861,346
2008	2,146	343,884,905
2007	2,628	519,576,251
2006	2,746	482,193,083
2005	2,586	345,444,070
2004	2,441	323,424,589
2003	2,339	376,871,561
2002	2,556	297,617,993
2001	2,399	284,359,070
2000	2,614	287,741,638

* Data through June 2009.

Source: City of Tacoma Public Works Department, Building Division.

PIERCE COUNTY AND CITY OF TACOMA TAXABLE RETAIL SALES (\$000)

<u>Year</u>	<u>Pierce County</u>	<u>City of Tacoma</u>
2008	\$11,621,810	\$ 4,288,739
2007	12,449,284	4,665,527
2006	12,068,965	4,536,401
2005	11,177,879	4,218,012
2004	10,055,822	3,832,668
2003	9,448,120	3,708,718
2002	8,802,690	3,475,274
2001	8,510,487	3,527,642
2000	8,222,293	3,440,507

Source: Washington State Department of Revenue.

**PIERCE COUNTY AND WASHINGTON STATE
MEDIAN HOUSEHOLD INCOME**

<u>Year</u>	<u>Pierce County</u>	<u>Washington State</u>
2008(1)	\$58,903	\$60,010
2007(2)	57,733	59,119
2006	56,487	56,184
2005	55,669	54,085
2004	54,101	53,890
2003	51,644	50,846
2002	50,206	50,003
2001	49,342	49,364
2000	47,585	48,301

(1) Projected.

(2) Preliminary estimates.

Source: Washington State Office of Financial Management.

Income. Historic personal income and per capita income levels for Pierce County and the State are shown below:

**PIERCE COUNTY AND STATE OF WASHINGTON
TOTAL PERSONAL AND PER CAPITA INCOME**

<u>Year</u>	<u>Pierce County</u>		<u>State of Washington</u>	
	<u>Total Personal Income (\$000)</u>	<u>Per Capita Income</u>	<u>Total Personal Income (\$000)</u>	<u>Per Capita Income</u>
2007(1)	\$ 28,949,941	\$ 37,446	\$265,738,395	\$ 41,203
2006	27,149,797	35,551	245,764,517	38,639
2005	25,027,972	33,406	226,585,245	36,227
2004	23,426,242	31,604	218,431,726	35,347
2003	22,234,218	30,202	202,942,123	33,214
2002	21,502,845	29,519	197,451,578	32,606
2001	20,702,070	28,905	193,498,304	32,319
2000	19,416,742	27,582	187,853,404	31,780

(1) Last available data.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.

TACOMA METROPOLITAN AREA (PIERCE COUNTY)
RESIDENT CIVILIAN LABOR FORCE AND EMPLOYMENT AND AVERAGE CIVILIAN
NONAGRICULTURAL WAGE AND SALARY EMPLOYMENT

Employment within the County is described in the following tables:

NAICS Industry Title⁽¹⁾	Annual Average				
	2009(1)	2008	2007	2006	2005
Resident Labor Force					
Employment	364,920	372,530	366,370	355,500	348,540
Unemployment	38,900	22,510	18,080	19,100	21,700
Total	403,810	395,040	384,460	374,600	370,240
Percent Of Labor Force	9.6%	5.7%	4.7%	5.1%	5.9%
 Total Nonfarm	 269,800	 280,500	 280,900	 271,700	 263,800
Total Private	210,800	223,600	226,300	217,100	209,500
Goods Producing	37,200	43,700	46,300	43,400	40,800
Mining and Logging	400	400	500	400	400
Construction	19,800	23,500	25,400	22,900	20,600
Specialty Trade Contractors	13,000	15,000	16,000	14,000	12,600
Manufacturing	17,100	19,800	20,400	20,100	19,700
Services Providing	232,600	236,800	234,900	228,300	223,000
Trade, Transportation And Utilities	52,500	55,600	56,400	53,600	52,200
Wholesale Trade	10,700	11,400	11,400	10,500	10,200
Retail Trade	30,800	32,900	33,400	31,700	30,900
Food And Beverage Stores	5,200	5,500	5,400	5,300	5,200
General Merchandise Stores	7,600	7,400	7,500	6,700	6,600
Transportation, Warehousing And Utilities	10,900	11,400	11,600	11,500	11,100
Information	3,300	3,700	3,700	3,600	3,400
Financial Activities	12,800	13,300	13,700	14,500	14,300
Professional And Business Services	23,200	24,900	25,500	24,200	22,600
Admin, Support, Waste Mgmt & Remed.	12,700	14,300	15,200	14,400	13,600
Administrative And Support Services	11,000	12,900	13,800	13,300	12,600
Education And Health Services	42,800	41,600	40,500	39,100	38,300
Ambulatory Health Care Services	14,000	13,600	13,300	12,900	12,700
Hospitals	11,500	9,600	9,100	8,800	8,600
Leisure And Hospitality	26,600	27,800	27,400	26,400	26,000
Food Services And Drinking Places	21,100	22,100	22,100	21,200	20,900
Other Services	12,700	12,900	12,700	12,400	12,000
Government	59,000	56,900	54,900	54,600	54,300
Federal Government	11,500	10,800	10,300	10,500	10,200
State Government	12,200	11,900	11,400	11,200	11,400
State Government Educational Services	4,000	3,800	3,600	3,700	3,700
Local Government	35,300	34,300	33,300	32,900	32,800
Local Government Educational Services	19,200	18,200	18,000	18,000	18,200

(1) Average through June 2009.

Source: Washington State Employment Security Department.

INITIATIVE AND REFERENDUM

Under the State Constitution, the voters of the State have the ability to initiate legislation and modify existing legislation through the powers of initiative and referendum, respectively. The initiative power in Washington may not be used to amend the State Constitution. Initiatives and referenda are submitted to the voters upon receipt of a petition signed by at least 8% (initiative) and 4% (referenda) of the number of voters registered and voting for the office of Governor at the preceding regular gubernatorial election. Any law approved in this manner by a majority of the voters may not be amended or repealed by the Legislature within a period of two years following enactment, except by a vote of two-thirds of all the members elected to each house of the Legislature. After two years, the law is subject to amendment or repeal by the Legislature in the same manner as other laws.

LITIGATION CONCERNING THE BONDS AND TACOMA WATER

There is no litigation pending or threatened in any court (local, state, or federal) to restrain or enjoin the issuance or delivery of the Bonds, or questioning the creation, organization, existence, or title to office of the officers of the Department, the Water Division or the City, the Pledge of Net Revenue, the validity or enforceability of the Bond Ordinance, or the proceedings for the authorization, execution, sale, and delivery of the Bonds.

The City and Tacoma Water are parties to lawsuits in their normal course of business, but neither the City nor Tacoma Water believes that any of such litigation will have a significant adverse impact upon the financial condition of the City or Tacoma Water.

Regional Water Supply System, Department of Revenue Tax Issue. Tacoma Water is currently appealing a decision by the Department of Revenue that capital payments received from Tacoma's Second Supply Project partners during 1999 through 2002 are subject to the service and other activities business and occupation tax rate of 1.5 percent. The potential tax liability for the time period covered by the appeal period, 1999 through 2002, is approximately \$196,000. During 2003 through 2007, Tacoma Water received significant payments from its Second Supply Project partners for initial project construction, equaling a potential tax liability of approximately \$1,025,000. Additionally, future capital payments may be subject to a business and occupation tax rate of 1.5 percent.

Regional Water Supply System Construction Claim. Tacoma Water recently denied a construction claim submitted by a Second Supply Project contractor. Pending liability on the construction claim is projected at \$200,000 to \$3 million.

Public Fire Protection Cost Recovery. In response to an October 2008 Washington State Supreme Court ruling that public fire protection costs are the responsibility of general government, Tacoma Water removed these costs from the water rates effective January 19, 2009. Public fire protection costs were invoiced to the cities and counties served by Tacoma. Representatives from the larger entities (Pierce County and the cities of University Place and Federal Way) declined to pay these costs. Tacoma Water filed suit in Pierce County Superior Court to have its legal rights determined. Revenue owed to Tacoma Water is \$5.97 million for the 2009/2010 biennium. Approximately \$2.28 million is owed by the entities which have declined to pay.

TAX MATTERS

This advice was written to support the promotion or marketing of the Bonds. This advice is not intended or written by Foster Pepper PLLC to be used, and may not be used, by any person or entity for the purpose of avoiding any penalties that may be imposed on any person or entity under the U.S. Internal Revenue Code. Prospective purchasers of the Bonds should seek advice based on their particular circumstances from an independent tax advisor.

The following discussion generally describes certain aspects of the principal U.S. federal tax treatment of U.S. persons that are beneficial owners ("Owners") of Bonds who have purchased Bonds in the initial offering and who hold the Bonds as capital assets within the meaning of Section 1221 of the Code. For purposes of this discussion, a "U.S. person" means an individual who, for U.S. federal income tax purposes, is (i) a citizen or resident of the United States, (ii) a corporation, partnership or other entity created or organized in or under the laws of the United

States or any political subdivision thereof, (iii) an estate, the income of which is subject to U.S. federal income taxation regardless of its source of income, or (iv) a trust, if either: (A) a United States court is able to exercise primary supervision over the administration of the trust, and one or more United States persons have the authority to control all substantial decisions of the trust or (B) a trust has a valid election in effect to be treated as a United States person under the applicable treasury regulations.

This summary is based on the Internal Revenue Code of 1986, as amended to the date hereof (the “Code”), published revenue rulings, administrative and judicial decisions, and existing and proposed Treasury regulations (all as of the date hereof and all of which are subject to change, possibly with retroactive effect). This summary does not discuss all of the tax consequences that may be relevant to an Owner in light of its particular circumstances, such as an Owner who may purchase Bonds in the secondary market, or to Owners subject to special rules, such as certain financial institutions, insurance companies, tax-exempt organizations, non-U.S. persons, taxpayers who may be subject to the alternative minimum tax or personal holding company provisions of the Code, or dealers in securities. Accordingly, before deciding whether to purchase any Bonds, prospective purchasers should consult their own tax advisors regarding the United States federal income tax consequences, as well as tax consequences under the laws of any state, local or foreign taxing jurisdiction or under any applicable tax treaty, of purchasing, holding, owning and disposing of the Bonds.

In General. As described herein under the heading “THE BONDS—Designation of the Bonds as ‘Build America Bonds,’” the City has made irrevocable elections to have the Bonds treated as “Build America Bonds” within the meaning of Section 54AA(d) of the Code that are “qualified bonds” within the meaning of section 54AA(g) of the Code. As a result of these elections, interest on the Bonds is not excludable from the gross income of the Owners for federal income tax purposes, and Owners of the Bonds will not be allowed any federal tax credits as a result of ownership of or receipt of interest payments on the Bonds.

Payments of Interest. Interest paid on the Bonds will generally be taxable to Owners as ordinary interest income at the time it accrues or is received, in accordance with the Owner’s method of accounting for U.S. federal income tax purposes. Owners who are cash-method taxpayers will be required to include interest in income upon receipt of such interest payment; Owners who are accrual-method taxpayers will be required to include interest as it accrues, without regard to when interest payments are actually received.

Disposition or Retirement. Upon the sale, exchange or other disposition of a Bond, or upon the retirement of a Bond (including by redemption), an Owner will recognize capital gain or loss equal to the difference, if any, between the amount realized upon the disposition or retirement (excluding any amounts attributable to accrued but unpaid interest, which will be taxable as such) and the Owner’s adjusted tax basis in the Bond. Any such gain or loss will be United States source gain or loss for foreign tax credit purposes. If the City defeases any Bonds, such Bonds may be deemed to be retired and “reissued” for federal income tax purposes as a result of the defeasance. In such event, the Owner of a Bond would recognize a gain or loss on the Bond at the time of defeasance.

Backup Withholding. An Owner may, under certain circumstances, be subject to “backup withholding” (currently the rate of this withholding tax is 28%, but may change in the future) with respect to interest on the Bonds. This withholding generally applies if the owner of a Bond (a) fails to furnish the Bond Registrar or other payor with its taxpayer identification number; (b) furnishes the Bond Registrar or other payor an incorrect taxpayer identification number; (c) fails to report properly interest, dividends or other “reportable payments” as defined in the Code; or (d) under certain circumstances, fails to provide the Bond Registrar or other payor with a certified statement, signed under penalty of perjury, that the taxpayer identification number provided is its correct number and that the Owner is not subject to backup withholding. Any amount withheld may be creditable against the Owner’s U.S. federal income tax liability and be refundable to the extent it exceeds the Owner’s U.S. federal income tax liability.

The amount of “reportable payments” for each calendar year and the amount of tax withheld, if any, with respect to payments on the Bonds will be reported to the Owners and to the Internal Revenue Service.

ERISA Consideration

The Employees Retirement Income Security Act of 1974, as amended (“ERISA”), and the Code generally prohibit certain transactions between a qualified employee benefit plan under ERISA or tax-qualified retirement plans and

individual retirement accounts under the Code (collectively, the “Plans”) and persons who, with respect to a Plan, are fiduciaries or other “parties in interest” within the meaning of ERISA or “disqualified persons” within the meaning of the Code. All fiduciaries of Plans should consult their own tax advisors with respect to the consequences of any investment in the Bonds.

DESCRIPTION OF RATINGS

Moody’s and S&P have assigned ratings of “Aa3” and “AA,” respectively, to the Bonds. Ratings were applied for by the City and certain information was supplied by the City to the rating agencies to be considered in evaluating the Bonds. The ratings reflect only the views of the rating agencies and an explanation of the significance of the ratings may be obtained from the rating agencies. There is no assurance that the ratings will be retained for any given period of time or that the ratings will not be revised downward or withdrawn entirely by the rating agencies if, in their judgment, circumstances so warrant. Any such downward revision or withdrawal of the ratings would be likely to have an adverse effect on the market price of the Bonds.

UNDERWRITING

The Bonds are being purchased by Citigroup Global Markets Inc. (the “Underwriter”) at an aggregate price of \$76,262,240, which represents the principal amount of the Bonds, less an Underwriter’s discount of \$512,760. After the initial public offering, the public offering prices may be varied from time to time.

FINANCIAL ADVISOR

DashenMusselman Inc. has acted as financial advisor to Tacoma Water in connection with the issuance of the Bonds. The financial advisor has not audited, authenticated, or otherwise verified the information set forth in this Official Statement or the other information available from Tacoma Water with respect to the appropriateness, accuracy, and completeness of the disclosure of such information, and the financial advisor makes no guarantee, warranty, or other representation on any matter related to such information. DashenMusselman Inc. is an independent financial advisory and consulting organization and is not engaged in the business of underwriting, marketing, or trading of municipal securities or any other negotiable instruments.

APPROVAL OF COUNSEL

Legal matters incident to the authorization, issuance, and sale of the Bonds by the City are subject to the approving legal opinion of Foster Pepper PLLC, Seattle, Washington, Bond Counsel. The form of the opinion of Bond Counsel with respect to the Bonds is attached as Appendix D. The opinion of Bond Counsel is given based on factual representations made to Bond Counsel, and under existing law, as of the date of initial delivery of the Bonds, and Bond Counsel assumes no obligation to revise or supplement its opinion to reflect any facts or circumstances that may thereafter come to its attention, or any changes in law that may thereafter occur. The opinion of Bond Counsel is an expression of its professional judgment on the matters expressly addressed in its opinion and does not constitute a guarantee of result. Bond Counsel will be compensated only upon the issuance and sale of the Bonds.

Certain legal matters will be passed upon for the Underwriter by its counsel, K&L Gates LLP, Seattle, Washington, and any opinion of such counsel will be limited in scope, addressed solely to the Underwriter, and cannot be relied upon by investors.

LIMITATIONS ON REMEDIES

Any remedies available to the owners of the Bonds upon the occurrence of an event of default under the Bond Ordinance are in many respects dependent upon judicial actions, which are in turn often subject to discretion and delay and could be both expensive and time consuming to obtain. If the City fails to comply with its covenants under the Bond Ordinance or to pay principal of or interest on the Bonds, there can be no assurance that available remedies will be adequate to fully protect the interests of the owners of the Bonds.

In addition to the limitations on remedies contained in the Bond Ordinance, the rights and obligations under the Bonds and the Bond Ordinance may be limited by and are subject to bankruptcy, insolvency, reorganization, fraudulent conveyance, moratorium, and other laws relating to or affecting creditors' rights, to the application of equitable principles, and to the exercise of judicial discretion in appropriate cases. The opinion to be delivered by Foster Pepper PLLC, as Bond Counsel, concurrently with the issuance of the Bonds, will be subject to limitations regarding bankruptcy, insolvency, and other laws relating to or affecting creditors' rights. The various other legal opinions to be delivered concurrently with the issuance of the Bonds will be similarly qualified. A complete copy of the proposed form of opinion of Bond Counsel is set forth in Appendix D.

CONTINUING DISCLOSURE UNDERTAKING

Basic Undertaking to Provide Annual Financial Information and Notice of Material Events. To assist the Underwriter in meeting the requirements of United States Securities and Exchange Commission ("SEC") Rule 15c2-12(b)(5) (the "Rule"), as applicable to a participating underwriter for the Bonds, the City will undertake (the "Undertaking") for the benefit of holders of the Bonds to provide or cause to be provided, either directly or through a designated agent, to the Municipal Securities Rulemaking Board ("MSRB") in an electronic format as prescribed by the MSRB, accompanied by identifying information as prescribed by the MSRB, annual financial information and operating data of the type included in this Official Statement as generally described below ("annual financial information"); and to the MSRB timely notice of the occurrence of any of the following events with respect to the Bonds (as currently defined as follows or as redefined by MSRB in the future), if material: (i) principal and interest payment delinquencies; (ii) non payment related defaults; (iii) unscheduled draws on debt service reserves reflecting financial difficulties; (iv) unscheduled draws on credit enhancements reflecting financial difficulties; (v) substitution of credit or liquidity providers, or their failure to perform; (vi) adverse tax opinions or events affecting the tax exempt status of the Bonds; (vii) modifications to rights of holders of the Bonds; (viii) Bond calls (other than scheduled mandatory redemptions of Term Bonds for which notice is given pursuant to Exchange Act Release 34-23856); (ix) defeasances; (x) release, substitution, or sale of property securing repayment of the Bonds; and (xi) rating changes. The City also will provide to the MSRB timely notice of a failure by the City to provide required annual financial information on or before the date specified below.

