

FROM THE DIRECTOR

When operating in a year that included the warmest, driest spring and summer on record, followed by the wettest late fall and winter on record, Tacoma Public Utilities did what we've disciplined ourselves to do: adapt.

In 2015, no other word describes our approach better than adaptability. On the financial, operational and human fronts, Tacoma Public Utilities flexed itself to ensure continued reliable service in the face of challenging circumstances.

A historic drought led to an unprecedented low winter snowpack. Since snowpack serves as a vital resource for a utility like ours that provides drinking water and generates hydroelectricity, we had to rely on planning and predictive analytics to fulfill our objectives.

Tacoma Power filled its reservoirs earlier in the spring than normal – a calculated risk that proved to be the right one. Despite the dry conditions, the utility continued to meet customer demand and sell wholesale power while also meeting its requirements to protect fish.

During the summer, when river flows were at historic lows, Tacoma Water relied on its abundant local groundwater supply to help meet system demands. This ensured stored water was prioritized for meeting instream flow requirements and protecting critical fish runs. Additionally, the utility exercised other supply-side options, supplementing its ability to provide water to customers. In July, Tacoma Water asked its customers to voluntarily reduce non-essential water use such as lawn irrigation. The positive response by customers reflects the strong collaboration between the utility and its customers.



WILLIAM A. GAINES, DIRECTOR & CEO



TPU ADMINISTRATION BUILDING

The drought provided both Tacoma Power and Tacoma Water lessons that can be relied upon in the future, both during lower water years and in normal operations.

Early in 2015, Tacoma Public Utilities welcomed Chris Robinson to its executive team as the new Tacoma Power superintendent. He replaced Ted Coates, who ably led the power utility for nearly six years. Mr. Robinson brings more than 20 years of experience to his role, 15 of those with Tacoma Power.

We continued to focus on development and implementation of long-term strategic plans this year, as a framework for continued successful operations.

Tacoma Power launched a strategic planning process to outline its game plan for the next several years. The plan, which will be complete in mid-2016, identifies initiatives focused on financial fitness, customer service and operational excellence.

Staff from Tacoma Water continued implementation of strategic planning elements developed in 2011. The utility joined other utilities this year in an effort to identify long-term regional resource and infrastructure needs. Going forward, Tacoma Water will take a closer look at its long-term supply outlook and will formalize its findings next year.

Tacoma Rail continued to focus on safety as its top priority. The railroad worked with regulatory agencies to develop new policies and procedures to handle hazardous commodities safely and efficiently. It also upgraded sections of track, increased inspection frequency and improved employee safety training.

Focusing on the intersection of customer and environmental objectives, late in 2015, Tacoma Power began work on a community solar project. The project helps customers get the benefit of generous state solar incentives. The utility saw significant interest from customers after announcing the project in October. Construction of four solar arrays will be complete in early 2016.

**BEING ABLE TO ADAPT TO
OUR CONSTANTLY CHANGING
ENVIRONMENT REQUIRES KNOWING
WHERE WE ARE AND WHERE WE
WANT TO GO.**

We undertook two important organization-wide initiatives this year. We implemented a new system of key performance metrics and benchmarking to help our senior management team and Public Utility Board monitor organizational performance. An increased focus on emergency planning and preparedness led to development of a Continuity of Operations Plan, which would be implemented in the event of natural or man-made disasters or malevolent attack.

Why is all of this important? Ultimately, we strive to ensure our decisions, processes and outcomes benefit our customers. The best way to know if it's working is to ask them. So we did.

We conducted our second semiannual residential customer satisfaction survey in 2015 and learned that, for the most part, we're on the right track. We received an 87% positive rating for overall customer satisfaction, 87% of our customers said they have a high level of trust in us and 83% said we are responsive to their needs.

One of the measures we're most proud of relates to our employees: 87% of customers said we have friendly and courteous employees, and 87% said our employees are well-trained and knowledgeable. In turn, 78% of employees indicated they are satisfied or highly satisfied with their work at Tacoma Public Utilities.

There's one certain thing we learned from 2015; being able to adapt to our constantly changing environment requires knowing where we are and where we want to go, and having the analytical and strategic skills required to change course when needed. That will serve us well in years as unpredictable as 2015, but also in the normal course of the utility business.



William A. Gaines became the Director and CEO of Tacoma Public Utilities in 2007, after serving briefly as Tacoma Power superintendent. He has developed an exceptional record of success and accomplishment over the course of more than 30 years in the utility industry that has included senior executive roles at Seattle City Light and Puget Sound Energy.

His career has emphasized organizational leadership, strategic and energy supply planning, commercial transactions and policymaking. His educational background is in engineering and finance. Bill serves as a board member and leader with several regional and national electric utility industry organizations, including the Large Public Power Council (LPPC) and the American Public Power Association (APPA). He also serves on the Tacoma/Pierce County Chamber of Commerce Board, the Pierce County Economic Development Board, and on advisory boards at Washington State University and the University of Washington.



PUBLIC UTILITY BOARD BIOS

Mark Patterson, secretary, is an attorney with the local law firm Vandeberg, Johnson & Gandara. He is a board member of Franke Tobey Jones and on the personnel committee of Associated Ministries of Tacoma/Pierce County. He joined the Public Utility Board in 2012.

Karin Larkin, a former City of Tacoma and State of Washington employee, joined the board in 2015. She has a long history of public service, having served 31 years in Tacoma's city government and her last five years prior to retirement as an assistant director at the Washington State Department of Commerce.