Type of Annual Financial Information Undertaken to be Provided. The annual financial information that the City undertakes to provide will consist of (i) annual financial statements of Tacoma Public Utilities Water Division, which statements will include the Water Division Fund, prepared (except as otherwise noted therein) in accordance with the Budget Accounting and Reporting System presented by the Washington State Auditor pursuant to RCW 43.09.200 (or any successor statute), which statements will not be audited, except that if and when audited financial statements are otherwise prepared and available to the City they will be provided; (ii) principal amount of outstanding Parity Bonds and debt service coverage; (iii) water rates; and (iv) numbers of customers and water sales; and will be provided to the MSRB not later than the last day of the ninth month after the end of each fiscal year of the City (currently, a fiscal year ending December 31 as such fiscal year may be changed as required or permitted by State law, commencing with the City's fiscal year ending December 31, 2010).

The annual financial information may be provided in a single or multiple documents and may be incorporated by specific reference to documents available to the public on the Internet website of the MSRB or filed with the SEC.

Amendment of Undertaking. The Undertaking is subject to amendment after the primary offering of the Bonds without the consent of any holder of any Bond, or of any broker, dealer, municipal securities dealer, participating underwriter, rating agency, or the MSRB, under the circumstances and in the manner permitted by the Rule and with an opinion of bond counsel.

The City will give notice to the MSRB of the substance (or provide a copy) of any amendment to the Undertaking and a brief statement of the reasons for the amendment. If the amendment changes the type of annual financial information to be provided, the annual financial information containing the amended financial information will include a narrative explanation of the effect of that change on the type of information to be provided.

Termination of Undertaking. The City's obligations under the Undertaking shall terminate upon the legal defeasance, prior redemption, or payment in full of all of the Bonds. In addition, the City's obligations under the Undertaking shall terminate if those provisions of the Rule that require the City to comply with the Undertaking are

invalid, have been repealed retroactively, or otherwise do not apply in respect of the Bonds for any reason, as confirmed by an opinion of nationally recognized bond counsel to the City, and the City provides timely notice of such termination to the MSRB.

Remedy for Failure to Comply with Undertaking. No failure by the City or other obligated person to comply with the Undertaking will constitute a default in respect of the Bonds. The sole remedy of any holder or beneficial owner of a Bond will be to seek an order of specific performance from an appropriate court to compel the City or other obligated person to comply with the Undertaking.

Compliance with Continuing Disclosure Undertakings

The City has complied with all prior undertakings under the Rule.

MISCELLANEOUS

Any statements in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and are not a representation of fact. This Official Statement is not to be construed as an agreement or contract between the City and the purchasers or owners of any Bonds.

CITY OF TACOMA, WASHINGTON,
DEPARTMENT OF PUBLIC UTILITIES

By /s/ John Kirner
Superintendent of Water Division

By /s/ Robert K. Biles
Finance Director

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APPENDIX A

SUMMARY OF THE BOND ORDINANCE

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SUMMARY OF PRINCIPAL PROVISIONS OF THE BOND ORDINANCE

Following is a summary of the principal, substantive provisions of the Bond Ordinance, which summary is qualified in its entirety by reference to the complete text of the Bond Ordinance on file with the City Clerk of the City.

DEFINITIONS

As used in the Bond Ordinance, the following words have the following meanings:

“Accreted Value” means: (1) with respect to any Capital Appreciation Bonds, as of the time of calculation, the sum of the amount representing the initial principal amount of such Capital Appreciation Bonds as set forth in the applicable Parity Bond Authorizing Ordinance plus the interest accumulated, compounded and unpaid thereon as of the most recent compounding date, or (2) with respect to original issue discount bonds under the Code, as of the time of calculation, the amount representing the initial public offering price of such original issue discount bonds plus the amount of the discounted principal which has accreted since the date of issue, determined in accordance with the provisions of the applicable Parity Bond Authorizing Ordinance.

“Annual Debt Service” means, for any fiscal year of the Water System, all amounts required to be paid in respect of interest on and principal of Parity Bonds (excluding interest payments capitalized by Parity Bonds and excluding the accrued interest paid to the City upon the issuance of Parity Bonds) and Payment Agreement Payments in respect of Parity Payment Agreements, subject to the following:

Debt Service on Term Bonds. For purposes of calculating debt service on Term Bonds, only the scheduled mandatory redemption amounts payable in respect of principal of Term Bonds shall be taken into account in any fiscal year prior to the Term Bond Maturity Year, and only the principal amount scheduled to remain outstanding after payment of all prior mandatory redemption amounts shall be taken into account in the Term Bond Maturity Year;

Interest on Parity Bonds. For purposes of determining compliance with the Coverage Requirement, the Reserve Requirement and the conditions for the issuance of Future Parity Bonds or the creation of Contract Resource Obligations,

Generally. Except as otherwise provided with respect to Variable Interest Rate Bonds with respect to Parity Bonds with respect to which a Payment Agreement is in force, interest on any issue of Parity Bonds payable in a fiscal year shall be calculated based on the actual amount of accrued, accreted or otherwise accumulated interest that is payable in that fiscal year in respect of that issue taken as a whole, at the rate or rates set forth in the Parity Bond Authorizing Ordinance;

Interest on Variable Interest Rate Bonds. The amount of interest deemed to be payable on any issue of Variable Interest Rate Bonds shall be calculated on the assumption that the interest rate on those bonds would be equal to the rate (the “assumed RBI-based rate”) that is 90% of the average Bond Buyer Revenue Bond Index or comparable index during the fiscal quarter preceding the quarter in which the calculation is made; except that, for purposes of determining actual compliance with the Coverage Requirement in any past fiscal year, the actual amount of interest paid on any issue of Variable Interest Rate Bonds shall be taken into account;

Interest on Parity Bonds With Respect to Which a Payment Agreement or Parity Payment Agreement is in Force. Debt service on Parity Bonds with respect to which a Payment Agreement or Parity Payment Agreement is in force shall be based on the net economic effect on the City expected to be produced by the terms of the Parity Bonds and the terms of the Payment Agreement.

Interest on Parity Bonds designated as “Build America Bonds.” The interest on Parity Bonds designated as Build America Bonds, including the Bonds, for purposes of calculating the Reserve Requirement, shall be based on the net interest after the 35% federal credit payment or such other federal credit to be received for Future Parity Bonds. The owners of the Bonds shall be deemed to have consented to this subsection. This

subsection shall be in effect when 60% of the then current owners of Parity Bonds, including the Bonds, have consented to this amendment to the definition of Annual Debt Service.

“Average Annual Debt Service” means the sum of the Annual Debt Service for the remaining years to the last scheduled maturity of the applicable issue or issues of Parity Bonds divided by the number of those years.

“Bond Fund” means that special fund of the City known as the Water Revenue Bond Fund, created by Ordinance No. 25392 in the Water Division Fund of the City for the payment of the principal of, mandatory sinking fund payments and interest on the Parity Bonds.

“Bond Insurance” means any bond insurance, letter of credit, guaranty, surety bond or similar credit enhancement device providing for or securing the payment of all or part of the principal of and interest on any Parity Bonds.

“Bond Insurer” means any provider of Bond Insurance approved by the City Council by ordinance or resolution.

“Bond Register” means the books or records maintained by the Bond Registrar on which are recorded the names and addresses of the owners of each of the Bonds.

“Bond Registrar” means the Fiscal Agency.

“Build America Bonds” means any series of Parity Bonds to which the City irrevocably elects to have Section 54AA of the Code apply.

“Capital Appreciation Bonds” means any Parity Bonds, all or a portion of the interest on which is compounded and accumulated at the rates or in the manner, and on the dates, set forth in the applicable Parity Bond Authorizing Ordinance and is payable only upon redemption or on the maturity date of such Parity Bonds. Parity Bonds that are issued as Capital Appreciation Bonds, but later convert to obligations on which interest is paid periodically, shall be Capital Appreciation Bonds until the conversion date and thereafter shall no longer be Capital Appreciation Bonds, but shall be treated as having a principal amount equal to their Accreted Value on the conversion date.

“Code” means the Internal Revenue Code of 1986, as amended, together with corresponding final, temporary or proposed regulations and revenue rulings issued or amended with respect thereto by the U.S. Treasury Department or the Internal Revenue Service to the extent applicable to the Bonds.

“Contract Resource Obligation” means an obligation of the City, designated as a Contract Resource Obligation and entered into pursuant to the Bond Ordinance, to make payments for water supply, transmission or other commodity or service to another person or entity (including without limitation a separate utility system created pursuant to the Bond Ordinance). The Water System has designated the Regional System as a Contract Resource Obligation.

“Coverage Requirement” in any fiscal year of the Water System means an amount of Net Revenue of the Water System equal to at least 1.25 times the Annual Debt Service that year on all Parity Bonds.

“DTC” means The Depository Trust Company.

“Fiscal Agency” means the fiscal agency of the State of Washington in New York, New York, whose duties include registering and authenticating the Bonds, maintaining the Bond Register, transferring ownership of the Bonds, and paying principal and interest on the Bonds.

“Future Parity Bonds” means all revenue bonds and other obligations (including Parity Payment Agreements) of the City issued or entered into after the date of the issuance of the Bonds and then outstanding, the payment of which constitutes a charge and lien on the Net Revenue of the Water System equal in rank with the charge and lien upon such revenue required to be paid into the Bond Fund to pay and secure the payment of the principal of and interest on the Bonds and the Outstanding Parity Bonds.

“Gross Revenue of the Water System” or **“Gross Revenue”** means in any fiscal year of the Water System all of the revenues of the Water System, including but not limited to revenue from the sale or transmission of water; the sale, lease or furnishing of other commodities, services, properties or facilities; the imposition of connection, capital improvement or other charges; utility local improvement district assessments that are pledged to Parity Bonds; and earnings from the investment of money in the Water Division Fund. However, Gross Revenue shall not include earnings of the Regional System or any other separate utility system that may be acquired or constructed by the City pursuant to the Bond Ordinance; principal proceeds of Parity Bonds or other borrowing; grants for capital or other capital contributions; or earnings or proceeds from any investments in a trust, defeasance or escrow fund created to defease or refund Water System obligations (until commingled with other earnings and revenues of the Water System defined as Gross Revenue) or held in a special account for the purpose of paying a rebate to the United States government under the Code.

“Independent Consulting Engineer” means either (1) an independent licensed professional engineer experienced in the design, construction or operation or the development of rates and charges of municipal utilities of comparable size and character to the Water System, or (2) an independent certified public accountant or other professional consultant experienced in the development of rates and charges for municipal utilities of comparable size and character to the Water System.

“Letter of Representations” means the Blanket Letter of Representations from the City to DTC in the form on file with the Director of Finance.

“Maximum Annual Debt Service” means at the time of calculation, the maximum amount of Annual Debt Service that will mature or come due in the current year or any future year on the Parity Bonds.

“Net Revenue of the Water System” or **“Net Revenue”** means the Gross Revenue minus (1) Operation and Maintenance Expenses, (2) deposits into the Rate Stabilization Account and (3) proceeds from the sale of property of the Water System, and plus withdrawals from the Rate Stabilization Account.

“Operation and Maintenance Expenses” means all expenses incurred by the City in causing the Water System to be operated and maintained in good repair, working order and condition, including without limitation: deposits, premiums, assessments or other payments for insurance, if any, on the Water System; payments into pension funds; State-imposed taxes; amounts due under Contract Resource Obligations, including Regional Supply System costs, but only at the times described in the Bond Ordinance; payments made to any other person or entity for the receipt of water supply or transmission or other right, commodity or service; payments made to any other person or entity that are required in connection with the operation of the Water System or the acquisition or transmission of water and that are not subordinate to the lien of the Parity Bonds; and payments with respect to any other expenses of the Water System that are properly treated as operation and maintenance expenses under generally accepted accounting principles applicable to municipal corporations. Operation and Maintenance Expenses does not include any depreciation or taxes levied or imposed by the City, Payment Agreement Payments, or payments to the City in lieu of taxes, or capital additions or capital replacements to the Water System.

“Outstanding Parity Bonds” means the 2001 Bonds, the 2003 Bonds and the 2005 Bonds.

“Parity Bonds” means the Outstanding Parity Bonds, the Bonds and any Future Parity Bonds.

“Parity Bond Authorizing Ordinance” means the ordinance and/or resolution of the City that authorizes the issuance and sale and establishes the terms of a particular issue of Parity Bonds and other matters relating to the same plan of finance.

“Parity Payment Agreement” means a Payment Agreement under which the City’s payment obligations are expressly stated to constitute a charge and lien on the Net Revenue of the Water System equal in rank with the charge and lien upon such revenue required to be paid into the Bond Fund to pay and secure the payment of the principal of and interest on Parity Bonds.

“Payment Agreement” means a written agreement, for the purpose of managing or reducing the City’s exposure to fluctuations or levels of interest rates, currencies or commodities, or for other interest rate, investment, asset or liability management purposes, entered into on either a current or forward basis by the City and a Qualified Counterparty, all as authorized by any applicable laws of the State.

“Payment Agreement Payments” means the amounts periodically required to be paid by the City to the Qualified Counterparty pursuant to a Payment Agreement.

“Payment Agreement Receipts” means the amounts periodically required to be paid by the Qualified Counterparty to the City pursuant to a Payment Agreement.

“Plan of Additions” means the system or plan of additions to and betterments and extensions of the Water System described in the Bond Ordinance, as such plan of additions may be amended, updated, supplemented or replaced.

“Principal and Interest Account” means the account of that name created in the Bond Fund for the payment of the principal of and interest and mandatory redemption requirements, if any, on the Parity Bonds.

“Public Utility Board” means the board of that name created under the Tacoma City Charter.

“Qualified Counterparty” means a party (other than the City or a party related to the City) who is the other party to a Payment Agreement and (1)(a) whose senior debt obligations are rated in one of the three highest rating categories of each of the Rating Agencies (without regard to any gradations within a rating category) or (b) whose obligations under the Payment Agreement are guaranteed for the entire term of the Payment Agreement by a bond insurer or other institution which has been assigned a credit rating in one of the two highest rating categories of each of the Rating Agencies, and (2) who is otherwise qualified to act as the other party to a Payment Agreement under any applicable laws of the State.

“Rate Stabilization Account” means the fund of that name created in the Water Division Fund.

“Regional Supply System Costs” means with respect to each month all costs attributable to the Regional System, to the extent not paid from the proceeds of Parity Bonds or other sources, resulting from the ownership, operation, maintenance, and termination of, and repair, renewals, replacements, additions, improvements, betterments, and modifications to the Regional System, including, without limitation: (1) operating expenses; (2) the amount required to be paid into the bond fund for Regional System bonds; (3) any amount that the City may be required during such month to pay for the prevention or correction of any unusual loss or damage or for renewals, replacements, repairs, additions, improvements, betterments, and modifications that are necessary to keep the Regional System in good operating condition, to improve the operation thereof or to prevent a loss; and (4) all other charges or obligations against the revenues of the Regional System.

“Regional System” means the Regional Water Supply System, comprised of certain property and facilities to obtain and receive deliveries of water for the participants from the exercise by the City of the Second Diversion Water Right from the Green River and granted by the State of Washington Department of Ecology, which property and facilities include: (1) a Main Branch pipeline to Tacoma with a 72 MGD nominal capacity; (2) headworks improvements associated with the second diversion water right; (3) related fisheries and environmental enhancements; (4) improvements and additions to the Howard Hanson Dam to raise the summer storage pool to elevation of 1,167 feet in phase 1 to provide an additional 20,000 acre feet of water storage, together with improvements and additions related to accommodating fish passage; and (5) additional related water treatment facilities; and as the same will be added to, improved, and extended.

“Reserve Account” means the account of that name created in the Bond Fund for the purpose of securing the payment of the principal of and interest on the Parity Bonds.

“Reserve Insurance” means any bond insurance, letter of credit, guaranty, surety bond or similar credit enhancement device obtained by the City equal to part or all of the Reserve Requirement for any Parity Bonds which

is issued by an institution which has been assigned a credit rating at the time of issuance of the device in one of the two highest rating categories of each of the Rating Agencies.

“Reserve Requirement” means as of any date the lesser of Maximum Annual Debt Service or 125% of average Annual Debt Service on all the outstanding Parity Bonds. Once the 2001 Bonds are no longer outstanding, the Reserve Requirement for a series of Parity Bonds shall not exceed 10% of the net proceeds of such Bonds.

“Term Bond Maturity Year” means any calendar year in which Term Bonds are scheduled to mature.

“Term Bonds” means those Bonds designated as such in the Bond Sale Resolution and those Parity Bonds designated as such in the applicable Parity Bond Authorizing Ordinance.

“Variable Interest Rate” means any variable interest rate or rates to be borne by any Parity Bonds. The method of computing such a variable interest rate shall be as specified in the applicable Parity Bond Authorizing Ordinance, which ordinance or resolution also shall specify either (1) the particular period or periods of time or manner of determining such period or periods of time for which each value of such variable interest rate shall remain in effect or (2) the time or times upon which any change in such variable interest rate shall become effective. A Variable Interest Rate may, without limitation, be based on the interest rate on certain bonds or may be based on interest rate, currency, commodity or other indexes.

“Variable Interest Rate Bonds” means, for any period of time, any Parity Bonds that bear a Variable Interest Rate during that period, except that Parity Bonds shall not be treated as Variable Interest Rate Bonds if the net economic effect of interest rates on particular Parity Bonds of an issue and interest rates on other Parity Bonds of the same issue, as set forth in the applicable Parity Bond Authorizing Ordinance, or the net economic effect of a Payment Agreement with respect to particular Parity Bonds, in either case is to produce obligations that bear interest at a fixed interest rate; and Parity Bonds with respect to which a Payment Agreement is in force shall be treated as Variable Interest Rate Bonds if the net economic effect of the Payment Agreement is to produce obligations that bear interest at a Variable Interest Rate.

“Water Division Fund” means Fund No. 4600 of the City, or any successor fund or funds, into which is paid the Gross Revenue of the Water System.

“Water System” means the water system of the City as it now exists, and all additions thereto and betterments and extensions thereof at any time made for so long as any of the Parity Bonds are outstanding. The Water System shall not include the Regional System or any other water supply or service or other facilities that may be created, acquired or constructed by the City as a separate utility system as provided in the Bond Ordinance.

“2001 Bonds” means the City’s Water System Revenue Refunding Bonds, 2001, issued in the original principal amount of \$32,900,000 pursuant to Ordinance No. 26849.

“2003 Bonds” means the City’s Water System Revenue and Refunding Bonds, 2003, issued in the original principal amount of \$51,380,000 pursuant to Ordinance No. 27109.

“2005 Bonds” means the City’s Water System Revenue and Refunding Bonds, 2005, issued in the original principal amount of \$46,550,000 pursuant to Ordinance No. 24705.

PAYMENT OF AND SECURITY FOR THE BONDS

Bond Fund. The Bond Fund has been created in the Water Division Fund and is divided into two accounts: the Principal and Interest Account and the Reserve Account. So long as any Parity Bonds are outstanding, the City is required to set aside and pay into the Bond Fund out of the Net Revenue, certain fixed amounts without regard to any fixed proportion, namely:

(a) Into the Principal and Interest Account on or before each interest or principal and interest payment date of any Parity Bonds at least an amount which, together with other money on deposit therein, will be sufficient

to pay the interest, or principal and interest, to become due and payable on the Parity Bonds on that payment date, including any Parity Bonds subject to mandatory redemption on that date, and net payments due on Parity Payment Agreements; and

(b) Into the Reserve Account the Reserve Requirement for the Bonds. The City may at any time provide all or any part of the Reserve Requirement through Reserve Insurance, and the amount available to be drawn upon under that Reserve Insurance shall be credited against the Reserve Requirement, subject to the following:

Reserve Insurance shall not be cancelable on less than three years' notice. On receipt of a notice of cancellation of any Reserve Insurance or upon notice that the entity providing the Reserve Insurance no longer meets the requirements of the Bond Ordinance, the City shall substitute Reserve Insurance in the amount required to make up the deficiency created in the Reserve Account or in the alternative shall create a special account in the Water Division Fund and deposit therein, on or before the 25th day of each of the 36 succeeding calendar months (commencing with the 25th day of the calendar month next following the date of the notice) 1/36th of the amount sufficient, together with other money and investments on deposit in the Reserve Account, to equal the Reserve Requirement in effect as of the date the cancellation or disqualification of the entity becomes effective. Those amounts shall be deposited in the special account from money in the Water Division Fund after making provision for payment of Operation and Maintenance Expenses and for required payments into the Bond Fund. Amounts on deposit in that special account shall not be available to pay debt service on Parity Bonds or for any other purpose of the City, and shall be transferred to the Reserve Account on the effective date of any cancellation of a Reserve Insurance to make up all or part of the deficiency caused thereby. Amounts in that special account or in the Reserve Account may be transferred back to the Water Division Fund and used for any purpose if and when qualifying Reserve Insurance is obtained.

Except for withdrawals therefrom and payments over time as authorized by the Bond Ordinance, the Reserve Account is required to be maintained at the Reserve Requirement, as it is adjusted from time to time, at all times so long as any Parity Bonds are outstanding. For the purpose of determining the amount credited to the Reserve Account, obligations in which money in the Reserve Account has been invested shall be valued at the greater of cost or accreted value.

In the event that there shall be a deficiency in the Principal and Interest Account to meet maturing installments of either principal or interest or mandatory redemption requirements, as the case may be, that deficiency shall be made up from the Reserve Account by the withdrawal of cash or draws on the Reserve Insurance therefrom for that purpose. Any deficiency created in the Reserve Account by reason of any such withdrawal shall within 12 months be made up from Net Revenue available after making necessary provisions for the required payments into the Principal and Interest Account.

The money in the Reserve Account may be applied to the payment of the last outstanding bonds payable out of the Bond Fund, except that any money in the Reserve Account (including investment earnings) in excess of the Reserve Requirement may be withdrawn and deposited in the Principal and Interest Account and spent for the purpose of retiring Parity Bonds or may be deposited in any other fund or account and spent for any other lawful Water System purpose. When the total amount in the Bond Fund (including investment earnings) equals the total amount of principal and interest for all Parity Bonds to the last maturity thereof, no further payment need be made into the Bond Fund.

The City may provide for the purchase, redemption or defeasance of any Parity Bonds by the use of money on deposit in any account in the Bond Fund as long as the money remaining in those accounts is sufficient to satisfy the required deposits in those accounts for the remaining Parity Bonds.

All money in the Bond Fund may be kept in cash or invested in legal investments (including the City's investment pool) maturing, for investments in the Principal and Interest Account, not later than the dates when the funds are required for the payment of principal of or interest on the Parity Bonds and, for investments in the Reserve Account, maturing (or subject to redemption, or repurchase and redemption, at the option of the City) on a date not later than 15 years from the date of investment.

Earnings from investments in the Principal and Interest Account shall be deposited in that account. Earnings from investments in the Reserve Account shall be deposited in that account if necessary to meet the Reserve Account Requirement. Notwithstanding the provisions for the deposit of earnings, any earnings that are subject to federal arbitrage rebate requirements may be withdrawn from the Bond Fund for deposit into a separate fund or account created for the purpose of compliance with those rebate requirements.

If the City provides for all or part of the Reserve Requirement by Reserve Insurance, excess amounts in the Reserve Account may be withdrawn from that account and deposited either in the Principal and Interest Account and/or in the Water Division Fund, subject to applicable state law and federal law.

FGIC Reserve Account Surety Policies. Debt service reserve fund policies issued by Financial Guaranty Insurance Company (“FGIC”) were obtained for the 1997 Bonds, 2001 Bonds and 2005 Bonds. See “SECURITY FOR THE BONDS – The Reserve Policies” in the Official Statement.

FSA Reserve Account Surety Policy. A debt service reserve fund policy issued by Financial Security Assurance Inc. (“FSA”) was obtained for the 2003. See “SECURITY FOR THE BONDS – The Reserve Policies” in the Official Statement.

Rate Stabilization Account. There has previously been established in the Water Division Fund a Rate Stabilization Account. The City may at any time, as determined by the City and as consistent with the Bond Ordinance, deposit in the Rate Stabilization Account Gross Revenue and any other money received by the Water System and available to be used therefor, excluding principal proceeds of Parity Bonds or other borrowing. Net Revenue for a fiscal year shall not include deposits into the Rate Stabilization Account. The City may withdraw money from the Rate Stabilization Account for inclusion in the Net Revenue for any fiscal year of the Water System, except that (a) the total amount withdrawn from the Rate Stabilization Account in any fiscal year of the Water System may not exceed the total debt service of the Water System in that year; and (b) the Net Revenue in that fiscal year, disregarding the amounts withdrawn from the Rate Stabilization Account, must equal at least 1.0 times the Annual Debt Service that year on all Parity Bonds. Such deposits or withdrawals may be made up to and including the date 90 days after the end of the fiscal year for which the deposit or withdrawal will be included as Net Revenue for that fiscal year. Earnings from investments in the Rate Stabilization Account shall be deposited in that fund or another Water System fund and shall not be included as Net Revenue unless and until withdrawn from that fund as provided by the Bond Ordinance. No deposit of Gross Revenue shall be made into the Rate Stabilization Account to the extent that such deposit would prevent the City from meeting the Coverage Requirement in the relevant fiscal year.

Pledge of Net Revenue and Lien Position. The Net Revenue of the Water System and all money and investments held in the Bond Fund, the Rate Stabilization Account, and the Construction Fund (except money and investments held in a separate fund or account created for the purpose of compliance with rebate requirements under the Code), is pledged to the payment of the Parity Bonds and to make payments into the Reserve Account required by the Bond Ordinance and the Parity Bond Authorizing Ordinances, and this pledge shall constitute a lien and charge upon the Net Revenue prior and superior to any other charges whatsoever.

COVENANTS WITH BONDOWNERS

The City covenants and agrees with the owner of each Bond at any time outstanding, as follows:

Operation and Maintenance. It will at all times maintain, preserve and keep the properties of the Water System in good repair, working order and condition, will make all necessary and proper additions, betterments, renewals and repairs thereto, and improvements, replacements and extensions thereof, and will at all times operate or cause to be operated the properties of the Water System and the business in connection therewith in an efficient manner and at a reasonable cost.

Rate Covenants. It will establish, maintain and collect rates and charges for services and facilities provided by the Water System that will be fair and equitable, and will adjust those rates and charges from time to time so that:

The Gross Revenue will be sufficient to (i) pay all Operation and Maintenance Expenses, (ii) pay when due all amounts that the City is obligated to pay into the Bond Fund and the accounts therein, and (iii) pay all taxes, assessments or other governmental charges lawfully imposed on the Water System or the revenue therefrom or payments in lieu thereof and any and all other amounts which the City may now or hereafter become obligated to pay from the Gross Revenue by law or contract; and

The Net Revenue of the Water System in each fiscal year of the Water System will be at least equal to the Coverage Requirement; and

Failure of the City to comply with the rate covenants described above shall not be an Event of Default as defined in the Bond Ordinance if the City promptly retains an Independent Consulting Engineer to recommend to the City Council adjustments in the rates of the Water System necessary to meet those covenants and if the City Council adopts the recommended modifications within 180 days of the date the failure becomes known to the City Council.

Sale, Transfer or Disposition of the Water System. It will sell, transfer or otherwise dispose of any of the works, plant, properties, facilities or other part of the Water System or any real or personal property comprising a part of the Water System only upon approval by ordinance and only consistent with one or more of the following:

The City may exchange any of the works, plant, properties, facilities or other part of the Water System for works, plant, properties or facilities of substantially the same type, use and value; or

The City in its discretion may carry out such a sale, transfer or disposition (each, as used in this subparagraph, a “transfer”) if the facilities or property transferred are not material to the operation of the Water System, or shall have become unserviceable, inadequate, obsolete or unfit to be used in the operation of the Water System or are no longer necessary, material or useful to the operation of the Water System; or

The City in its discretion may carry out such a transfer if the aggregate depreciated cost value of the facilities or property being transferred under this subparagraph (3) in any fiscal year of the Water System comprises no more than 3% of the total assets of the Water System; or

The City may sell, lease, mortgage or otherwise dispose of the Water System, including all additions to and betterments and extensions thereof at any time made, that are used, useful or material in the operation of the Water System, if provision is made for the replacement thereof or if the City receives from the purchaser or transferee an amount equal to or greater than the greatest of the following:

(a) An amount which will be in the same proportion to the net amount of Bonds and Future Parity Bonds then outstanding (defined as the total amount of the Parity Bonds less the amount of cash and investments in the Bond Fund and accounts therein) that the Gross Revenue of the Water System from the portion of the Water System sold or disposed of for the preceding year bears to the total Gross Revenue of the Water System for that period; or

(b) An amount which will be in the same proportion to the net amount of Bonds and Future Parity Bonds then outstanding (as defined above) that the Net Revenue from the portion of the Water System sold or disposed of for the preceding year bears to the total Net Revenue of the Water System for such period; or

(c) An amount which will be in the same proportion to the net amount of Bonds and Future Parity Bonds then outstanding (as defined above) that the depreciated cost value of the portion of the Water System sold or disposed of bears to the depreciated cost value of the entire Water System immediately prior to such sale or disposition.

The amount required to be paid to the City under this section may be reduced by any “equity credits” or similar amounts based on prior capital contributions or other payments to the City which, under any contract between the City and the purchaser or transferee, are allowed as a setoff against the purchase or transfer price that would otherwise be payable to the City.

The City may accept from the purchaser or transferee the amount calculated as described above, payable, with interest, amortized over the number of years of remaining life of the portion of the Water System sold or disposed of or such shorter period of time as determined by the City. However, the contract of transfer or sale must provide that the payments to the City shall be either superior to or equal to the lien on the revenues of the purchaser or transferee of all other obligations of the purchaser or transferee.

No Free Service. Except to aid the poor or infirm and for fire-fighting purposes and if the City elects to provide free service for such purposes, it will not furnish or supply or permit the furnishings or supplying of any service or facility in connection with the operation of the Water System free of charge to any person, firm or corporation, public or private.

Liens Upon the Water System. Except as otherwise provided in the Bond Ordinance, it will not at any time create or permit to accrue or to exist any lien or other encumbrance or indebtedness upon the Gross Revenue or any part thereof, prior or superior to the lien thereon for the payment of the Parity Bonds, and will pay and discharge, or cause to be paid and discharged, any and all lawful claims for labor, materials or supplies which, if unpaid, might become a lien or charge upon the Gross Revenue or any part thereof, prior or superior to, or on a parity with, the lien of the Parity Bonds, or which might impair the security of the Parity Bonds.

Books and Accounts. It will keep proper books, records and accounts with respect to the operations, income and expenditures of the Water System in accordance with generally accepted accounting practices relating to municipal utilities and any applicable rules and regulations prescribed by the State, and will cause those books, records and accounts to be audited on an annual basis by the State Auditor (or, if such audit is not made by the State Auditor within 270 days after the close of any fiscal year of the Water System, by a certified public accountant selected by the City). It will prepare annual financial and operating statements as soon as practicable after the close of each fiscal year of the Water System showing in reasonable detail the financial condition of the Water System as of the close of the previous year, and the income and expenses for such year, including the amounts paid into the Bond Fund and into any and all special funds or accounts created pursuant to the provisions of the Bond Ordinance, the status of all funds and accounts as of the end of such year, and the amounts expended for maintenance, renewals, replacements and capital additions to the Water System. Such statements shall be sent to the owner of any Parity Bonds upon written request therefor being made to the City. The City may charge a reasonable cost for providing such financial statements.

Collection of Delinquent Accounts. On at least an annual basis, it will determine all accounts that are delinquent and will take such actions as the City determines are reasonably necessary to enforce payment of those delinquent accounts.

Maintenance of Insurance. It at all times will carry fire and extended coverage, public liability and property damage and such other forms of insurance with responsible insurers and with policies payable to the City on such of the buildings, equipment, works, plants, facilities and properties of the Water System as are ordinarily carried by municipal or privately owned utilities engaged in the operation of like systems, and against such claims for damages as are ordinarily carried by municipal or privately owned utilities engaged in the operation of like systems, or it will self-insure or will participate in an insurance pool or pools with reserves adequate, in the reasonable judgment of the City, to protect the Water System and the owners of the Parity Bonds against loss.

Condemnation Awards and Insurance Proceeds. If the City receives any condemnation awards or proceeds of an insurance policy in connection with any loss of or damage to any property of the Water System, it shall apply the condemnation award or insurance proceeds, in the City's sole discretion, either (i) to the cost of replacing or repairing the lost or damaged properties, (ii) to the payment, purchase or redemption of Parity Bonds, or (iii) to the cost of improvements to the Water System.

Tax Covenant. The City also will covenant in the Tax and Arbitrage Certification to be executed at closing that it will not take or permit to be taken on its behalf any action that would adversely affect the exclusion of the interest on the Bonds from the gross income of the recipients thereof for purposes of federal income taxation and will take or require to be taken such acts as may be permitted by State law and as may from time to time be required under applicable law to continue the exclusion of the interest on the Bonds from the gross income of the recipients thereof for purposes of federal income taxation.

PROVISIONS FOR FUTURE PARITY BONDS

The City reserves the right to issue Future Parity Bonds and to enter into Parity Payment Agreements for purposes of the Water System or to refund a portion of the Parity Bonds if the following conditions are met and complied with at the time of the issuance of those Future Parity Bonds or entering into the Parity Payment Agreement:

(a) There shall be no deficiency in the Bond Fund and no Event of Default shall have occurred and be continuing.

(b) The Parity Bond Authorizing Ordinance shall provide that all assessments and interest thereon that may be levied in any utility local improvement district created for the purpose of paying, in whole or in part, the principal of and interest on those Future Parity Bonds, shall be paid directly into the Bond Fund, except for any prepaid assessments permitted by law to be paid into a construction fund or account.

(c) The Parity Bond Authorizing Ordinance shall provide for the payment of the principal thereof and interest thereon out of the Bond Fund.

(d) The Parity Bond Authorizing Ordinance shall provide for the payment of amounts into the Bond Fund to meet mandatory redemption requirements applicable to any Term Bonds to be issued and for regular payments to be made for the payment of the principal of such Term Bonds on or before their maturity, or, as an alternative, the mandatory redemption of those Term Bonds prior to their maturity date from money in the Principal and Interest Account.

(e) The Parity Bond Authorizing Ordinance shall provide for the deposit into the Reserve Account of (i) an amount, if any, necessary to fund the Reserve Requirement upon the issuance of those Future Parity Bonds from Future Parity Bond proceeds or other money legally available, or (ii) Reserve Insurance or an amount plus Reserve Insurance necessary to fund the Reserve Requirement upon the issuance of those Future Parity Bonds, or (iii) amounts necessary to fund the Reserve Requirement from Net Revenue within five years from the date of issuance of those Future Parity Bonds, in five approximately equal annual payments.

(f) There shall be on file with the City either: a certificate of the Director of Finance demonstrating that during any 12 consecutive calendar months out of the immediately preceding 24 calendar months Net Revenue was at least equal to 1.25 times the projected Maximum Annual Debt Service for all Parity Bonds plus the Future Parity Bonds proposed to be issued; or a certificate of an Independent Consulting Engineer that in his or her opinion the Net Revenue will be at least equal to 1.25 times the projected Average Annual Debt Service for all Parity Bonds plus the Future Parity Bonds proposed to be issued. In providing that certificate, the Independent Consulting Engineer may take into account the following adjustments:

(i) Any changes in rates in effect and being charged, or rates expected to be charged in accordance with a program of specific rates, rate levels or increases in overall rate revenue approved by ordinance or resolution;

(ii) Net revenue from customers of the Water System who have become customers during the 12 consecutive month period or thereafter, and their estimate of net revenue from any customers to be connected to the Water System who have paid the required connection charges, adjusted to reflect one year's net revenue from those customers;

(iii) The Independent Consulting Engineer's estimate of customers anticipated to be served by facilities or improvements financed in substantial part by those Future Parity Bonds (or additional Parity Bonds expected to be issued during the five-year period); and

(iv) Net revenue from any person, firm, corporation or municipal corporation under any executed contract for water or other utility service, which revenue was not included in the historical Net Revenue of the Water System.

If the Future Parity Bonds proposed to be issued are for the sole purpose of refunding outstanding bonds payable from the Bond Fund, no such coverage certification shall be required if the Annual Debt Service on the Parity Bonds after the issuance of the Future Parity Bonds is not, for any year in which Parity Bonds are outstanding, more than \$5,000 over the Annual Debt Service on the Parity Bonds prior to the issuance of those Future Parity Bonds.