Monique Trudnowski is co-owner and operator of Adriatic Grill Italian Cuisine & Wine Bar. She is a founding member of the Washington Tourism Alliance and is the board chair for the Tacoma Regional Convention and Visitor Bureau. She also serves on the Board of Directors for the Broadway Center for the Performing Arts.

Bryan Flint is the executive director of the Greater Metro Parks Foundation. He is a member of both Rotary No. 8 and an American Leadership Foundation Senior Fellow. He joined the Public Utility Board in 2011.

Woodrow Jones retired from the City of Tacoma, where he worked in Human Resources for more than 20 years. He joined the Public Utility Board in 2009 and stays active in the community. He is past president and current member of the Sunrise Rotary and a member of the Tacoma-Pierce County Black Collective.

MANAGEMENT TEAM BIOS

William A. Gaines became the Director and CEO of Tacoma Public Utilities in 2007, after serving briefly as Tacoma Power superintendent. He has developed an exceptional record of success and accomplishment over the course of more than 30 years in the utility industry that has included senior executive roles at Seattle City Light and Puget Sound Energy.

Chris Robinson was named superintendent and COO of Tacoma Power in 2015. During his 15-year tenure with Tacoma Power, Chris has served as power manager and assistant power manager. Prior to Tacoma Power, Chris worked as a consultant with multiple electrical utilities. Chris serves on the boards of the Public Power Council, River Partners and the Pacific Northwest Utilities Conference Committee.

PICTURED FROM LEFT:

M. PATTERSON, K. LARKIN, M. TRUDNOWSKI, B. FLINT, W. JONES



Linda McCrea was named superintendent and COO of Tacoma Water in 2010. She has been with Tacoma Water since 1980, serving as deputy superintendent since 2006 and as the water distribution manager for 13 years before that. Linda represents the Pacific Northwest Section on the national American Water Works Association Water Utility Council. She is also a co-chair of the Utility Management Committee for the Association of Metropolitan Water Agencies.

Dale King was named superintendent and COO of Tacoma Rail in 2008. Dale served previously as the director of rail services for Weyerhaeuser Co. and has also served with Burlington Northern Railroad. Dale is a certified member of the American Society of Transportation & Logistics, now a part of APICS.

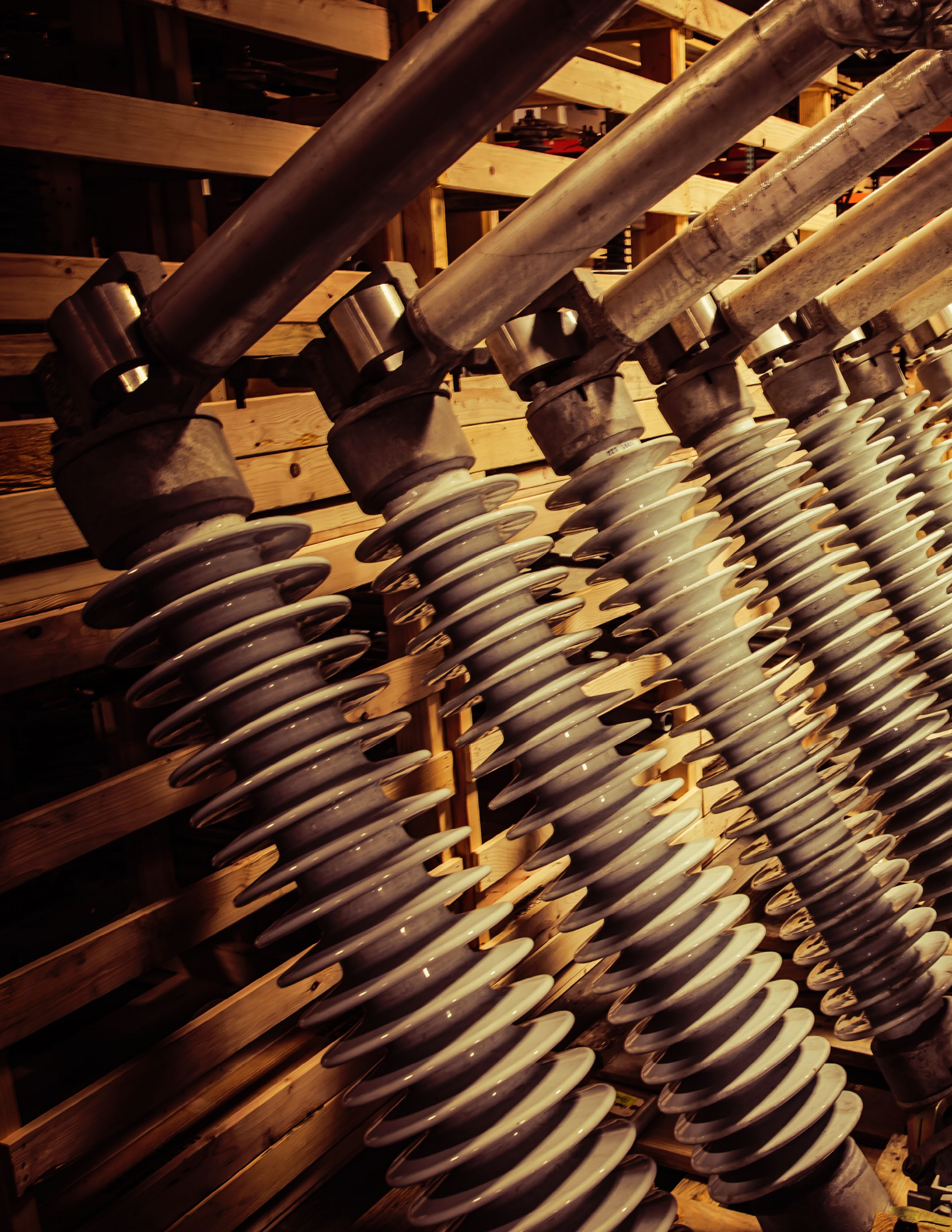
Steven Hatcher has served as Tacoma Public Utilities' Customer Services manager since 2006. Steve has prior experience as a city administrator and is a retired United States Army officer. He is a member of American Association of Blacks in Energy and the Pierce County Black Collective; he is also a member of the E Source Customer Experience Executive Council.

Robert Mack joined Tacoma Public Utilities in 2007 as the deputy director for public affairs. Bob is a former principal in the Tacoma law firm Smith Alling and has also served in various offices of Washington state government. He is a board member of the Tahoma Audubon Society.

Christine Gleason has served as Community & Media Services manager since 2006 and was a communicator for Tacoma Power for three years prior. Christine has nearly 20 years of experience in communications and marketing. She is a member of the International Association of Business Communicators.

Jim Sant was named deputy director for administration in 2012. His previous experience includes 10 years of service at Puget Sound Energy, where he served as assistant treasurer and director of financial planning and analysis. Prior to that, he was the regional financial manager at Verizon Wireless.

PICTURED FROM LEFT:
**J. SANT, C. GLEASON, D. KING, W. GAINES,
 R. MACK, L. MCCREA, C. ROBINSON, S. HATCHER**



TACOMA **POWER**



2015

THE DRIEST,
THEN THE WARMEST AND
FINALLY THE WETTEST YEAR
ON RECORD

TACOMA | POWER

Led by new superintendent Chris Robinson, Tacoma Power proved resilient over the course of a record-setting year in 2015. Facing weather that was first the driest, then the warmest and finally the wettest on record, the utility had to adapt quickly to changing conditions. The year started with the lowest springtime runoff on record for Western Washington. Snowpack was less than 20% of normal, with many areas in the region recording zero snowpack for the year. Early in the year, Tacoma Power took proactive steps to develop a plan to collect wintertime rain and fill storage reservoirs well above normal levels. As a result, the utility refilled reservoirs by early summer. That stored water was used later to augment river flows, protect fish and minimize the potential environmental impacts of the drought.

Caring for the environment near its hydroelectric projects is a primary concern for Tacoma Power. To that end, the utility began construction on a facility that will collect migrating young salmon from the upper Cowlitz River. The collector will improve natural fish runs and help Tacoma Power meet its Federal Energy Regulatory Commission

license obligations. The \$35 million construction project is scheduled for completion near the end of 2016. Another fish project, a floating fish collector, was commissioned in early 2015 and successfully operated in the spring and into the early summer. Construction on two new fish hatcheries was nearly completed by the end of the year and will soon begin operating.

In honor of Tacoma Power's work with fish, the utility captured its fourth straight Outstanding Stewards of America's Waters Award from the National Hydropower Association. This recent award recognizes a pioneering fish passage project in which fish ladders were carved into bedrock to allow fish to get through, helping secure salmon and steelhead populations.

**CARING FOR THE
ENVIRONMENT NEAR ITS
HYDROELECTRIC PROJECTS
IS A PRIMARY CONCERN
FOR TACOMA POWER.**

The financial picture

In 2015, as in every year, Tacoma Power's primary financial goal was to manage costs in a way that maintains low rates for customers. A big part of meeting that goal was completing the implementation of a financing plan that includes use of \$122 million of financial reserves to call the utility's outstanding 2005B bonds, reducing debt service over the next several years. With an eye toward the future, Tacoma Power also executed an interim \$100 million financing agreement to fund capital improvements in advance of a long-term bond issue. Those efforts form the basis of a long-range plan to maintain financial strength and minimize the impact of future rate increases.

Tacoma Power's credit ratings were confirmed by Moody's and Fitch in 2015 as part of their regular monitoring and review cycle for the utility. The utility's existing credit ratings of Aa3/AA/AA- by Moody's, Standard & Poor's, and Fitch, respectively, continue to allow Tacoma Power access to low-interest rates for future borrowing needs.

The Tacoma Public Utility Board and City Council approved a 3% overall rate increase that took effect in April. Power rates remain among the lowest rates for similarly sized utilities in the region.

Wholesale transactions for the year were characterized by strong sale volumes and deteriorating wholesale prices. The quantity of wholesale power sales (net of purchases) was 1.6 million megawatt-hours, exceeding the budget estimate of 1.2 million megawatt-hours. However, due to the steady decline of wholesale power prices, annual revenue was only \$43.6 million compared to budget estimates of \$56.1 million.



WOOD DUCK NEST BOX ON CUSHMAN WILDLIFE LANDS

Laying the groundwork for success

The year also saw the start of a new strategic plan, the direction and objectives of which will form the foundation for the next budget development process.

Tacoma Power's conservation programs continued to hit high notes, with yet another year of exceeding goals. The utility acquires energy conservation as a way to manage load growth by avoiding adding new, costly generation sources and thereby keeping rates low for customers. Conservation also provides homeowners and businesses technical assistance and financial incentives to reduce their cost of energy efficiency improvements. At the end of the 2014-15 biennium, the utility projected year-end savings of over 13 average megawatts – five more than the target.