Nothing contained in the foregoing provisions relating to Future Parity Bonds shall prevent the City from issuing Future Parity Bonds to refund maturing Parity Bonds, money for the payment of which is not otherwise available, or revenue bonds that are a charge or lien upon the Gross Revenue subordinate to the charge or lien of the Parity Bonds, or from pledging the payment of utility local improvement district assessments into a bond redemption fund created for the payment of the principal of and interest on those junior lien bonds as long as such utility local improvement district assessments are levied for improvements constructed from the proceeds of those junior lien bonds.

SEPARATE UTILITY SYSTEMS; CONTRACT RESOURCE OBLIGATIONS

Separate Utility Systems. The City may create, acquire, construct, finance, own and operate one or more additional systems for water supply, transmission, treatment or other commodity or service. The Regional System has been created as a separate system. The revenue of any separate utility system shall not be included in the Gross Revenue of the Water System and may be pledged to the payment of revenue obligations issued to purchase, construct, condemn or otherwise acquire or expand the separate utility system. Neither the Gross Revenue nor the Net Revenue of the Water System shall be pledged by the City to the payment of any obligations of a separate utility system except (1) as a Contract Resource Obligation upon compliance with requirements of the Bond Ordinance relating thereto and/or (2), with respect to the Net Revenue, on a basis subordinate to the lien of the Parity Bonds on that Net Revenue.

Contract Resource Obligations. The City may at any time enter into one or more contracts or other obligations for the acquisition, from facilities to be constructed, of water supply, transmission, treatment or other commodity or service relating to the Water System. The City may determine that such contract or other obligation is a Contract Resource Obligation. The City's obligations with respect to the Regional System are a Contract Resolution Obligation. The City may provide that all payments under a Contract Resource Obligation (including payments prior to the time that water supply, transmission, treatment or other commodity or service is being provided, or during a suspension or after termination of supply or service) shall be Operation and Maintenance Expenses if the following requirements are met at the time such Contract source Obligation is entered into:

- (a) No Event of Default under the Bond Ordinance has occurred and is continuing; and
- (b) There shall be on file a certificate of an Independent Consulting Engineer stating that (i) the payments to be made by the City in connection with the Contract Resource Obligation are reasonable for the supply, transmission, treatment or other service rendered; (ii) the source of any new supply, and any facilities to be constructed to provide the supply, transmission, treatment or other service, are sound from a water or other commodity supply or transmission planning standpoint, are technically and economically feasible in accordance with prudent utility practice, and are likely to provide supply or transmission or other service no later than a date set forth in the Independent Consulting Engineer's certification; and (iii) the Net Revenue (further adjusted by the Independent Consulting Engineer's estimate of the payments to be made in accordance with the Contract Resource Obligation) for the five fiscal years following the year in which the Contract Resource Obligation is incurred, as such Net Revenue is estimated by the Independent Consulting Engineer (with such estimate based on such factors as he or she considers reasonable), will be at least equal to the Coverage Requirement.

Payments required to be made under Contract Resource Obligations shall not be subject to acceleration.

Nothing contained in the foregoing provisions relating to the Contract Resource Obligations shall be deemed to prevent the City from entering into other agreements for the acquisition of water supply, transmission, treatment or other commodity or service from existing facilities and from treating those payments as Operation and Maintenance Expenses of the Water System, or to prevent the City from entering into other agreements for the acquisition of water supply, transmission, treatment or other commodity or service from facilities to be constructed and from

agreeing to make payments with respect thereto, such payments constituting a lien and charge on Net Revenue subordinate to that of Parity Bonds.

ADVANCE REFUNDING OR DEFEASANCE OF BONDS

The City may issue advance refunding bonds pursuant to the laws of the State or use money available from any other lawful source to pay the principal of and interest on the Bonds, or such portion thereof included in a refunding or defeasance plan, as the same become due and payable and to redeem and retire, release, refund or defease the Bonds and to pay the costs of such refunding or defeasance. In the event that money and/or Government Obligations sufficient in amount, together with known earned income from the investments thereof, to redeem and retire, release, refund or defease the defeased Bonds in accordance with their terms, are set aside irrevocably in a special fund for and pledged irrevocably to such redemption, retirement or defeasance (the "trust account"), then all right and interest of the owners of the defeased Bonds in the covenants of the Bond Ordinance and in the Net Revenue and the funds and accounts pledged to the payment of such defeased Bonds, other than the right to receive the funds so set aside and pledged, thereafter shall cease and become void. Such owners thereafter shall have the right to receive payment of the principal of and interest or redemption price on the defeased Bonds from the trust account.

After the establishing and full funding of such a trust account, the City then may apply any money in any other fund or account established for the payment or redemption of the defeased Bonds to any lawful purposes as it shall determine, subject only to the rights of the owners of any other Parity Bonds.

If the refunding plan provides that the defeased Bonds to be issued be secured by money and/or Government Obligations pending the prior redemption of the defeased Bonds and if such refunding plan also provides that certain money and/or Government Obligations are pledged irrevocably for the prior redemption of the defeased Bonds included in that refunding plan, then only the debt service on the Bonds which are not defeased Bonds and the refunding bonds, the payment of which is not so secured by the refunding plan, shall be included in the computation of the Coverage Requirement for the issuance of Future Parity Bonds and the annual computation of the Coverage Requirement for determining compliance with the rate covenants.

AMENDATORY OR SUPPLEMENTAL ORDINANCES

The Bond Ordinance shall not be modified or amended in any respect subsequent to the initial issuance of the Bonds, except as provided in and in accordance with and subject to the provisions of the Bond Ordinance described in this section.

Without Bondowners' Consent. The City, from time to time, and at any time, without the consent of or notice to the registered owners of the Bonds, may pass supplemental or amendatory ordinances as follows:

- (1) To cure any formal defect, omission, inconsistency or ambiguity in the Bond Ordinance in a manner not adverse to the owner of any Parity Bond;
- (2) To impose upon the Bond Registrar (with its consent) for the benefit of the registered owners of the Bonds any additional rights, remedies, powers, authority, security, liabilities or duties which may lawfully be granted, conferred or imposed and which are not contrary to or inconsistent with the Bond Ordinance as theretofore in effect;
- (3) To add to the covenants and agreements of, and limitations and restrictions upon, the City in the Bond Ordinance, other covenants, agreements, limitations and restrictions to be observed by the City that are not contrary or inconsistent with the Bond Ordinance as theretofore in effect;
- (4) To confirm, as further assurance, any pledge under, and the subjection to any claim, lien or pledge created or to be created by the Bond Ordinance of any other money, securities or funds;

(5) To authorize different denominations of the Bonds and to make correlative amendments and modifications to the Bond Ordinance regarding exchangeability of Bonds of different authorized denominations, redemptions of portions of Bonds of particular authorized denominations and similar amendments and modifications of a technical nature;

(6) To modify, alter, amend or supplement the Bond Ordinance in any other respect that is not materially adverse to the registered owners of the Parity Bonds and that does not involve a change described under “With Bondowners’ Consent” below,

(7) Because of change in federal law or rulings, to maintain the exclusion from gross income of the interest on the Bonds from federal income taxation; and

(8) To add to the covenants and agreements of, and limitations and restrictions upon, the City in the Bond Ordinance, other covenants, agreements, limitations and restrictions to be observed by the City which are requested by a Bond Insurer or provider of Reserve Insurance and which are not materially adverse to the registered owners of the Parity Bonds.

Before the City shall adopt any such supplemental ordinance without Bondowners’ consent, there shall have been delivered to the City and the Bond Registrar an opinion of Bond Counsel, stating that such supplemental ordinance is authorized or permitted by the Bond Ordinance and, upon the execution and delivery thereof, will be valid and binding upon the City in accordance with its terms and will not adversely affect the exclusion from gross income for federal income tax purposes of interest on the tax-exempt Bonds.

With Bondowners’ Consent. Except for any supplemental ordinance entered into pursuant to the provisions described above, subject to the terms and provisions described below, registered owners of not less than 60% in aggregate principal amount of the Parity Bonds shall have the right from time to time to consent to and approve the passage by the City of any supplemental ordinance deemed necessary or desirable by the City for the purpose of modifying, altering, amending, supplementing or rescinding, in any particular, any of the terms or provisions contained in the Bond Ordinance; except that, unless approved in writing by the registered owners of all Parity Bonds, nothing contained in these provisions for amendatory or replacement ordinances shall permit, or be construed as permitting:

(i) A change in the times, amounts or currency of payment of the principal of or interest on any outstanding Parity Bond, or a reduction in the principal amount or redemption price of any outstanding Parity Bond or a change in the redemption price of any outstanding Parity Bond or a change in the method of determining the rate of interest thereon, or

(ii) A preference of priority of any Parity Bond or Bonds or any other bond or bonds, or

(iii) A reduction in the aggregate principal amount of Parity Bonds, the consent of the registered owners of Parity Bonds of which is required for any such supplemental ordinance.

If at any time the City shall pass any supplemental ordinance for any of the purposes described in this subsection, the Bond Registrar shall cause notice of the proposed supplemental ordinance to be given by first-class United States mail to all registered owners of the Parity Bonds, to any Bond Insurer, and to the Rating Agencies if the Bonds are rated by those agencies. Such notice shall briefly set forth the nature of the proposed supplemental ordinance and shall state that a copy thereof is on file at the office of the Bond Registrar for inspection by all registered owners of the Parity Bonds.

Within two years after the date of the mailing of such notice, the City may adopt such supplemental ordinance in substantially the form described in such notice, but only if there shall have first been delivered to the Bond Registrar (i) the required consents, in writing, of the registered owners of the Parity Bonds, and (ii) an opinion of bond counsel stating that such supplemental ordinance is authorized or permitted by the Bond Ordinance and, upon the execution and delivery thereof, will be valid and binding upon the City in accordance with its terms and will not adversely affect the exclusion from gross income for federal income tax purposes of interest on the Parity Bonds.

If registered owners of not less than 60% of the Parity Bonds shall have consented to and approved the execution and delivery thereof as provided by the Bond Ordinance, no owner of the Parity Bonds shall have any right to object to the passage of such supplemental ordinance, or to object to any of the terms and provisions contained therein or the operation thereof, or in any manner to question the propriety of the passage thereof, or to enjoin or restrain the City or the Bond Registrar from passing the same or from taking any action pursuant to the provisions thereof.

Upon the execution and delivery of any supplemental ordinance, the Bond Ordinance shall be, and be deemed to be, modified and amended in accordance therewith, and the respective rights, duties and obligations under the Bond Ordinance of the City, the Bond Registrar and all registered owners of Parity Bonds, shall thereafter be determined, exercised and enforced under the Bond Ordinance subject in all respects to such modifications and amendments.

DEFAULTS AND REMEDIES

Events of Default. The following shall constitute “Events of Default” with respect to the Bonds:

If a default is made in the payment of the principal of or interest on any of the Bonds when the same shall become due and payable.

If the City defaults in the observance and performance of any other of the covenants, conditions and agreements on the part of the City set forth in the Bond Ordinance or any covenants, conditions or agreements on the part of the City contained in any Parity Bond Authorizing Ordinance and such default or defaults have continued for a period of six months after the City has received from the Bondowners’ Trustee (as defined below) or from the registered owners of not less than 25% in principal amount of the Parity Bonds, a written notice specifying and demanding the cure of such default. However, if the default in the observance and performance of any other of the covenants, conditions and agreements is one which cannot be completely remedied within the six months after written notice has been given, it shall not be an Event of Default with respect to the Bonds as long as the City takes active steps within the 6 months after written notice has been given to remedy the default and is diligently pursuing such remedy.

If the City files a petition in bankruptcy or is placed in receivership under any state or federal bankruptcy or insolvency law.

Bondowners’ Trustee. So long as an Event of Default has not been remedied, a bondowners’ trustee (the “Bondowners’ Trustee”) may be appointed by the registered owners of 25% in principal amount of the Parity Bonds. That appointment shall become effective immediately upon acceptance thereof by the Bondowners’ Trustee. Any Bondowners’ Trustee shall be a bank or trust company organized under the laws of the State of Washington or the State of New York or a national banking association. The bank or trust company acting as Bondowners’ Trustee may be removed at any time, and a successor Bondowners’ Trustee may be appointed, by the registered owners of a majority in principal amount of the Parity Bonds. The Bondowners’ Trustee may require such security and indemnity as may be reasonable against the costs, expenses and liabilities that may be incurred in the performance of its duties.

In the event that any Event of Default in the sole judgment of the Bondowners’ Trustee is cured and the Bondowners’ Trustee furnishes to the City a certificate so stating, that Event of Default shall be conclusively deemed to be cured and the City, the Bondowners’ Trustee and the registered owners of the Parity Bonds shall be restored to the same rights and position they would have held if no Event of Default had occurred.

The Bondowners’ Trustee appointed in the manner provided by the Bond Ordinance, and each successor thereto, is declared to be a trustee for the registered owners of all the Parity Bonds and is empowered to exercise all the rights and powers conferred on the Bondowners’ Trustee by the Bond Ordinance.

Suits at Law or in Equity. Upon the happening of an Event of Default and during the continuance thereof, the Bondowners’ Trustee may, and upon the written request of the registered owners of not less than 25% in principal amount of the Parity Bonds outstanding shall, take such steps and institute such suits, actions or other proceedings, all as it may deem appropriate for the protection and enforcement of the rights of the registered owners of the Parity

Bonds, to collect any amounts due and owing to or from the City, or to obtain other appropriate relief, and may enforce the specific performance of any covenant, agreement or condition contained in the Bond Ordinance or in any of the Parity Bonds.

Nothing contained in the provisions of the Bond Ordinance relating to defaults and remedies shall, in any event or under any circumstance, be deemed to authorize the acceleration of maturity of principal on the Parity Bonds, and the remedy of acceleration is expressly denied to the registered owners of the Parity Bonds under any circumstances including, without limitation, upon the occurrence and continuance of an Event of Default.

Any action, suit or other proceedings instituted by the Bondowners' Trustee hereunder shall be brought in its name as trustee for the Bondowners for the ratable benefit of all of the registered owners of those Parity Bonds, subject to the provisions of the Bond Ordinance. The respective registered owners of the Parity Bonds, by taking and holding the same, shall be conclusively deemed irrevocably to appoint the Bondowners' Trustee the true and lawful trustee of the respective registered owners of those Parity Bonds, with authority to institute any such action, suit or proceeding; to receive as trustee and deposit in trust any sums becoming distributable on account of those Parity Bonds; to execute any paper or documents for the receipt of money; and to do all acts with respect thereto that the registered owner himself or herself might have done in person. Nothing in the Bond Ordinance shall be deemed to authorize or empower the Bondowners' Trustee to consent to accept or adopt, on behalf of any registered owner of the Parity Bonds, any plan of reorganization or adjustment affecting the Parity Bonds or any right of any registered owner thereof, or to authorize or empower the Bondowners' Trustee to vote the claims of the registered owners thereof in any receivership, insolvency, liquidation, bankruptcy, reorganization or other proceeding to which the City is a party.

Application of Money Collected by Bondowners' Trustee. Any money collected by the Bondowners' Trustee at any time shall be applied in the following order of priority:

first, to the payment of the charges, expenses, advances and compensation of the Bondowners' Trustee and the charges, expenses, counsel fees, disbursements and compensation of its agents and attorneys; and

second, to the payment to the persons entitled thereto of all installments of interest then due on the Parity Bonds in the order of maturity of such installments and, if the amount available shall not be sufficient to pay in full any installment or installments maturing on the same date, then to the payment thereof ratably, according to the amounts due thereon to the persons entitled thereto, without any discrimination or preference; and

third, to the payment to the persons entitled thereto of the unpaid principal amounts of any Parity Bonds which shall have become due (other than Parity Bonds previously called for redemption for the payment of which money is held pursuant to the provisions hereto), whether at maturity or by proceedings for redemption or otherwise, in the order of their due dates and, if the amount available shall not be sufficient to pay in full the principal amounts due on the same date, then to the payment thereof ratably, according to the principal amounts due thereon to the persons entitled thereto, without any discrimination or preference.

Duties and Obligations of Bondowners' Trustee. The Bondowners' Trustee shall not be liable except for the performance of such duties as are specifically set forth in the Bond Ordinance. During an Event of Default, the Bondowners' Trustee shall exercise such of the rights and powers vested in it hereby, and shall use the same degree of care and skill in its exercise, as a prudent person would exercise or use under the circumstances in the conduct of his or her own affairs. The Bondowners' Trustee shall have no liability for any act or omission to act hereunder except for the Bondowners' Trustee's own negligent action, its own negligent failure to act or its own willful misconduct. The duties and obligations of the Bondowners' Trustee shall be determined solely by the express provisions of the Bond Ordinance, and no implied powers, duties or obligations of the Bondowners' Trustee shall be read into the Bond Ordinance.

The Bondowners' Trustee shall not be required to expend or risk its own funds or otherwise incur individual liability in the performance of any of its duties or in the exercise of any of its rights or powers as the Bondowners' Trustee, except as may result from its own negligent action, its own negligent failure to act or its own willful misconduct.

The Bondowners' Trustee shall not be bound to recognize any person as a registered owner of any Bond until his title thereto, if disputed, has been established to its reasonable satisfaction.

The Bondowners' Trustee may consult with counsel and the opinion of such counsel shall be full and complete authorization and protection in respect of any action taken or suffered by it hereunder in good faith and in accordance with the opinion of such counsel. The Bondowners' Trustee shall not be answerable for any neglect or default of any person, firm or corporation employed and selected by it with reasonable care.

Suits by Individual Bondowners Restricted. Neither the registered owner nor the beneficial owner of any one or more of Parity Bonds shall have any right to institute any action, suit or proceeding at law or in equity for the enforcement of same unless:

an Event of Default has happened and is continuing; and

a Bondowners' Trustee has been appointed; and

such owner previously shall have given to the Bondowners' Trustee written notice of the Event of Default on account of which such suit, action or proceeding is to be instituted; and

the registered owners of 25% in principal amount of the Parity Bonds, after the occurrence of such Event of Default, has made written request of the Bondowners' Trustee and have afforded the Bondowners' Trustee a reasonable opportunity to institute such suit, action or proceeding; and

there have been offered to the Bondowners' Trustee security and indemnity satisfactory to it against the costs, expenses and liabilities to be incurred therein or thereby; and

the Bondowners' Trustee has refused or neglected to comply with such request within a reasonable time.

No registered owner or beneficial owner of any Parity Bond shall have any right in any manner whatever by his action to affect or impair the obligation of the City to pay from the Net Revenue the principal of and interest on such Parity Bonds to the respective owners thereof when due.