Working with four partner agencies in 2015, Tacoma Power led a study of the energy savings of hybrid ductless heat pump/ electric resistance heating systems. The study found those heating systems to be more cost effective than all-electric resistance heating in new construction homes. Building codes in Washington were changed as a result, which will save money for electricity consumers across the state. The utility was recognized for that work by the Northwest Energy Efficiency Alliance, an agency that acknowledges outstanding achievement for innovative solutions that help Washington achieve more energy savings.

TACOMA POWER'S
CONSERVATION PROGRAMS
CONTINUED TO HIT
HIGH NOTES, WITH YET
ANOTHER **YEAR OF**
EXCEEDING GOALS.

Every year, Tacoma Power strives to improve its performance in the area of power outages by reducing the length of outages and how many people they effect. In 2015, the weather made that a particular challenge by delivering three significant storms instead of the more typical one. But the utility was prepared for those emergencies because of the work it does all year to trim trees and vegetation on hundreds of miles of power lines. That work is a major contributor to the high reliability of Tacoma Power's system and resulted in the ability to maintain an average number of customers who lost power across the year and the duration for which they were out.

Tacoma Power is proud to report that it continues recruitment and outreach efforts to increase diversity in its job applicant pools. That includes working with the military and veteran populations and fostering partnerships with schools to ensure a pipeline of qualified applicants. Tacoma Power also managed three apprenticeship programs and provided training and work experiences to almost 40 apprentices and trainees in 2015.



SOLAR PANELS ON TPU CAMPUS

FINANCIAL HIGHLIGHTS

In millions, for the years ended December 31,	2015	2014	2013	2012	2011
Total Income	\$413.7	\$447.0	\$418.8	\$400.2	\$377.4
Operating Expenses	319.2	314.0	296.1	285.0	264.4
Income Available for Debt Service	\$94.5	\$133.0	\$122.7	\$115.2	\$113.0
Debt Service	\$37.2	\$58.7	\$52.4	\$ 56.5	\$ 56.5
Debt Service Coverage	2.54x	2.26x	2.34x	2.04x	2.00x
Plant Additions	\$127.1	\$122.9	\$146.3	\$134.4	\$125.5
Number of Customers	174,562	172,531	171,506	169,012	169,112
Average Rates (per kWh)					
Residential	\$0.085	\$0.081	\$0.078	\$0.074	\$0.070
Commercial	\$0.087	\$0.084	\$0.081	\$0.077	\$0.072
General/Industrial	\$0.055	\$0.053	\$0.051	\$0.049	\$0.047

Sales of Electric Energy (dollars in millions)	2015	2014
Residential	149.20	150.97
Commercial	26.96	26.59
General	116.05	114.72
Contract	21.36	21.15
Bulk	50.38	82.8
Others	1.64	1.61

Total Consumption (mwh in millions)	2015	2014
Residential	1.76	1.85
Commercial	0.31	0.32
General	1.97	2.04
Contract	0.51	0.52
Others	1.95	2.88

Power Sources (mwh in millions)	2015	2014
Nisqually	0.51	0.64
Cushman	0.27	0.36
Cowlitz	1.63	2.11
BPA	3.67	3.85
Others	0.30	0.31

Operating Expenses	2015	2014
Purchased Power	\$ 126,315,151	33%
Depreciation	57,381,578	16%
Distribution & Transmission	47,400,006	15%
Admin. & Pension	45,977,299	13%
Other Operating Expenses	43,603,789	11%
Hydraulic Power	26,595,133	6%
Click! Network	25,304,001	5%
Other Production Expenses	3,999,158	1%

REPORT OF INDEPENDENT AUDITORS

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

Report on the Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Washington Department of Public Utilities, Power Division (the Division), which comprise the statements of net position as of December 31, 2015 and 2014, and the related statements of revenue, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Division as of December 31, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

Change in Accounting Principle

As discussed in Note 2 to the financial statements, effective January 1, 2015, the Division adopted requirements of Governmental Accounting Standards Board (GASB) Statement No. 68, Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27, and GASB Statement No. 71, Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68. The beginning net position has been adjusted for this change. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis on pages 5 through 13, schedule of proportionate share of net pension liability on page 48 and schedule of the city of Tacoma's contributions employer contributions on page 48 be presented to supplement the basic financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The statistical data presented on pages 50 through 66 and the superintendent's report presented on pages 67 through 81 are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and, accordingly, we express no opinion on it.

Miss Adams LLP

Tacoma, Washington
April 1, 2016

MANAGEMENT'S DISCUSSION & ANALYSIS

The following discussion and analysis of Tacoma Power's financial performance provides an overview of the financial activities for the years ended December 31, 2015 and 2014. 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 (GAAP) in the United States of America applied on a consistent basis and include amounts that are based on management's best estimates and judgment.

The basic financial statements, presented on a comparative basis for the years ended December 31, 2015 and 2014, include the Statements of Net Position, Statements of Revenues, Expenses and Changes in Net Position and Statements of Cash Flows. The Statements of Net Position present information on all of the Utility's assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference being reported as net position. The Statements of Revenues, Expenses and Changes in Net Position 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, non-capital financing, capital and related financing, and investing activities.

The Notes to 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.

With the implementation of Governmental Accounting Standards Board (GASB) Statement No. 68, the Division's 2015 beginning net position has been adjusted to conform to the new reporting and accounting requirements (See Note 2 to the Financial Statements). The year of 2014 has not been restated due to the unavailability of the historic information from the plan.