Payment Solely From Net Revenue and Certain Funds. Nothing in the provisions of the Bond Ordinance relating to defaults and remedies shall be deemed to require payment to Bondowners from any source other than the Net Revenue and money and investments in the funds pledged thereto by the Bond Ordinance.

PAYMENT AGREEMENTS AND PARITY PAYMENT AGREEMENTS

Calculation of Debt Service on Parity Bonds With Respect to Which a Payment Agreement Is in Force. Debt service on Parity Bonds with respect to which a Payment Agreement is in force shall be calculated based on the net economic effect on the City expected to be produced by the terms of the Parity Bonds and the terms of the Payment Agreement, including but not limited to the effects that (i) Parity Bonds that would, but for a Payment Agreement, be treated as obligations bearing interest at a Variable Interest Rate instead shall be treated as obligations bearing interest at a fixed interest rate, and (ii) Parity Bonds that would, but for a Payment Agreement, be treated as obligations bearing interest at a fixed interest rate instead shall be treated as obligations bearing interest at a Variable Interest Rate. Accordingly, the amount of interest deemed to be payable on any Parity Bonds with respect to which a Payment Agreement is in force shall be an amount equal to the amount of interest that would be payable at the rate or rates stated in those Parity Bonds plus Payment Agreement Payments minus Payment Agreement Receipts. For the purposes of calculating as nearly as practicable Payment Agreement Receipts and Payment Agreement Payments, under a Payment Agreement that includes a variable rate component determined by reference to a pricing mechanism or index that is not the same as the pricing mechanism or index used to determine the variable rate interest component on the Parity Bonds to which the Payment Agreement is related, it shall be assumed that the fixed rate used in calculating Payment Agreement Payments will be equal to 105% of the fixed rate specified by the Payment Agreement and that the pricing mechanism or index specified by the Payment Agreement is the same as the pricing mechanism or index specified by the Parity Bonds.

Debt Service on Parity Payment Agreements. No additional debt service shall be taken into account with respect to a Parity Payment Agreement for any period during which Payment Agreement Payments on that Parity Payment Agreement are taken into account in determining Annual Debt Service on related Parity Bonds. However, for any period during which Payment Agreement Payments are not taken into account in calculating Annual Debt Service on any outstanding Parity Bonds because the Parity Payment Agreement is not then related to any outstanding Parity Bonds, debt service on that Parity Payment Agreement shall be taken into account by assuming:

if the City is obligated to make Payment Agreement Payments based on a fixed rate and the Qualified Counterparty is obligated to make payments based on a variable rate index, that payments by the City will be based on the assumed fixed pay or rate, and that payments by the Qualified Counterparty will be based on a rate equal to the average rate determined by the variable rate index specified by the Parity Payment Agreement during the fiscal quarter preceding the quarter in which the calculation is made; and

if the City is obligated to make Payment Agreement Payments based on a variable rate index and the Qualified Counterparty is obligated to make payment based on a fixed rate, that payments by the City will be based on a rate equal to the average rate determined by the variable rate index specified by the Parity Payment Agreement during the fiscal quarter preceding the quarter in which the calculation is made, and that the Qualified Counterparty will make payments based on the fixed rate specified by the Parity Payment Agreement.

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APPENDIX B

BOOK-ENTRY SYSTEM

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BOOK-ENTRY SYSTEM

The following information has been provided by the Depository Trust Company, New York, New York (“DTC”). The City makes no representation regarding the accuracy or completeness thereof. Beneficial Owners (as hereinafter defined) should therefore confirm the following with DTC or the Participants (as hereinafter defined).

DTC will act as securities depository for the Bonds. The Bonds will be issued as fully-registered bonds registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Bond certificate will be issued for each maturity of the Bonds in the principal amount of each such maturity and will be deposited with DTC.

DTC, the world’s largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org.

Purchases of the Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC’s records. The ownership interest of each actual purchaser of each Bond (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owners entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of the Bonds with DTC and their registration in the name of Cede & Co., or such other DTC nominee, do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC’s records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

When notices are given, they shall be sent by the Bond Registrar to DTC only. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices shall be sent to DTC. If less than all of the Bonds are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the City as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Payments on the Bonds will be made to Cede & Co. or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Bond Registrar, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC (nor its nominee), the Bond Registrar, or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or any other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or the Bond Registrar, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC or any successor (the "Depository") may determine not to continue to act as securities depository for the Bonds, and the City may advise the Depository of its determination to discontinue book-entry of the Bonds through such Depository. If the City is unable to retain a qualified successor to the Depository or the City has determined that it is in the best interest of the City not to continue the book-entry system of transfer or that the interests of Beneficial Owners might be adversely affected if the book-entry system is continued, Bond certificates will be delivered to the Beneficial Owners or their nominees in registered form, in the denomination of \$5,000 or any integral multiple of \$5,000. In the event the book-entry system is discontinued, the persons to whom Bond certificates are delivered and in whose names the Bonds are registered will be treated as "bondowners" for all purposes of the Bond Ordinance.

With respect to Bonds registered on the Bond Register in the name of Cede & Co., as nominee of DTC, the City and the Bond Registrar shall have no responsibility or obligation to any Participant or to any person on behalf of whom a Participant holds an interest in the Bonds with respect to (i) the accuracy of the records of DTC, Cede & Co. or any Participant with respect to any ownership interest in the Bonds; (ii) the delivery to any Participant or any other person, other than a bondowner as shown on the Bond Register, of any notice with respect to the Bonds, including any notice of redemption; (iii) the payment to any Participant or any other person, other than a bondowner as shown on the Bond Register, of any amount with respect to principal of, premium, if any, or interest on the Bonds; (iv) the selection by DTC or any Participant of any person to receive payment in the event of a partial redemption of the Bonds; (v) any consent given action taken by DTC as registered owner; or (vi) any other matter. The City and the Bond Registrar may treat and consider Cede & Co., in whose name each Bond is registered on the Bond Register, as the holder and absolute owner of such Bond for the purpose of payment of principal and interest with respect to such Bond, for the purpose of giving notices of redemption and other matters with respect to such Bond, for the purpose of registering transfers with respect to such Bond, and for all other purposes whatsoever. For the purposes of this Official Statement, the term "Beneficial Owner" shall include the person for whom the Participant acquires an interest in the Bonds.

APPENDIX C

2008 AND 2007 FINANCIAL STATEMENTS

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES

TACOMA WATER

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FINANCIAL DATA

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INDEPENDENT AUDITOR'S REPORT

Chair and Members of the Public Utility Board
City of Tacoma, Washington Department of Public Utilities, Water Division
Tacoma, Washington

We have audited the accompanying balance sheets of City of Tacoma, Washington Department of Public Utilities, Water Division as of December 31, 2008 and 2007 and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Division's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of City of Tacoma, Washington Department of Public Utilities, Water Division as of December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis preceding the financial statements is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The statistical data and additional supplemental information following the financial statements and notes to the financial statements are also not a required part of the basic financial statements but are supplementary information provided for purposes of additional analysis. We did not audit or perform any other procedures on this information and express no opinion on it.

Moss Adams LLP

Portland, Oregon
May 15, 2009

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MANAGEMENT'S DISCUSSION AND ANALYSIS

The management of Tacoma Water (the Utility) offer readers of these financial statements this narrative overview and analysis of the financial activities of the Utility for the years ended December 31, 2008 and 2007. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues, provide an overview of the Utility's financial activities, and identify changes in the Utility's financial position. We encourage readers to consider the information presented here in conjunction with the financial statements and notes taken as a whole.

The management of the Finance Department of the City of Tacoma is responsible for preparing the accompanying financial statements and for their integrity. The statements were prepared in accordance with generally accepted accounting principles applied on a consistent basis and include amounts that are based on management's best estimates and judgments.

The basic financial statements, presented on a comparative basis for the years ended December 31, 2008 and 2007 include Balance Sheets; Statements of Revenues, Expenses and Changes in Net Assets; and Statements of Cash Flows. The Balance Sheets present information on all of the Utility's assets and liabilities, with the difference between the two reported as net assets. The Statements of Revenues, Expenses and Changes in Net Assets report all of the revenues and expenses during the time periods indicated. The Statements of Cash Flows provide information on cash receipts and disbursements during the year and report changes in cash resulting from operating, investing and financing activities.

The notes to the financial statements provide additional disclosures that are essential to a full understanding of the data provided in the financial statements. They are an integral part of the Utility's presentation of financial position, results of operations, and changes in cash flows.

Financial Highlights

- The assets of Tacoma Water exceeded its liabilities at the close of 2008 by \$404.0 million and 2007 by \$391.8 million. Of these amounts, \$8.2 million in 2008 and \$10.5 million in 2007 may be used to meet Tacoma Water's ongoing obligation to citizens and creditors.
- Tacoma Water's total net assets increased \$12.2 million in 2008 and \$16.9 million in 2007. The 2008 increase is largely attributed to resources from System Development Charges and donated assets by contractors. Private contractors donated \$5.6 million in 2008 and \$3.5 million in 2007.
- Tacoma Water's operating revenues equaled \$57.0 million, an increase of \$4.3 million or 8.2% in 2008 compared to 2007 operating revenues of \$52.7 million.
- In 2008, Tacoma Water's net utility plant of \$590.6 million increased by \$22.1 million or 3.9% over 2007's \$568.5 million balance.
- Tacoma Water's Long Term Liabilities decreased by \$8.4 million during the current fiscal year and decreased \$3.8 million during 2007. The key factor in the current fiscal year decrease was normal principal payments as no new debt was issued.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Utility's basic financial statements. Tacoma Water's basic financial statements are comprised of two components: 1) financial statements, 2) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

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For 2008, the Utility is reporting operating income of \$7.7 million compared to \$7.4 million in 2007 and \$6.7 million in 2006. The Utility's 2008 operating revenue increased 8.2% versus an 8.6% increase in operating expenses. Net income for 2008 is \$12.2 million compared to \$16.9 million in 2007 and \$29.3 million in 2006. Of the net income, capital contributions for 2008 were \$14.1 million compared to \$12.8 million in 2007 and \$30.5 million in 2006. Included in capital contributions are donated fixed assets; donated fixed assets were \$5.6 million in 2008, \$3.5 million in 2007 and \$4.5 million in 2006. There were 859 new meters installed for 2008 compared to 1,093 new meters installed in 2007 and 1,295 new meters installed for 2006. This trend of decline in the new meters installed is the result of the current housing market.

The following table highlights Tacoma Water's operating results for the years 2008 - 2006.

Operating Results (In thousands)

	2008	2007	2006	08/07 Increase (Decrease)	07/06 Increase (Decrease)
Operating Revenues	\$ 57,025	\$ 52,726	\$ 50,873	\$ 4,299	\$ 1,853
Operating Expenses	49,286	45,365	44,129	3,921	1,236
Operating Income	7,739	7,361	6,744	378	617
Net Non-Operating Income (Expenses)	(4,615)	1,278	(3,602)	(5,893)	4,880
Capital Contributions	14,137	12,801	30,462	1,336	(17,661)
Transfers Out	(5,014)	(4,563)	(4,302)	(451)	(261)
Change in Net Assets (Net Income)	\$ 12,247	\$ 16,877	\$ 29,302	\$ (4,630)	\$ (12,425)

Net Assets

Net assets may serve over time as a useful indicator of the Utility's financial position. Assets exceeded liabilities by \$404.0 million for 2008, \$391.8 million for 2007 and \$374.9 million for 2006. These changes in net assets representing net income resulted in an increase of \$12.2 million or 3.1% for the 2008/2007 change and \$16.9 million or 4.5% for the 2007/2006 change. Changes in all years are largely due to capital contributions. Capital contributions for 2008 were \$8.6 million for system development charges and \$5.6 million for donated fixed assets entirely from private contractors. In the year 2007, capital contributions were \$9.3 million for system development charges and \$3.5 million for donated assets all from private contractors. In the year 2006, capital contributions were \$25.9 million in cash contributions from customers and system development charges and \$4.5 million for donated fixed assets from which \$4.0 million were private contractors.

The investment in capital assets net of related debt or the Utility's equity investment in capital assets for 2008 is \$383.5 million, an increase of \$23.5 million or 6.5% over 2007. Investment in capital assets for 2007 was \$360.0 million, an increase of \$17.0 million or 5.0% over 2006's \$343.0 million.

Restricted net assets for 2008 were \$12.3 million, a decrease of \$8.9 million or 42.1% from 2007. Restricted net assets for 2007 were \$21.2 million, reflecting a decrease of \$2.9 million or 12.2% from the 2006 restricted net asset amount of \$24.2 million. The majority of decrease of restricted net assets was in the SDC fund. The Utility used system development charges to finance 2008 capital projects with the intent to reimburse with future bonds in 2009.

In 2008, unrestricted net assets were \$8.2 million, a decrease of \$2.3 million or 21.7% over 2007. Unrestricted net assets for 2007 were \$10.5 million, representing an increase of \$2.8 million or 36.5% from 2006's \$7.7 million amount.

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The analysis below highlights the changes in Tacoma Water's net assets for the years 2008, 2007 and 2006.

Tacoma Water's Net Assets (In thousands)

Description	2008	2007	2006	08/07 Increase (Decrease)	07/06 Increase (Decrease)
Net Utility Plant	\$ 591,141	\$ 569,041	\$ 543,386	\$ 22,100	\$ 25,655
Current and Other Assets	105,781	123,788	134,216	(18,007)	(10,428)
Total Assets	\$ 696,922	\$ 692,829	\$ 677,602	\$ 4,093	\$ 15,227

Net Assets:

Invested in Capital Assets, Net of Related Debt	\$ 383,507	\$ 360,036	\$ 343,020	\$ 23,471	\$ 17,016
Restricted	12,299	21,246	24,189	(8,947)	(2,943)
Unrestricted	8,204	10,481	7,677	(2,277)	2,804
Total Net Assets	404,010	391,763	374,886	12,247	16,877
Long-Term Liabilities	218,869	227,316	231,066	(8,447)	(3,750)
Current and Other Liabilities	74,043	73,750	71,650	293	2,100
Total Liabilities	292,912	301,066	302,716	(8,154)	(1,850)
Total Net Assets & Liabilities	\$ 696,922	\$ 692,829	\$ 677,602	\$ 4,093	\$ 15,227

Revenues

Water sales increased by \$3.3 million, or 6.8% in 2008 to \$51.6 million from \$48.4 million in 2007. Water sales increased by \$1.5 million or 3.2% in 2007 from 2006's \$46.9 million. Residential and domestic customers increased \$1.9 million in the 2008 due to an average 7.5% water rate increase over 2007 rates approved by the Public Utility Board and City Council effective January 1, 2008. Another notable increase was the \$0.5 million or 11.6% increase in 2008 and 21.6% in 2007 for the Simpson Tacoma Kraft Company under a new contract from August 1, 2005 through July 31, 2015.

Total operating revenues increased by \$4.3 million in 2008 to \$57.0 million from 2007, 76.1% was due to water sales. This increase resulted from an average water rate increase of 7.5%. The increase was \$1.9 million or 3.7% to \$52.7 million in 2007, up from \$50.9 million in 2006.

The following table highlights Tacoma Water's water sales by type of customer for 2008, 2007, and 2006.

Water Sales

(In thousands)

Type of Customer	2008	2007	2006	08/07 Increase (Decrease)	07/06 Increase (Decrease)
Residential and Domestic	\$ 34,593	\$ 32,646	\$ 31,218	\$ 1,947	\$ 1,428
Commercial and Industrial	8,979	8,298	7,751	681	547
Special Rate – Simpson Tacoma	4,372	3,918	3,222	454	696
Municipal	349	396	363	(47)	33
Other Public Buildings and Grounds	1,680	1,644	1,596	36	48
Sale to Other Utilities	1,252	1,434	1,641	(182)	(207)
Unbilled Revenue	417	37	1,067	380	(1,030)
Total	\$ 51,642	\$ 48,373	\$ 46,858	\$ 3,269	\$1,515

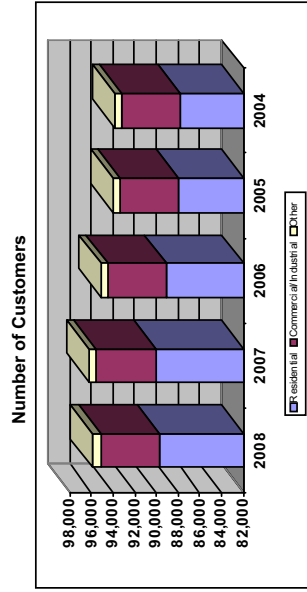
The largest portion of the Utility's revenues was from sales to residential customers. Approximately 67.0% of water sales were to residential customers in 2008, 67.5% for 2007 and 66.6% in 2006. Residential sales are followed by commercial and industrial sales at 17.4% for

2008, 17.2% for 2007 and 16.5% for 2006. Special rate sales to Simpson Tacoma Kraft represent 8.5% of total sales for 2008, 8.1% in 2007 and 6.9% in 2006.

Customers

Over the last five years, the overall number of customers had remained steady, growing at a rate of approximately 1.0% a year until the 2008 decline of 0.4%. In 2008, there were 95,858 customers of which 89,680 or 93.6% were residential. The remaining 5,466 or 5.7% were commercial and industrial, and 712 or 0.7% were other rate classes combined.

Below is a graphical representation of the number of customers by customer type for the last 5 years.



Expenses

Operating expenses in 2008 increased \$3.9 million or 8.6% compared to 2007. Operating expenses in 2007 increased \$1.2 million or 2.8% compared to 2006. In 2008, the largest increase was depreciation expense of \$1.7 million or 14.5% reflecting the \$22.1 million increase in net depreciable assets.

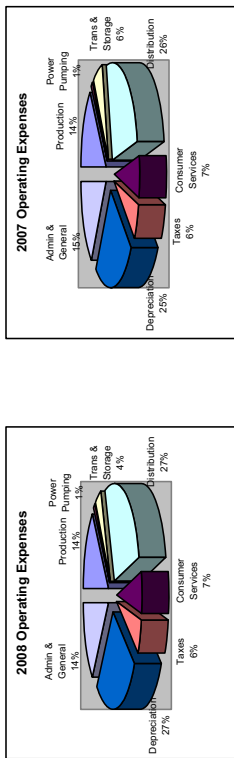
Other 2008 significant increases were in distribution expense by \$1.2 million or 10.3% and production expense of \$860,000 or 13.9%. Of the \$1.2 million increase in distribution expense in 2008, \$835,000 was labor and related benefit costs and \$240,000 was for fleet replacement fees.

The following table highlights Tacoma Water's operating expenses for 2008 – 2006.

Operating Expenses (in thousands)

Category	2008	2007	2006	08/07 Increase (Decrease)	07/06 Increase (Decrease)
Source of Supply	\$ 4,306	\$ 3,396	\$ 3,300	\$ 910	\$ 96
Water Treatment	2,743	2,793	2,558	(50)	235
Total Production Expense	7,049	6,189	5,858	860	331
Power Pumping Expense	343	361	253	(18)	108
Transmission and Storage Expense	2,151	2,615	2,704	(464)	(89)
Distribution Expense	13,223	11,990	11,720	1,233	270
Customer Accounting and Service	3,354	3,083	2,853	271	230
Taxes	2,882	2,925	3,407	(43)	(482)
Depreciation	13,016	11,364	11,557	1,652	(193)
Administrative and General	7,268	6,838	5,777	430	1,061
Total Operating Expenses	\$ 49,286	\$ 45,365	\$ 44,129	\$ 3,921	\$ 1,236

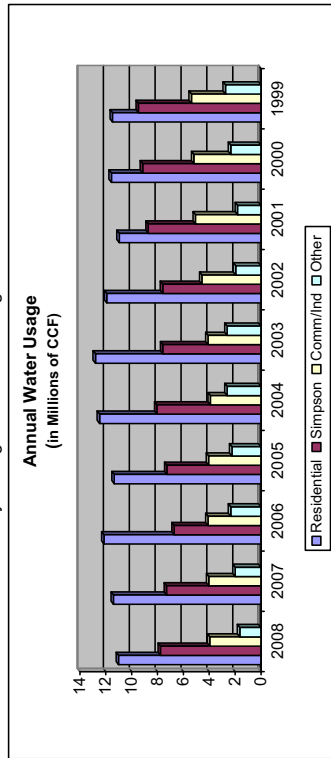
The following is a graphical presentation of Tacoma Water's operating expenses.



Water Users

The Utility generates the majority of its revenues from its residential customer base. Residential customers used 11.0 million CCF (100 cubic feet) or approximately 45.2% of the 24.4 million CCF of water consumed by the Utility's customers in 2008; Simpson Tacoma Kraft Company used approximately 7.8 million CCF or 31.9%; commercial and industrial customers used 4.0 million CCF or 16.2%. The remaining 1.6 million CCF or 6.7% was consumed by other customers.

Looking at the 10-year water usage trend, year 1999 was the highest with 29.08 million CCF, which declined over the next three years picking up in year 2003 with 27.06 million CCF. However, the trend shows a decline in usage over the next 5 years to current year usage of 24.4 million CCF. This trend can be explained by plumbing code changes, conservation activities and reduction of use by the high water consuming commercial/industrial users.



Capital Assets—Utility Plant

Tacoma Water has invested in a broad range of utility assets. At the end of 2008, Tacoma Water had \$590.6 million in net utility plant, an increase of \$22.1 million or 3.9% from 2007. At the end of 2007, Tacoma Water had \$568.5 million in net utility plant, an increase of \$25.7 million or 4.7% from 2006. In the current year, the distribution crews installed 1,435 new water services.

From year to year, the majority of Tacoma Water's capital is invested in distribution facilities; which make up \$282.7 million or 47.9% for 2008; \$259.1 million or 45.6% for 2007; and \$234.4

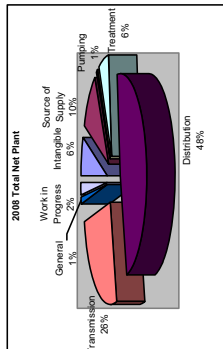
million or 43.2% for 2006. In addition, Tacoma Water added or replaced 23.7 miles of main in 2008; compared to 19.9 miles in 2007, and 19.1 miles in 2006.

The following table summarizes Tacoma Water's capital assets, net of accumulated depreciation, for the years ended December 31, 2008, 2007 and 2006.

Capital Assets, Net of Accumulated Depreciation (In thousands)

	Net Utility Plant	2008	2007	2006	08/07 Increase (Decrease)	07/06 Increase (Decrease)
Intangible Plant		\$ 34,845	\$ 34,795	\$ 34,803	\$ 50	\$ (8)
Source of Supply Plant		57,207	57,877	44,146	13,731	13,731
Pumping Plant		6,363	5,267	5,390	1,096	(123)
Water Treatment Plant		37,635	39,155	15,995	(1,520)	23,160
Transmission Plant		155,412	154,112	155,987	1,300	(1,875)
Distribution Plant		282,746	259,120	234,398	23,626	24,722
General Plant		6,457	5,313	6,260	1,144	(947)
Construction Work in Progress		9,928	12,854	45,859	(2,926)	(33,005)
Total		\$ 590,593	\$ 568,493	\$ 542,838	\$ 22,100	\$ 25,655

The following graph provides a visual presentation of the allocation of Tacoma Water's capital investment.



Debt Administration

As of year end 2008, the Utility had outstanding revenue bond obligations of \$192.3 million (net of unamortized bond premiums and deferred loss on refunding), a decrease of \$6.2 million or 3.2% from 2007 amounts. As of year end 2007, Tacoma Water had outstanding revenue bond obligations of \$198.5 million (net of unamortized bond premiums and deferred loss on refunding), a decrease of \$5.9 million or 2.9% from 2006 amounts. The Utility did not issue new bonds in 2006, 2007 or 2008.

All outstanding bonds are insured and rated Aaa by Moody's Investors Service and AAA by Standard & Poor's.

The Utility is required by its bond covenants to maintain a times debt service coverage of 1.25. In 2008, principal and interest were covered 3.08 times, in 2007, were covered 3.27 times, and in 2006, were covered 3.26 times.

During 2008, the Utility entered into Washington State Public Works Board Loan agreements for \$10 million and Drinking Water State Revolving Loan for \$4 million, although none were issued. These loans were for the McMillin Reservoir reconstruction. At the end of 2008, the Utility had an outstanding State loan balance of \$25.0 million, a decrease of \$1.7 million. At the end of

2007, Tacoma Water had an outstanding State loan balance of \$26.7 million, an increase of \$3.1 million from the 2006 balance of \$23.6 million.

Additional information on Tacoma Water's long-term debt can be found in Note 4 of the financial statements and in the supplementary Statistical Data.

Summary

The management of the Finance Department of the City of Tacoma is responsible for preparing the information in this annual report. We prepared the financial statements according to generally accepted accounting principles and they fairly portray Tacoma Water's financial position and operational results.

The financial statements have been audited by Moss Adams, LLP. We have made available to them all pertinent information necessary to complete the audit. Management considers and takes appropriate action on audit recommendations.

Management has established and maintains a system of internal controls, which includes organizational, administrative and accounting processes. These controls provide reasonable assurance that records and reports are complete and reliable, that assets are used appropriately and that business transactions are carried out as authorized.


William A. Gaines
Director of Utilities
Chief Executive Officer


Robert K. Biles
Finance Director

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

BALANCE SHEETS

	DECEMBER 31,	
	2008	2007
ASSETS		
UTILITY PLANT		
In Service, at Original Cost	\$ 705,571,558	\$671,605,223
Less - Accumulated Depreciation	(124,906,754)	(115,966,258)
Total	580,664,804	555,638,965
Construction Work In Progress	9,928,454	12,854,050
Net Utility Plant	590,593,258	568,493,015
NON-UTILITY PROPERTY, NET	547,541	547,541
SPECIAL FUNDS		
Construction Funds	13,930,776	20,251,838
Debt Service Funds	2,092,216	1,928,744
Bond Reserve Funds	5,884,382	5,851,669
Other - Investments	53,318,912	64,373,190
Notes & Contracts Receivable - SDC & Other	5,084,574	6,109,432
Total Special Funds	80,310,860	98,514,873
CURRENT ASSETS		
Operating Funds Cash and Equity in		
Pooled Investments	9,035,906	11,229,062
Accounts Receivable	5,418,276	5,073,383
(Net of Allowance for Doubtful Accounts		
of \$335,032 in 2008 and \$300,964 in 2007)		
Accrued Unbilled Revenues	3,591,571	3,174,427
Materials and Supplies	2,617,021	2,349,055
Receivables from Affiliates	455,711	95,023
Prepayments.....	1,032,982	1,229,285
Total Current Assets	22,151,467	23,150,235
DEFERRED CHARGES		
Unamortized Debt Expense	1,865,740	2,036,570
Other Deferred Charges	1,453,416	86,769
Total Deferred Charges	3,319,156	2,123,339
TOTAL ASSETS	\$696,922,282	\$692,829,003

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

	DECEMBER 31,	
	2008	2007
NET ASSETS AND LIABILITIES		
NET ASSETS		
Invested in Capital Assets, Net of Related Debt ...	\$383,506,857	\$360,036,128
Restricted for:		
Regional Water Supply System Construction Fund .	2,644,292	683,368
Water Assurance and System Development Charges .	8,453,514	19,519,178
Debt Service Funds	1,201,618	1,044,075
Unrestricted	8,204,023	10,480,568
Total Net Assets	404,010,304	391,763,317
LONG-TERM LIABILITIES, NET OF CURRENT MATURITIES		
Revenue Bonds	186,406,888	192,487,573
Public Works Trust Fund Loans	21,338,420	22,913,176
Drinking Water State Revolving Fund Loan	1,932,632	2,093,684
Muckleshoot Agreements	9,191,075	9,821,357
Total Long-Term Liabilities.....	218,869,015	227,315,790
CURRENT LIABILITIES		
Current Maturities of Long-Term Liabilities	7,801,533	7,995,814
Accrued Taxes	1,221,907	924,779
Accrued Expenses and Contracts Payable	2,685,678	1,972,622
Salaries, Wages and Fringe Benefits Payable	573,350	390,721
Interest Payable	890,598	884,669
Accrued Compensated Absences	2,280,006	2,039,218
Customers' Deposits	246,805	226,719
Payables to Affiliates	588,428	735,145
Total Current Liabilities	16,288,305	15,169,687
DEFERRED CREDITS		
Retained on Contract Payments	34,650	97,035
Customer Advances for Construction	6,038,897	6,471,205
Deferred Revenue - SDC & Other.....	50,058,137	49,858,546
Other Deferred Credits	1,622,974	2,153,423
Total Deferred Credits	57,754,658	58,580,209
Total Liabilities	292,911,978	301,065,686
TOTAL NET ASSETS AND LIABILITIES	<u>\$696,922,282</u>	<u>\$692,829,003</u>

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	YEAR ENDED DECEMBER 31,	
	2008	2007
OPERATING REVENUES	\$57,024,540	\$52,726,210
OPERATING EXPENSES		
Operations	15,716,720	14,965,145
Production	7,048,696	6,189,263
Administrative and General	10,622,247	9,922,107
Depreciation	13,016,544	11,363,970
Other Taxes	2,881,877	2,924,930
Total Operating Expenses	49,286,084	45,365,415
Net Operating Income	7,738,456	7,360,795
NON-OPERATING REVENUES (EXPENSES)		
Interest Income	3,730,407	5,255,881
Gain from Disposition of Property	-	4,200,000
Other	61,265	306,680
Interest on Long-Term Debt	(9,428,638)	(9,984,084)
Amortization of Debt Discount, Expense, Premium and Loss on Refunding	29,855	39,040
Interest Charged to Construction	992,519	1,460,639
Total Non-Operating Revenues (Expenses)	(4,614,592)	1,278,156
Net Income Before Capital Contributions and Transfers	3,123,864	8,638,951
Capital Contributions		
Cash	8,554,112	9,308,102
Donated Fixed Assets	5,583,493	3,493,105
Transfers		
City of Tacoma Gross Earnings Tax	(4,500,155)	(4,359,041)
Transfer to Other Funds	(514,327)	(203,616)
CHANGE IN NET ASSETS (NET INCOME)	12,246,987	16,877,501
TOTAL NET ASSETS - BEGINNING OF YEAR	391,763,317	374,885,816
TOTAL NET ASSETS - END OF YEAR	\$404,010,304	\$391,763,317

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

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATEMENTS OF CASH FLOWS

	YEAR ENDED DECEMBER 31,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash from Customers	\$56,262,503	\$54,716,533
Cash Paid to Suppliers	(14,693,692)	(15,175,318)
Cash Paid to Employees	(18,116,480)	(17,563,426)
Taxes Paid	(2,584,749)	(3,352,669)
Net Cash Provided by Operating Activities	20,867,582	18,625,120
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Transfer to Other Funds	(514,327)	(203,616)
Transfer Out for Gross Earnings Tax	(4,500,155)	(4,359,041)
Net Cash Used in Non-Capital Financing Activities	(5,014,482)	(4,562,657)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital Expenditures	(27,515,917)	(32,065,004)
Proceeds from PWTf Pre-Construction Loan	-	4,500,000
Principal Payments on Long-Term Debt	(8,440,371)	(13,067,485)
Interest Paid	(9,422,709)	(9,979,433)
Sale of Property	-	4,200,000
System Development Charges, CIAC and Other	7,728,561	18,695,827
Net Cash Used in Capital and Related Financing Activities	(37,650,436)	(27,716,095)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest Received on Investments	3,730,407	5,255,881
Other Net Non-Op Revenues and Expenses	61,265	306,680
Net Change in Deferred Charges	(1,366,647)	319,893
Net Cash Provided by Investing Activities	2,425,025	5,882,454
Net Change in Cash and Equity in Pooled Investments	(19,372,311)	(7,771,178)
Cash & Equity in Pooled Investments at January 1 ...	103,634,503	111,405,681
Cash & Equity in Pooled Investments at December 31 .	\$84,262,192	\$103,634,503

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

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2008 AND 2007

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Operations of Tacoma Water. The Water Division, doing business as Tacoma Water (Tacoma Water), is a blended component unit of the City of Tacoma (the City), Department of Public Utilities (the Department). The Department consists of Tacoma Power, Tacoma Water and Tacoma Rail and is governed by a five-member Public Utility Board (the Board) appointed by the City Council. Certain matters relating to utility operations such as system expansion, issuance of bonds, and fixing of utility rates and charges are initiated and executed by the Board, but also require formal City Council approval.

Tacoma Water owns and operates the City's Water System which includes a surface water supply source (the Watershed); several extensive well fields; a water transmission system consisting of several pipelines, water treatment and quality facilities; various reservoirs, standpipes and pump stations; and an extensive distribution system. Tacoma Water supplies water to approximately 96,000 customers and has approximately 272 employees. Tacoma Water's service area includes the City of Tacoma and urbanized areas of Pierce and South King Counties. Water service outside the City limits is provided under franchises granted by both Pierce and King Counties. Tacoma Water is organized functionally as Water Supply, Water Quality, Water Distribution, Second Supply Project and Water Resource Planning.

Water Supply designs, constructs, maintains and operates the water supply structures, wells, pumping stations, reservoirs, standpipes, transmission mains and associated property. Water use by retail customers varies from year to year primarily because of weather conditions, customer growth, economic conditions in Tacoma Water's service area and conservation efforts.

Water Quality operates and maintains the Green River Watershed and Headworks, operates and maintains water treatment equipment, and monitors water quality.

Water Distribution engineers, designs, constructs, operates and maintains all distribution system facilities including mains, hydrants, valves, service connections and metering.

Water Resource Planning provides planning for cost-effective resources to meet future needs, including water supply projects and conservation activities. Resource Planning manages watershed lands to provide for fisheries and wildlife populations, manages real estate property acquisitions and dispositions, and acquires and grants right-of-way easements.

Second Supply Project was developed to meet Tacoma Water's own future water supply requirements as well as to increase regional supply. The Second Supply Project Pipeline is approximately 34 miles long. Its route follows a more northerly route than Tacoma Water's existing Pipeline No. 1, traversing south King County and thereby making water available to the urbanized areas north and east of the City. Tacoma Water owns and operates the Second Supply Project. (See Note 5, Second Supply Project Agreement.)

Shared Services. Tacoma Water receives certain services from other departments and agencies of the City, including those normally considered to be general and administrative. Tacoma Water is charged for services received from other City departments and agencies and additionally, must pay gross earnings tax to the City.

	YEAR ENDED DECEMBER 31,	
	2008	2007
Reconciliation of Net Operating Income to Net Cash Provided by Operating Activities:		
Net Operating Income	\$7,738,456	\$7,360,795
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	13,016,544	11,363,970
Cash provided by (used in) changes in operating assets and liabilities:		
Accounts Receivable and Unbilled Revenue	(762,037)	1,990,323
Receivables from Affiliates	(360,688)	166,109
Materials and Supplies	(267,966)	(21,412)
Prepayments	196,303	(1,016,565)
Accrued Taxes	297,128	(427,739)
Salaries, Wages and Fringe Benefits Payable	182,629	67,919
Accrued Compensated Absences	240,788	112,861
Customers' Deposits	20,086	11,639
Accrued Expenses and Contracts Payable	713,056	(1,717,925)
Payables to Affiliates	(146,717)	735,145
Total Adjustments	13,129,126	11,264,325
Net Cash Provided by Operating Activities	<u>\$20,867,582</u>	<u>\$18,625,120</u>
Reconciliation of Cash and Equity in Pooled Investments to Balance Sheet:		
Cash and Equity in Pooled Investments		
in Special Funds	\$75,226,286	\$92,405,441
Cash and Equity in Pooled Investments		
in Operating Funds	9,035,906	11,229,062
Cash and Equity in Pooled Investments		
at December 31	<u>\$84,262,192</u>	<u>\$103,634,503</u>

Basis of Presentation. The financial statements of Tacoma Water are prepared under the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP) issued by the Governmental Accounting Standards Board (GASB) applicable to governmental entities that use proprietary fund accounting. Revenues are recognized when earned, and costs and expenses are recognized when incurred.

Tacoma Water follows the provisions of Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71). In general, SFAS No. 71 permits an entity with cost-based rates to defer certain costs or income that would otherwise be recognized when incurred to the extent that the rate-regulated entity is recovering or expects to recover such amounts in rates charged to its customers.

Tacoma Water generally follows the uniform system of accounts prescribed by the National Association of Regulatory Utility Commissioners and the Division of Audits of the State Auditor's Office. Tacoma Water is exempt from payment of Federal income tax.

Utility Plant and Depreciation. Utility plant is stated at original cost (See Note 2), which includes both direct costs of construction or acquisition and indirect costs, including an allowance for funds used during construction.