Financial Highlights

- Tacoma Power reported a decrease in total net position of \$1.6 million (106.6%) in 2015, compared to an increase of \$23.7 million (3.0%) in 2014.
- Operating revenues decreased \$30.6 million (6.9%) in 2015. Operating revenues in 2014 increased \$26.8 million (6.5%).
- Utility Plant in Service increased \$43.2 million (2.4%) in 2015 and \$43.7 million (2.5%) in 2014.
- Construction work in progress increased \$33.2 million (60.5%) in 2015 and \$31.4 million (134.1%) in 2014.

Overview of Financial Statements

Tacoma Power reported net operating income of \$34.1, \$68.1 and \$61.9 million in 2015, 2014 and 2013 respectively. Operating revenues decreased \$30.6 million during 2015 and operating expenses increased \$3.4 million. For 2014, operating revenues increased \$26.8 million and operating expenses increased \$20.7 million compared to 2013. Tacoma Power reported a decrease in net position of \$1.6 million in 2015 compared to an increase of \$23.7 million in 2014 and \$19.9 million in 2013.

The following tables highlight Tacoma Power's past three years' operating results and megawatt-hours billed.

Operating Results (in thousands)

Category	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Operating Revenues	\$ 410,626	\$ 441,246	\$ 414,462	\$ (30,620)	\$ 26,784
Operating Expenses	376,576	373,173	352,519	3,403	20,654
Net Operating Income	34,050	68,073	61,943	(34,023)	6,130
Net-Non Operating Expenses	(20,036)	(25,138)	(24,941)	5,102	(197)
Capital Contributions	5,708	4,120	5,200	1,588	(1,080)
BABs and CREBs subsidies	3,676	3,668	3,640	8	28
Transfers Out	(24,969)	(26,999)	(25,970)	2,030	(1,029)
Change in Net Position					
(Net Income)	\$ (1,571)	\$ 23,724	\$ 19,872	\$ (25,295)	\$ 3,852

Megawatt-Hours Billed (in thousands)

Type of Customer	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Residential	1,801	1,891	1,950	(90)	(59)
Commercial/General/Industrial	2,791	2,869	2,856	(78)	13
Wholesale	1,918	2,843	2,245	(925)	598
Total	6,510	7,603	7,051	(1,093)	552

Net Position

Net position may serve over time as a useful indicator of an entity's financial position. The following analysis highlights net position for the last three years.

Statements of Net Position (in thousands)

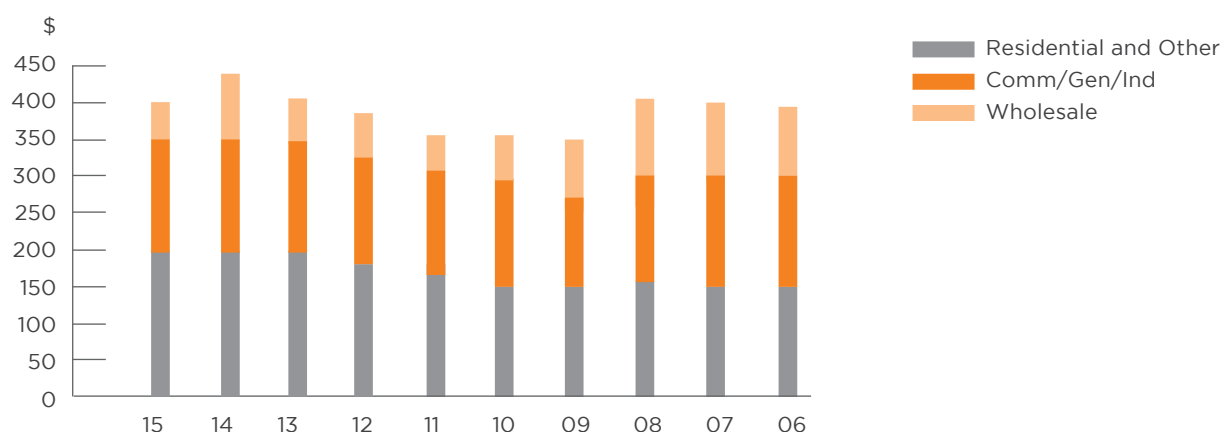
Description	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Net Utility and Non-Utility Plant	\$ 1,002,993	\$ 979,067	\$ 960,067	\$ 23,926	\$ 19,000
Current Assets, Other Assets and Special Funds	392,482	525,770	541,985	(133,288)	(16,215)
Total Assets	1,395,475	1,504,837	1,502,052	(109,362)	2,785
Deferred Outflows	10,977	8,026	15,941	2,951	(7,915)
Total Assets and Deferred Outflows	\$ 1,406,452	\$ 1,512,863	\$ 1,517,993	\$ (106,411)	\$ (5,130)
Net Position:					
Net Invested in Capital Assets	\$ 594,626	\$ 499,659	\$ 541,804	\$ 94,967	\$ (42,145)
Restricted	21,028	34,666	30,794	(13,638)	3,872
Unrestricted	210,279	288,478	226,481	(78,199)	61,997
Total Net Position	825,933	822,803	799,079	3,130	23,724
Long-Term Debt	441,928	530,581	564,961	(88,653)	(34,380)
Other Liabilities	86,555	111,479	105,953	(24,924)	5,526
Total Liabilities	528,483	642,060	670,914	(113,577)	(28,854)
Deferred Inflows	52,036	48,000	48,000	4,036	-
Total Net Position, Liabilities and Deferred Inflows	\$ 1,406,452	\$ 1,512,863	\$ 1,517,993	\$ (106,411)	\$ (5,130)

Revenues

2015 Compared to 2014

Operating revenues totaled \$410.6 million in 2015 compared to \$441.2 million in 2014, a decrease of \$30.6 million (6.9%). Revenues from general customers increased \$1.3 million (1.2%). There was a rate increase of 3.8% effective 2015, which was partially offset by a decrease of 62,000 MWh billed. Wholesale revenues in 2015 decreased \$32.4 million as compared to 2014. Streamflows in 2015 were 79% of 2014 streamflows, resulting in lower generation and therefore lower sales.