Provision for depreciation is made using the straight-line method, based on estimated economic lives of related operating assets placed in service at the beginning of the year. The composite depreciation rates for 2008 and 2007 were 2.26% and 2.20%. When operating plant assets are retired, their original cost together with removal cost, less salvage, is charged to accumulated depreciation. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and betterments is capitalized.

Allowance for Funds Used During Construction (AFUDC). AFUDC represents the cost of borrowed funds used for the construction of utility plant. Capitalized AFUDC is shown as part of the cost of utility plant and as a reduction of interest expense and income. The amount capitalized is net of interest income earned on unexpended bond proceeds.

Asset Valuation. Tacoma Water periodically reviews the carrying amount of its long-lived assets for impairment. An asset is considered impaired when estimated future cash flows are less than the carrying amount of the asset. In the event the carrying amount of such asset is not deemed recoverable, the asset is adjusted to its estimated fair value. Fair value is generally determined based on discounted future cash flow.

Special Funds. In accordance with bond resolutions, agreements and laws, separate restricted funds have been established. These funds, which consist of cash and investments, are restricted for specific uses including capital additions, debt service and extraordinary operations and maintenance costs.

Materials and Supplies. Materials and supplies consist primarily of items for construction and maintenance of utility plant and are valued at the lower of average cost or market.

Accounts Receivable. Accounts receivable are recorded when invoices are issued and are written off when they are determined to be uncollectible. The allowance for doubtful accounts is estimated based on Tacoma Water's historical losses, review of specific problem accounts, the existing economic conditions and the financial stability of its customers. Generally, Tacoma Water considers accounts receivable past due after 30 days.

Bond Premium, Discount, Issuance Costs and Loss on Refunding. Bond premium, discount and issuance costs are amortized using the bonds outstanding method over the terms of the issues to which they pertain. Loss on refunding is amortized on the straight line basis over the remaining life of the old debt or the life of the new debt, whichever is shorter. Bond issuance costs are included in deferred charges with others components recorded in long-term debt.

Compensated Absences. The City has two different policies for compensated absences. The City's original policy allows employees to accrue vacation based on the number of years worked with a maximum accrual equal to the amount earned in a two-year period. These employees also accrue one day of sick leave per month without any ceiling on the maximum accrued. The City implemented a new policy in 1998 allowing employees to earn PTO (personal time off) without distinction between vacation and sick leave. Employees who worked for the City prior to the change could choose to stay with the original policy or opt to convert to the new policy. The amount of PTO earned is based on years of service. The maximum accrual for PTO is 960 hours, and upon termination, employees are entitled to compensation for unused PTO at 100%. Vacation pay and PTO are recorded as a liability and expense in the year earned.

Employees in the original policy accumulate sick leave at the rate of one day per month with no maximum accumulation specified. Employee receives 25% of the value at retirement or 10% upon termination for any other reason. In the event of death, beneficiaries receive 25% of the value. The accrued liability is computed at 10%, which is considered the amount vested. Sick leave pay is recorded as an expense in the year earned.

Contributions in Aid of Construction and System Development Charges. GASB Statement No. 33, which addresses accounting for contributed capital, requires that contributed capital be recognized as revenue. Capital contributions include new service connections and system development charges. System development charges are collected on all new services prior to installation to ensure required new source, transmission and storage facilities needed to meet new demands are funded. The charge was developed using a cost-of-service approach and includes a share of historical plant investment and projected future outlays that will increase system capacity. Because the funds collected for this charge can only be used for system expansion projects, the balance is reflected as restricted in Tacoma Water's net assets. System development charges on uncompleted projects are recorded in deferred credits.

Revenues. Service rates are authorized by the Tacoma City Council. Revenues are recognized as earned and include an estimate of revenue earned but not billed to customers as of year-end. Utility revenues are derived primarily from the sale and transmission of water. Utility revenue from water sales is recognized when the water is delivered to and received by the customer.

Tacoma Water receives contract resource obligation revenue and debt service payments from our partners in the Second Supply Project Agreement which are recorded as operating revenue. Such revenues amounted to \$3.9 million and \$3.1 million for 2008 and 2007, respectively. Note 5 describes the terms of the agreement.

Environmental Remediation Costs. The Utility recognizes environmental obligations according to GASB Statement No. 49 "Accounting and Financial Reporting for Pollution Remediation Obligations". Accruals for expected pollution remediation outlays are recorded when one of five obligating events occurs and adjusted as further information develops or circumstances change. The five obligating events are applied when the Division is: 1) compelled to take action because of an imminent endangerment, 2) the Division is in violation of a pollution prevention-related permit or license, 3) the Division is named or evidence indicates that it will be named by a regulator as a responsible party or potentially responsible party, 4) named in a lawsuit to compel participation in pollution remediation or 5) the Division commences or legally obligates itself to commence pollution remediation.

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

Costs related to environmental remediation are charged to expense when the liability is recognized; outlays are capitalized when goods and services are acquired under specific circumstances as described in Statement No. 49. Measurement is based on the current value of the outlays for the individual remediation components using the expected cash flow technique, adjusted for recoveries from other parties.

Cash and Equity in Pooled Investments and Policies. Tacoma Water's cash is deposited with the City Treasurer in the City's general investment pool for the purpose of maximizing interest earnings through pooled investment activities. Cash and equity in pooled investments in the City's general investment pool are reported at fair value and changes in unrealized gains and losses are recorded in the Statements of Revenues, Expenses and Changes in Net Assets. Interest earned on such pooled investments is allocated to the participating funds based on each fund's average daily cash balance during the allocation period.

The general investment pool operates like a demand deposit account in that all City departments, including Tacoma Water, may deposit cash into the pool at any time and can also withdraw cash out of the pool without prior notice or penalty. Accordingly, balances are considered to be cash equivalents.

The City of Tacoma Investment Policy permits investments in certificates of deposit, obligations of the U.S. Treasury, agencies and instrumentalities, bankers' acceptances and repurchase and reverse repurchase agreements.

Repurchase agreements are settled delivered versus payment. The market value of collateralized securities must exceed the dollar amount of the repurchase agreement by 2% over the term of the agreement. Currently, the City participates only in overnight agreements. The underlying collateral must be an investment instrument that the City is authorized to purchase.

Tacoma Water's cash in banks held by the City Treasurer at December 31, 2008 and 2007 are entirely covered by federal depository insurance or on deposit with financial institutions recognized as qualified public depositories of the State of Washington under RCW Chapter 39.

Use of Estimates. The preparation of the financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Tacoma Water used estimates in determining of reported unbilled revenues, allowance for doubtful accounts, accrued compensated absences, depreciation, OPEB, self-insurance liabilities and other contingency. Actual results may differ from these estimates.

Significant Risks and Uncertainty. Tacoma Water is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include water conditions, weather and natural disaster-related disruptions, collective bargaining labor disputes, fish and other endangered species act issues, Environmental Protection Agency regulations, and federal government regulations or orders concerning the operation, maintenance and/or licensing of facilities.

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

Net Assets. Net assets consist of the following components:

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets and unspent bond proceeds, net of accumulated depreciation and outstanding balances of any bonds and other borrowings that are attributable to the acquisition, construction, or improvement of capital assets.
- Restricted – This component consists of net assets on which constraints are placed. Constraints include those imposed by creditors, contributors, enabling legislation or by law.
- Unrestricted – This component of net assets consists of net assets that are available for use.

Reclassifications. Changes have been made to prior year account classifications as needed to conform to the current year presentation format. One significant change related to capital assets classified as construction work in progress verses plant in service as follows:

UTILITY PLANT	2007 Reclassified in 2008 Report	2007 Reported
In Service, at Original Cost	\$ 671,605,223	\$ 619,239,712
Less Accumulated Depreciation	(115,966,258)	(115,966,258)
Total	555,638,965	503,273,454
Construction Work in Progress	12,854,050	65,219,561
Net Utility Plant	<u>\$ 568,493,015</u>	<u>\$ 568,493,015</u>

NOTE 2 UTILITY PLANT. A summary of the balances and changes in utility plant follows:

	Balance December 31, 2007	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2008
Intangible Plant	\$ 34,832,777	\$ 400,000	\$ (350,696)	\$ -	\$ 34,882,081
Source of Supply Plant	67,650,559	942,129	(3,930)	-	68,588,758
Pumping Plant	7,401,229	1,297,188	-	-	8,698,417
Water Treatment Plant	43,444,309	23,107	-	-	43,467,416
Transmission Facilities	181,786,717	2,345,728	(1,599)	-	184,130,846
Distribution Facilities	315,188,891	29,339,973	(1,893,126)	-	342,635,738
General Plant	21,300,741	2,638,416	(256,528)	(514,327)	23,168,302
Total Water Plant In Service	671,605,223	36,986,541	(2,505,879)	(514,327)	705,571,558
Less Accumulated Depreciation	115,966,258	13,016,544	(2,155,183)	(1,920,865)	124,906,754
	555,638,965	23,969,997	(350,696)	1,406,538	580,664,804
Construction Work in Progress	12,854,050	-	-	(2,925,596)	9,928,454
Net Utility Plant	<u>\$ 568,493,015</u>	<u>\$ 23,969,997</u>	<u>\$ (350,696)</u>	<u>\$ (1,519,058)</u>	<u>\$ 590,593,258</u>

NOTE 3 SPECIAL FUNDS. Cash and equity in pooled investments included in Tacoma Water's Special Funds consist of:

	2008	2007
Cash and Equity in Pooled Investments	\$ 13,930,776	\$ 20,251,838
Construction Funds	61,295,510	72,153,603
Other	<u>75,226,286</u>	<u>92,405,441</u>
Total		

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

NOTE 4 LONG-TERM DEBT. Long-term liability activity for the year ended December 31, 2008 was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Revenue Bonds	\$196,310,000	\$ -	\$(6,060,000)	\$190,250,000	\$5,880,000
Plus: Unamortized Premium	3,645,948	-	(378,709)	3,267,239	-
Less: Unamortized Discount	-	-	-	-	-
Less: Unamortized Loss on Refundings	<u>(1,408,375)</u>	-	<u>178,024</u>	<u>(1,230,351)</u>	-
Net Revenue Bonds	198,547,573	-	(6,260,685)	192,286,888	5,880,000
Washington State Public Works Board Loans	24,487,938	-	(1,574,756)	22,913,182	1,574,762
Drinking Water State Revolving Fund Loan	<u>2,254,736</u>	-	<u>(161,052)</u>	<u>2,093,684</u>	<u>161,052</u>
Total Long-Term Debt	225,290,247	-	(7,996,493)	217,293,754	7,615,814
Muckleshoot Liability (See Note 11)	<u>10,021,357</u>	-	<u>(644,563)</u>	<u>9,376,794</u>	<u>185,719</u>
Total Long-Term Liabilities	<u>\$235,311,604</u>	<u>\$ -</u>	<u>\$(8,641,056)</u>	<u>\$226,670,548</u>	<u>\$7,801,533</u>

Tacoma Water's long-term debt at December 31 consists of the following payable from revenues of Tacoma Water.

SENIOR LIEN BONDS

	<u>2008</u>	<u>2007</u>
2001 Water System Revenue Bonds, with interest rates ranging from 4.0% to 5.25%, due in yearly installments ranging from \$400,000 to \$4,795,000 through 2023.	\$30,460,000	\$30,840,000
Regional Water Supply System Revenue Bonds, 2002, with interest rates ranging from 3.5% to 5.50%, due in yearly installments ranging from \$800,000 to \$1,025,000 and term bonds due in installments ranging from \$1,125,000 to \$7,400,000 through 2032.	79,150,000	80,300,000
2003 Water System Revenue and Refunding Bonds, with interest rates ranging from 4.00% to 5.25%, due in yearly installments ranging from \$1,725,000 to \$3,505,000 through 2023.	37,830,000	40,695,000
2005 Water System Revenue and Refunding Bonds, with interest rates ranging from 3.5% to 5.0%, serial bonds due in yearly installments ranging from \$1,695,000 to \$4,760,000 through 2025.	<u>42,810,000</u>	<u>44,475,000</u>
Unamortized premium	190,250,000	196,310,000
Unamortized loss on refunding	3,267,239	3,645,948
Less Current Portion of Revenue Bond Debt	<u>(1,230,351)</u>	<u>(1,408,375)</u>
Long-term Portion of Revenue Bond Debt	<u>\$(5,880,000)</u>	<u>(6,060,000)</u>
	<u>\$186,405,888</u>	<u>\$192,487,573</u>

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TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

Scheduled principal maturities on the bonds and interest payments are as follows:

Year	Principal	Interest
2009	\$5,880,000	\$9,261,445
2010	\$6,075,000	\$9,038,895
2011	\$6,280,000	\$8,804,870
2012	\$6,550,000	\$8,526,483
2013	\$6,880,000	\$8,211,683
2014-2018	\$40,210,000	\$35,785,161
2019-2023	\$56,600,000	\$24,296,988
2024-2028	\$33,375,000	\$11,911,500
2029-2032	\$28,400,000	\$3,602,500

The fair value of Tacoma Water's long-term debt is based on quoted market prices. The fair market value of the Water System Revenue Bonds at December 31, 2008 and 2007 was \$113,010,415 and \$122,489,133, respectively. The fair market value of the Regional Water Supply System Revenue Bonds at December 31, 2008 and 2007 was \$66,957,498 and \$83,407,035, respectively.

The carrying amounts of the Washington State Public Works Board Loans and Drinking Water State Revolving Fund Loan approximate the fair value since such loans are exclusive and have no market.

Tacoma Water's revenue bonds are secured by the net revenue of Tacoma Water and all cash and investments held in the bond funds and construction funds. The bonds are also subject to certain financial and non-financial covenants.

JUNIOR LIEN DEBT

	<u>2008</u>	<u>2007</u>
Washington State Public Works Board Loans		
2001 Public Works Trust Fund construction loan for the Second Supply Project, with interest of .5% per annum, due in yearly installments of \$533,333 through 2021.	\$6,933,333	\$7,466,667
2001 Public Works Trust Fund pre-construction loan for the SSP Howard Hanson Dam Additional Storage Project, with interest of .5% per annum, due in yearly installments of \$52,632 through 2021.	684,212	736,842
2002 Public Works Trust Fund construction loan for the Middle and Headworks section of the SSP, with interest of .5% per annum, due in yearly installments of \$531,250 through 2022.	7,437,500	7,968,750
2002 Public Works Trust Fund pre-construction loan for the Middle and Headworks section of the SSP, with interest of .5% per annum, due in yearly installments of \$54,180 through 2021.	704,335	758,514
2004 Public Works Trust Fund pre-construction loan for the design of the Green River Ozone Facility with interest of .5% per annum, due in yearly installments of \$53,363 through 2024.	853,802	907,165
2006 Public Works Trust Fund pre-construction loan, with interest of .5% per annum, due in yearly installments of \$350,000 through 2026.	6,300,000	6,650,000

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TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

JUNIOR LIEN DEBT (CONTINUED)

	2008	2007
Drinking Water State Revolving Fund Loan		
2002 construction loan for the Portland Avenue Reservoir, with interest of 2.5% per annum, due in yearly installments of \$161,053 through 2021.	2,093,684	2,254,736
Subtotal Junior Lien Debt	25,006,866	26,742,674
Less current portion of debt	(1,735,814)	(1,735,814)
Long-Term portion of Junior Lien Debt	<u>\$23,271,052</u>	<u>\$25,006,860</u>

Scheduled principal maturities of Junior lien debt and interest payments are as follows:

Year	Principal	Interest
2009	\$1,735,810	\$166,908
2010	\$1,735,810	\$163,692
2011	\$1,735,810	\$143,108
2012	\$1,735,810	\$131,208
2013	\$1,735,810	\$119,308
2014-2018	\$8,679,049	\$418,036
2019-2023	\$6,545,405	\$183,572
2023-2026	\$1,103,362	\$ 10,764

NOTE 5 SECOND SUPPLY PROJECT AGREEMENT.

Participants in the Second Supply Project under the terms of the Second Supply Project Agreement, which defines their rights and obligations with regard to the Second Supply Project. Tacoma Water has a 15/36 Participant Share and each of the City of Kent, Covington Water District and Lakehaven Utility District has a 7/36 Participant Share in the Second Supply Project. Each Participant has contractual rights under the Second Supply Project Agreement (i) to use an undivided share of the Project equal to its project capacity share and to use available excess project capacity; (ii) to schedule for delivery and receive its Participant Share of Second Diversion Water at its points of delivery; (iii) to schedule for delivery and receive additional water at its points of delivery; and (iv) to its Participant Share of storage. Each Participant has a contractual obligation (i) to receive Second Diversion Water and additional water scheduled for delivery and delivered to it and (ii) to pay its Participant Share of Project Costs, including but not limited to Fixed and Variable O & M Costs, Initial Project Construction Costs and Capital Expenditures. Kent and Covington, in the "Repayment Agreement", pledge to pay Tacoma Water a defined share of the principal and interest debt service on the Regional Water Supply System Bonds. The term of the Second Supply Project Agreement extends through the operating life of the Second Supply Project including all renewals and replacements thereof and additions thereto. The Second Supply Project Agreement provides that all obligations incurred during its term will survive its termination or expiration and will survive until satisfied.

NOTE 6 SIGNIFICANT CUSTOMER. Contracted sales to Simpson Tacoma Kraft Company (Simpson) accounted for 8.5% and 8.1% of Tacoma Water's total water sales in 2008 and 2007, respectively.

Tacoma Water has contracted with Simpson to supply certain quantities of water under a take-or-pay arrangement at a specified rate through July 31, 2015.

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

NOTE 7

FLEET SERVICES FUND. The Department of Public Utilities has established a Fleet Services Fund to perform scheduled maintenance, repair and replacement of the Department vehicles and related equipment. Transfers of vehicles and equipment from Tacoma Water to the Fleet Services Fund are accounted for as transfers.

Tacoma Water pays the Fleet Services Fund for the use of the vehicles and equipment to cover fleet operating expenses. Payments made by Tacoma Water in 2008 and 2007 were \$3,396,652 and \$3,121,601, respectively.

Fleet Services' management makes an annual assessment of the capital replacement reserve balance for appropriate funding levels. It is the Fund's policy to maintain the Fund's maximum balance at a level that will provide adequate purchasing power for a three-year cycle and to return any excess funds to customers based on their scheduled monthly payments. The solvency of the Replacement Fund also allowed Fleet Services to return a portion of interest earned on Fund investments for the year to their customers. In 2008 and 2007, Fleet Services returned 75% of the interest earned on the capital replacement reserve to Tacoma Water's replacement fund. The amounts refunded in 2008 and 2007 were \$154,246 and \$160,813, respectively, which was used to offset the corresponding year's fleet expenses.