Operating Revenues (in millions)



In 2015 residential sales accounted for 41.4% of electric revenues, commercial and industrial revenues accounted for 44.8% and wholesale power revenues accounted for 13.8%.

2014 Compared to 2013

Operating revenues totaled \$441.2 million in 2014 compared to \$414.5 million in 2013, an increase of \$26.8 million (6.5%). Revenue from sales to residential and other customers decreased \$1.0 million. There was a 3.7% rate increase effective April 1, 2014 that was more than offset by a 60,000 decrease in MWh billed. Revenues from commercial, general, and industrial customers increased \$8.5 million primarily due to the rate increase effective April 1, 2014. The system average rate increase was 4.2%.

Telecommunications revenue increased \$0.9 million primarily due to a 10% rate increase in July 2014. Also, there was an increase in customer count for wholesale internet services.

Wholesale revenues in 2014 increased \$18.6 million as compared to 2013. Streamflows in 2014 were 130% of 2013 streamflows, resulting in higher generation and therefore higher sales.

In 2014 residential sales accounted for 38.3% of electric revenues, commercial and industrial revenues accounted for 40.9% and wholesale power revenues accounted for 20.8%.

Expenses

2015 Compared to 2014

Total operating expenses increased \$3.4 million or 0.9% compared to 2014.

Purchased power increased \$4.9 million (4.1%). Bonneville Power Administration (BPA) purchases increased \$8.1 million. The Slice and Block portions of the BPA contract increased \$3.1 million and credits for the Energy Conservation Agreement (ECA) decreased \$5.0 million. Purchases from Priest Rapids increased \$1.6 million. Part of the contract includes a credit for a portion of the proceeds of sale of the output from the project. Credits were less in 2015 than in 2014. Purchases from Grand Coulee Project Hydroelectric Authority increased \$0.3 million due to increased operating costs that were passed on to Tacoma Power. Other portfolio purchases decreased \$5.5 million primarily due to lower volume. Temperatures for most of the year were higher than normal and streamflows were lower.

Telecommunications expense increased \$5.7 million primarily due to an updated cost allocation between Power and Click! Previously, allocated costs were approximately 75% Click! and 25% Power. The cost allocation has been updated to reflect shared costs of approximately 94% to Click! and 6% to Power. This change was effective January 1, 2015.

Maintenance expense decreased \$5.6 million (16.8%). Generation maintenance increased \$0.5 million primarily due to a mechanical overhaul at Wynoochee. Distribution maintenance decreased \$2.6 million and Transmission maintenance expense decreased \$3.5 million. This is mostly due to the updated cost allocation between Power and Click!

Distribution operations expense decreased \$3.6 million (26.4%) primarily due to the updated cost allocation between Power and Click! and the implementation of GASB 68, resulting in a \$1.3 million decrease in pension expense.

Generation operations expense increased \$1.9 million (15.7%). Natural Resources costs increased \$1.3 million due to testing and operations of new fish related facilities and to hiring new personnel. Contributions to the Fleet Replacement Fund increased \$0.7 million.

2014 Compared to 2013

Total operating expenses increased \$20.7 million or 5.9% compared to 2013.

Purchased power decreased \$1.4 million (1.2%). Bonneville Power Administration (BPA) purchases decreased \$1.5 million. The Slice and Block portions of the BPA contract increased \$1.9 million and credits for the Energy Conservation Agreement (ECA) increased \$3.4 million. Purchases from Grand Coulee Project Hydroelectric Authority increased \$0.8 million due to a combination of increased volume and a small price increase. Other portfolio purchases decreased \$0.5 million due to increased generation as a result of higher streamflows.

Generation operations expense increased \$1.9 million (18.1%) primarily due to increased labor costs.

Distribution operations expense increased \$3.0 million (27.3%). The Transmission and Distribution section began contributing to the Fleet Replacement Fund for the first time this biennium in July, which accounts for \$2.6 million of the increase. The remainder is primarily increased labor costs, which include back wages due to a labor contract settlement.

Other operations expense increased \$1.6 million (12.5%). This is made up of a \$1.3 million increase in conservation and other customer assistance programs and an increase in other production expense of \$0.3 million. These increases included \$1.1 million in amortization of deferred conservation costs.

Maintenance expense increased \$5.6 million (20.2%). Generation maintenance increased \$2.5 million primarily due to an increase of \$0.9 million for painting of the penstocks at Cushman #2 and \$0.9 million for painting the spillway gate at Mayfield. Distribution maintenance increased \$3.3 million. The contributions to the Fleet Replacement Fund beginning in July make up \$1.2 million of this increase. The remainder is primarily due to increased labor costs and a decrease in time charged to capital projects. Transmission maintenance expense decreased \$0.2 million.

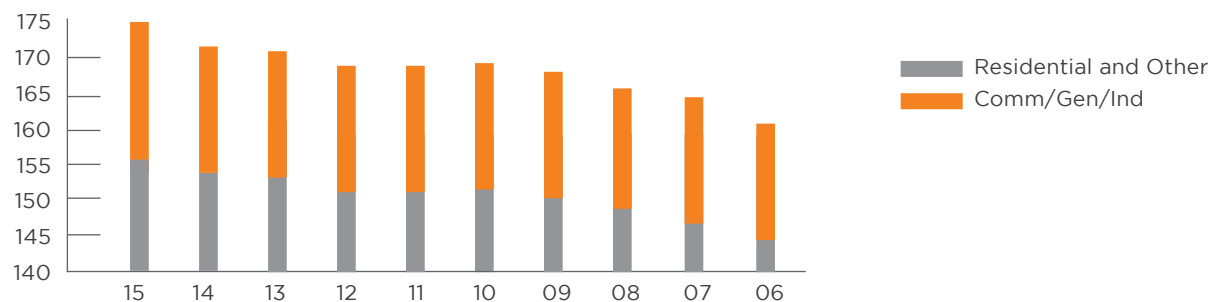
Administrative and general expenses increased \$6.0 million (11.5%) in 2014. Maintenance of general plant increased \$1.0 million, the credit for capitalized and general expense decreased \$0.8 million, and labor costs increased \$1.8 million.

Customer accounts expense increased \$2.2 million primarily due to an increase of \$1.5 million in customer records and collection expense and an increase of \$0.3 million in bad debt expense.

Customer Counts

Tacoma Power's overall customer growth during the past 10 years has been relatively steady averaging between less than 1% and 3% per year. The customer count for 2015 is 174,562 compared to 172,531 in 2014 and 171,506 in 2013.

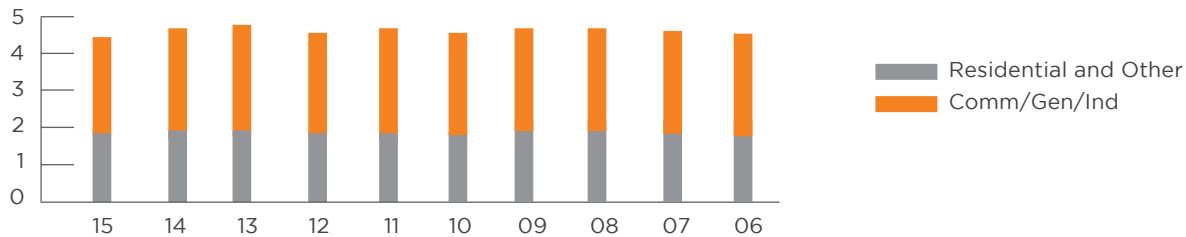
Number of Customers (in thousands)



Megawatt-hours Billed

Megawatt-hours billed to residential and other customers decreased 4.8% in 2015, while commercial/general/industrial billings increased 2.8%. Wholesale power billed in 2015 was 1,917,685 megawatt-hours compared to 2,842,694 in 2014, a decrease of 925,009 megawatt-hours or 32.5%. During 2015 hydro generation decreased 703 megawatt-hours compared to the previous year. Streamflows into Tacoma Power's system were 97% of average in 2015 compared to 125% of average in 2014.

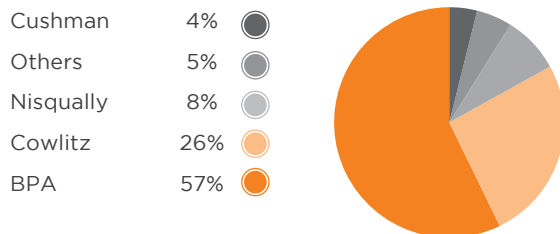
Megawatt-hours Billed (in millions)



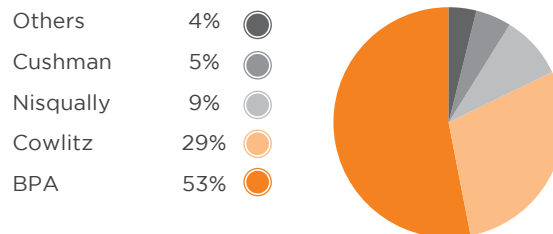
Sources of Power

Tacoma Power's total resources for power supply to serve its retail and wholesale customers for the last two years are shown in the following graphs.

Megawatt Hours Generated/Purchased - 2015



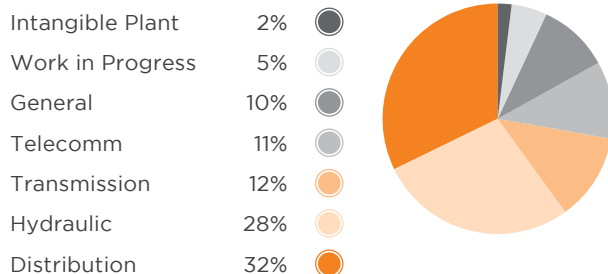
Megawatt Hours Generated/Purchased - 2014



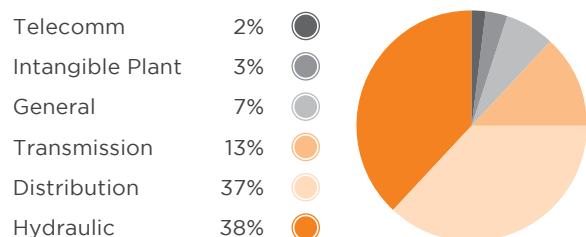
Utility Plant and Plant Additions

Tacoma Power has \$1.9 billion invested in its utility plant assets on a cost basis. The largest portion is for the combined distribution and transmission business unit, followed by its generation (hydroelectric) business unit. The following graphs show the allocation of plant additions and total investment in plant.