NOTE 8

SELF-INSURANCE FUND. The Department of Public Utilities maintains a self-insurance program and insurance policies. The Department has established a self-insurance fund to insure Tacoma Water and other divisions within the Department for certain losses arising from personal and property damage claims by third parties. The major risks to Tacoma Water are flooding, wind damage, chemical spills and earthquakes. Mitigating controls and emergency and business resumption plans are in place. To the extent damage or claims exceed insured values, rates may be impacted.

Tacoma Water is required to make payments to the Self-Insurance Fund to cover claims incurred by Tacoma Water and administrative expenses of the Fund. Tacoma Water's premium payments totaled \$120,000 in both 2008 and 2007. Liabilities have been accrued in the Self-Insurance Fund for environmental remediation costs expected to be incurred. No provision has been recorded for environmental remediation costs that could result from changes in laws or other circumstances currently not contemplated. Assets in the Self-Insurance Fund total \$4.8 million which exceeds accrued and incurred but not reported liabilities. Equity in the Self-Insurance Fund is transferred to the appropriate operating divisions in accordance with GASB 10. Management believes Tacoma Water's investment in the Self-Insurance Fund is more than adequate to settle all its known or estimated claims.

Performance and fidelity bonds covering all employees are provided in amounts up to \$1 million (subject to a \$50,000 deductible per occurrence). The insurance policies presently in effect include coverage on the Department's buildings and fleet vehicles as well as general liability and public official's liability. The current insurance policies have deductibles or self insured retentions of \$250,000 for buildings and vehicles and \$1,000,000 for general comprehensive liability. The public officials policy has a \$200,000 deductible for employee practices liability and \$100,000 deductible for all other issues. The general comprehensive liability policies provide \$20 million of coverage. The City has a policy to cover extraordinary worker's compensation claims with a limit of \$25 million (\$1 million deductible).

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

NOTE 9 TACOMA EMPLOYEES' RETIREMENT SYSTEM FUND (TERS). Pursuant to GASB Statement No. 50, "Pension Disclosures" – an amendment of GASB Statements No. 25 and No. 27, this note discloses the employer's disclosures and detailed information presented in an independent Comprehensive Annual Financial Report (CAFR) issued by the Retirement System. Further detailed information regarding these disclosures can be found in that report which may be obtained by writing to Tacoma Employees' Retirement System, 747 Market Street, Room 1544, Tacoma, Washington 98402.

1. The System is a single employer, defined benefit retirement plan covering employees of the City of Tacoma and is administered in accordance with Revised Code of Washington (RCW) Chapter 41.28 and Chapter 1.30 of the Tacoma Municipal Code. There are 1,820 vested retirees and beneficiaries of deceased retirees currently receiving benefits and 367 vested terminated employees entitled to future benefits but not yet receiving them. Currently, 3,124 active members are part of the System.
2. Basis of Accounting: The financial statements are prepared using the accrual basis of accounting. Employee and employer contributions are recognized as revenues in the period in which employee services are performed and expenses are recorded when the corresponding liabilities are incurred, regardless of when payment is made. The employer contribution rate is determined by the actuarial funding method identified as the "entry age cost method".
3. Investments: Equity securities, fixed income securities, real estate, and short-term investments are all reported at fair market value. Fair market value was determined by the custodian bank utilizing standard industry practices and verified by the performance consultant. No investment in any one corporation or organization exceeded 5% of net assets available for benefits.
4. Contracts: The System has no securities of the employer or related parties included in the plan assets. The System has not made any loans to the employer in the form of notes, bonds or other instruments.
5. Contribution Rates: Covered employees are required by Chapter 1.30 of the Tacoma Municipal Code to contribute based on the rates provided in the following table:

Applicable Period	City Rate	Member Rate	Total Rate
1/1/1980 to 12/31/1996	10.44%	8.89%	19.33%
1/1/1997 to 12/31/2000	9.02%	7.68%	16.70%
1/1/2001 to 2/1/2009	7.56%	6.44%	14.00%
2/2/2009 to 12/31/2009	8.64%	7.36%	16.00%
1/1/2010 to Forward	9.72%	8.28%	18.00%

Contributions city-wide totaled \$27.2 million in 2008 (\$14.5 million employer contributions and \$12.7 million employee contributions) and totaled \$25.7 million in 2007 (\$13.6 million employer contributions and \$12.1 million employee contributions).

6. Funding Status and Progress: Historical trend information about TERS is presented herewith as supplementary information. This information is based on the most recent actuarial valuation performed, dated January 1, 2007, and is intended to help assess TERS funding status on a going-concern basis, assess progress made in accumulating assets to pay benefits when due, and make comparisons with other public employee retirement systems.

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

7. Actuarial Methods and Significant Actuarial Assumptions:
- | | |
|-----------------------------------|---|
| Valuation Date: | January 1, 2007 |
| Actuarial Cost Method: | Entry Age |
| Amortization Method: | Level Percentage of the System's Projected Payroll |
| Remaining Amortization Period: | 30 years; open |
| Asset Valuation Method: | Assets are valued at market value, with a four-year smoothing of all market value gains and losses. |
| Actuarial Assumptions: | |
| Investment Rate of Return | 7.75% |
| Projected Salary Increases | 4.0% |
| Includes Inflation at | 3.25% |
| Post-Retirement Benefit Increases | 2.125% |

SCHEDULE OF FUNDING PROGRESS: (\$ in millions)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Liability (AAL) Entry Age (b)	Unfunded AAL (UAA) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAA as a Percentage of Covered Payroll (b-a/c)
1/1/03	\$740.1	\$686.8	(\$53.3)	107.8%	\$154.2	(34.6%)
1/1/05	\$807.3	\$754.3	(\$53.0)	107.0%	\$172.5	(30.7%)
1/1/07	\$1,021.3	\$895.8	(\$125.5)	114.0%	\$175.0	(71.7%)

ANNUAL PENSION COST AND NET PENSION OBLIGATION:

The City's annual pension cost and net pension obligation to the Retirement System for 2006 were as follows:

	(\$ in millions)
Annual Required Contribution (ARC)	\$13.2
Adjustment to ARC	-
Annual Pension Cost (APC)	13.2
Contributions made	13.2
Increase (Decrease) in Pension Obligation	-
Net Pension Obligation at beginning of year	-
Net Pension Obligation at end of year	\$ -

TREND INFORMATION
(\$ in millions)

Year Ending	Annual Pension Cost (APC)	% of APC Contributed	Net Pension Obligation
12/31/04	\$13.0	100%	\$0
12/31/05	\$13.0	100%	\$0
12/31/06	\$13.2	100%	\$0

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

NOTE 10 OTHER POST EMPLOYMENT BENEFITS (OPEB)

Plan Description. The City charges some early retirees not yet eligible for Medicare a health premium based on the claims experience of both actives and retirees. Since health claims costs generally increase with age, retiree health premiums would be significantly higher if they were determined without regard to active claims experience. GASB 45 requires that the portion of age-adjusted expected retiree health claims costs that exceed the premium charged to retirees be recognized as a liability for accounting purposes.

Funding Policy. The City uses pay as you go funding; GASB 45 does not require contributions to a separate trust.

Annual OPEB Cost and Net OPEB Obligation. The Present Value of Benefits (PVB) is the present value of projected benefits discounted at the valuation interest rate. The valuation interest rate used is 4.00% based upon the expected return for short term fixed income securities. This rate is used as the required contributions net of benefits paid are not prefunded.

The Normal Cost is that portion of the City provided benefit attributable to employee service in the current year. The Actuarial Accrued Liability (AAL) is the portion of the present value of benefits attributed to past service only. The Annual Required Contribution (ARC) is the amount the City would be required to report as an expense for the year. The ARC is equal to the Normal Cost plus an amount to amortize the unfunded Actuarial Accrued Liability (AAL). The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. Each year the ARC, less current year benefit payments, will accumulate as a liability, Net OPEB Obligation, on the balance sheet.

The following table is a summary of actuarial valuation results as of January 1, 2007.

Total membership:	
Active employees	3,674
Terminated vested employees	247
Retired employees	729
Dependents	184
Total	4,834
Annual Benefit Payments	\$ 8,527,863
Discount rate	4.00%
Present Value of Benefits (PVB)	\$ 236,595,810
Actuarial Accrued Liability (AAL)	\$ 178,137,499
Normal Cost	\$ 4,949,734
Annual required contribution (ARC)	\$ 14,159,338

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

The following table shows the City's Net OPEB Obligation broken down by the total value of the benefits provided, the member premiums and the City paid benefits.

Value of Subsidy at 4.00% Interest Rate	Total Value of Benefits	Member Paid Premiums	City Paid Benefits
Present Value of Benefits (PVB)			
Active employees	\$ 233,919,911	\$ 128,671,261	\$ 105,248,650
Inactive employees	151,028,255	19,681,095	131,347,160
Total	\$ 384,948,166	\$ 148,352,356	\$ 236,595,810

Actuarial Accrued Liability (AAL)			
Active employees	\$ 94,449,644	\$ 47,659,305	\$ 46,790,339
Inactive employees	151,028,255	19,681,095	131,347,160
Total	\$ 245,477,899	\$ 67,340,400	\$ 178,137,499

Normal Cost	\$ 11,155,450	\$ 6,205,715	\$ 4,949,734
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Annual Benefit Payments	\$ 11,074,373	\$ 2,546,510	\$ 8,527,863
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The following table shows the calculation of the Annual Required Contribution and Net OPEB Obligation for the City and for Tacoma Water as of December 31, 2008.

Determination of Annual Required Contribution	City	Tacoma Water
Normal Cost at Year-end	\$ 4,949,734	\$ 282,895
Amortization of UAAL	9,209,604	95,379
Annual Required Contribution (ARC)	\$ 14,159,338	\$ 378,274
Determination of Net OPEB Obligation		
Annual Required Contribution (ARC)	\$ 14,159,338	\$ 378,274
Interest on prior year Net OPEB Obligation	225,259	10,526
Adjustments to ARC	(318,828)	(14,898)
Annual OPEB Cost	\$ 14,065,769	\$ 373,902
Actual benefits paid	9,266,967	141,536
Increase in Net OPEB Obligation	\$ 4,798,802	\$ 232,366
Net OPEB Obligation - Beginning of year	5,631,475	263,141
Net OPEB Obligation - end of year	\$ 10,430,277	\$ 495,507

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

Funded Status and Funding Progress. The City uses pay as you go funding.

The following table shows the annual OPEB costs and net OPEB obligation for three years.

Year Ended	Annual OPEB Cost		Contributed		Net OPEB Obligation	
	City	Tacoma Water	City	Tacoma Water	City	Tacoma Water
12/31/2006	N/A	N/A	N/A	N/A	N/A	N/A
12/31/2007	\$ 14,159,338	\$ 378,274	\$ 8,527,863	\$ 115,133	\$ 5,631,475	\$ 263,141
12/31/2008	\$ 14,065,769	\$ 378,274	\$ 9,266,967	\$ 141,536	\$ 10,430,277	\$ 495,507

Actuarial Methods and Assumptions. The actuarial cost method used for determining the benefit obligations is the Entry Age Normal Cost Method. Under the principles of this method, the actuarial present value of the projected benefits of each individual included in the valuation is allocated as a level percentage of expected salary for each year of employment between entry age (defined as age at hire) and assumed exit (until maximum retirement age).

The portion of actuarial present value allocated to a valuation year is called the normal cost. The portion of this actuarial present value not provided for at a valuation date by the sum of (a) the actuarial value of the assets, and (b) the actuarial present value of future normal costs is called the Unfunded Actuarial Accrued Liability (UAAL). In determining the Annual Required Contribution, the UAAL is amortized as a level percentage of expected payrolls over 30 years for non-LEOFF Law Enforcement Officers Fire Fighters) 1 groups; for LEOFF 1, the UAAL is amortized as a level dollar amount over 30 years.

Actuarial Methods and Significant Actuarial Assumptions:

Valuation Date	January 1, 2007
Census Date	July 31, 2006
Actuarial Cost Method:	Entry Age
Amortization Method:	Combination of level percentage and level dollar amount, see note above.
Remaining Amortization Period:	30 years, open
Demographic Assumptions	Demographic assumptions regarding retirement, disability, and turnover are based upon pension valuations for the various pension plans.
Actuarial Assumptions:	
Discount Rate	4.0%
Health Cost Trend	10.0% in the first year (2007-8), 9% in the second year, and graded down 1% per year to 5% per year in the sixth and beyond.
Projected Payroll Increases	4.0%

TACOMA WATER
NOTES TO FINANCIAL STATEMENTS
(continued)

Eligibility:
TERS members are eligible for retiree medical benefits after becoming eligible for service retirement pension benefits (either reduced or full pension benefits):

- Age 55 with 10 years of service
- 20 years of service

Valuation of Retiree Premium:

The City uses the same premiums for retirees under age 65 as for active employees. Therefore, the retiree premium rates are being subsidized by the inclusion of actives in setting non-Medicare retiree rates. For TERS retirees, Regence developed monthly premium levels for 2007 and a projected claims cost per retiree under age 65.

	2007 Monthly		Projected Claim	Value of Retiree Premium
	Premium Levels	Cost per Retiree		
PPO	\$ 891.38	\$ 1,479.44		\$ 588.06
Selections	\$ 947.37	\$ 1,532.44		\$ 585.07

NOTE 11 COMMITMENTS AND CONTINGENCIES

Muckleshoot Indian Tribe Settlement. A mutually beneficial settlement agreement was reached with the Muckleshoot Indian Tribe in 1995. The settlement package has a cost of approximately \$30 million and includes five basic elements: 1) building a fish restoration facility and annual operation and maintenance of that facility, or in the alternative, providing \$12 million (indexed at 1995 dollars) into a fish restoration fund; 2) providing for enhanced flows in the Green River; 3) transferring certain lands; 4) establishing a trust fund payable over 40 years which is intended to provide for the general welfare, educational and other needs of the Tribe; and 5) limited access into the Green River Watershed. The settlement resolved past damage claims by the Tribe for Tacoma Water's historical operations on the river, gain the Tribe's support for the Second Supply Project and provide the basis for a long-term, cooperative working relationship on the Green River.

Tacoma Water has been implementing this agreement. In 2005, Tacoma Water concluded the alternative payment under item 1 and the transfer of certain lands under item 3.

Robison Construction Inc. On Tacoma Water's Second Supply Pipeline construction project, the contractor has developed two potential "additional work" construction claims arising out of work done by its subcontractor Northwest Boring, in boring tunnels for the I-5 and Green River crossings. The potential claims together are \$4,884,055. The contractor has filed formal claims with Tacoma Water in 2009. Tacoma Water disputes these claims, and the parties are engaging in settlement discussions.

General Legal Matters. The Utility is involved in various litigations in the normal course of business. In the opinion of management, the ultimate outcome of these claims will not have a material effect on the Utility's financial position beyond amounts already accrued as of December 31, 2008.

APPENDIX D

FORM OF OPINION OF BOND COUNSEL

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[FORM OF APPROVING LEGAL OPINION]

City of Tacoma, Washington

Re: City of Tacoma, Washington,
\$76,775,000 Water System Revenue Bonds, 2009 (Taxable Build America Bonds – Direct
Payment)

We have served as bond counsel to the City of Tacoma, Washington (the “City”), in connection with the issuance of the above-referenced bonds (the “Bonds”), and in that capacity have examined such law and such certified proceedings and other documents as we have deemed necessary to render this opinion. As to matters of fact material to this opinion, we have relied upon representations contained in the certified proceedings and other certifications of public officials furnished to us, without undertaking to verify the same by independent investigation.

The Bonds are issued by the City pursuant to Substitute Ordinance No. 27837 and Substitute Resolution No. 37890 (together, the “Bond Ordinance”) to provide the funds to (a) pay part of the cost of constructing capital improvements to the Water System; (b) provide for a reserve for the Bonds; and (c) pay the costs of issuance of the Bonds all as set forth in the Bond Ordinance.

For as long as any of the Bonds are outstanding, the City irrevocably has pledged to set aside from the Gross Revenue of the Water System and to pay into the “Water Revenue Bond Fund of the Water Division Fund” (the “Bond Fund”) the various amounts required by the Bond Ordinance to be paid into and maintained in such Bond Fund within the times provided by the Bond Ordinance. The Bonds are special limited obligations of the City and are not obligations of the State of Washington or any political subdivision thereof other than the City, and neither the full faith and credit nor the taxing power of the City or the State of Washington is pledged to the payment of the Bonds.

Reference is made to the Bonds and the Bond Ordinance for the definitions of capitalized terms used and not otherwise defined herein.

We express no opinion herein concerning the completeness or accuracy of any official statement, offering circular or other sales or disclosure material relating to the issuance of the Bonds or otherwise used in connection with the Bonds.

Based upon the foregoing, as of the date of initial delivery of the Bonds to the purchaser thereof and full payment therefor, it is our opinion that under existing law:

1. The City is a duly organized and legally existing first-class city under the laws of the State of Washington;
2. The Bonds have been duly authorized and executed by the City and are issued in full compliance with the provisions of the Constitution and laws of the State of Washington and the ordinances of the City relating thereto;
3. The City has irrevocably bound itself to set aside and pay into the Bond Fund and the Reserve Account therein out of Net Revenue of the Water System, amounts necessary to pay the principal of and interest on the Bonds as the same become due.
4. The City has pledged that the payments to be made into the Bond Fund and the Reserve Account out of Gross Revenue of the Water System shall be a lien and charge thereon equal in rank to the lien and charge upon such Revenue of the amounts required to pay and secure the payment of the Outstanding Parity Bonds and any

water system revenue bonds of the City hereafter issued on a parity with the Bonds, and superior to all other liens and charges except the Cost of Operation and Maintenance of the Water System and payments pursuant to Contract Resource Obligations. The City has reserved the right to issue future parity bonds on the terms set forth in the Bond Ordinance.

5. Interest on the Bonds is not excludable from gross income for federal tax purposes.

This opinion is given as of the date hereof, and we assume no obligation to revise or supplement this opinion to reflect any facts or circumstances that may hereafter come to our attention, or any changes in law that may hereafter occur.

We bring to your attention the fact that the foregoing opinions are expressions of our professional judgment on the matters expressly addressed and do not constitute guarantees of result.

Respectfully submitted,

FOSTER PEPPER PLLC