2015 Utility Plant

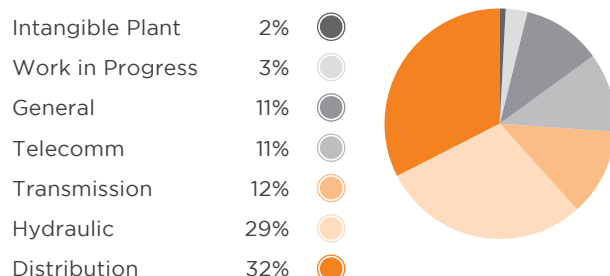


2015 Plant Additions

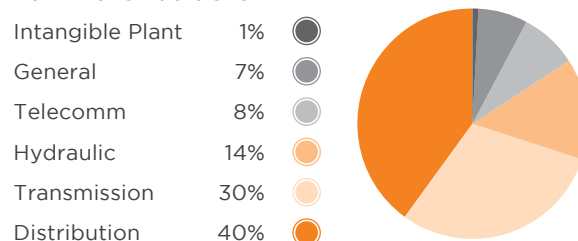


Additions to Hydraulic plant in 2015 were \$18.2 million, which included the Cushman fish hatcheries, Wynoochee modernization, and a hydro exciter replacement program. Distribution plant additions were \$17.3 million, which included addition and replacement programs for new services, pole replacements, and road related additions and replacements. Transmission plant additions were \$6.1 million, which included system reliability improvements and substation additions and replacements.

2014 Utility Plant



2014 Plant Additions



Additions to Hydraulic plant in 2015 were \$18.2 million, which included the Cushman fish hatcheries, Wynoochee modernization, and a hydro exciter replacement program. Distribution plant additions were \$17.3 million, which included addition and replacement programs for new services, pole replacements, and road related additions and replacements. Transmission plant additions were \$6.1 million, which included system reliability improvements and substation additions and replacements.

Additions in 2014 to distribution plant were \$18.3 million, which included addition and replacement programs for new services, pole replacements, and distribution transformers. Transmission plant additions were \$13.8 million, which included the North Bay Crossing Rehabilitation, system reliability improvements, and the salmon hatchery station upgrade. Hydraulic plant additions were \$6.4 million, which included the Cushman License Implementation and accessory electrical equipment at Alder and Wynoochee.

The following table summarizes Tacoma Power's capital assets, net of accumulated depreciation, for the years ended December 31, 2015 through 2013.

Capital Assets, Net of Accumulated Depreciation (in thousands)

Net Utility Plant	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Intangible Plant	\$ 29,404	\$ 29,510	\$ 29,949	\$ (106)	\$ (439)
Hydraulic Plant	359,992	349,472	350,698	10,520	(1,226)
Transmission Facilities	118,765	122,213	117,981	(3,448)	4,232
Distribution Facilities	284,826	288,242	290,152	(3,416)	(1,910)
General Plant	78,190	81,443	85,198	(3,253)	(3,755)
Telecommunications Plant	43,682	53,216	62,500	(9,534)	(9,284)
Construction Work in Progress	87,952	54,789	23,407	33,163	31,382
Total Net Utility Plant	\$ 1,002,811	\$ 978,885	\$ 959,885	\$ 23,926	\$ 19,000

Additional information on Tacoma Power's capital assets can be found in Note 3 of the financial statements and also in the supplementary Statistical Data.

Debt Administration

At December 31, 2015 Tacoma Power had outstanding revenue bonds of \$385.8 million, a decrease of \$154.3 million compared to 2014. In July 2015, Tacoma Power called \$122.1 million of Series 2005 B Electric System Revenue Bonds. No new revenue bonds were issued in 2015. On May 15, 2015 Tacoma Power entered into a 3-year line of credit agreement with Wells Fargo in the amount of \$100 million, of which draws were taken in the amount of \$50,250,000. Also, on May 1, 2015 Tacoma Power entered into a 3-year line of credit agreement with Key Bank in the amount of \$50 million, of which no draws were taken.

At December 31, 2014 Tacoma Power had outstanding revenue bonds of \$540.1 million, a decrease of \$28.3 million compared to 2013. No new bonds were issued in 2014.

All bonds are rated Aa3 by Moody's Investors Service, AA by Standard and Poor's and AA- by Fitch, Inc.

Additional information on Tacoma Power's long-term debt can be found in Note 5 of the financial statements.

Debt Service Coverage

Tacoma Power is required by its bond covenants to maintain a debt service coverage ratio of 1.25. In 2015, principal and interest were covered 2.54 times compared to 2.26 times in 2014 and 2.34 times in 2013.

Summary

The management of the Finance Department of the City of Tacoma is responsible for preparing the accompanying financial statements and for their integrity. We prepared the financial statements according to GAAP in the United States of America, and they fairly portray Tacoma Power's financial position and operating results. The Notes to Financial Statements are an integral part of the basic financial statements and provide additional financial information.

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 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/CEO



Andrew Cherullo
Finance Director

2015 FINANCIAL REPORTS

STATEMENTS OF NET POSITION

Assets and Deferred Outflows

December 31,	2015	2014
Utility Plant		
In Service, at Original Cost	\$ 1,861,142,589	\$ 1,817,897,475
Less - Accumulated Depreciation	(946,283,353)	(893,801,525)
Total	914,859,236	924,095,950
Construction Work in Progress	87,951,638	54,789,325
Net Utility Plant	1,002,810,874	978,885,275
Non-Utility Property	182,051	182,051
Special Funds		
Construction Funds	41,412,285	51,136,534
Debt Service Funds	24,549,803	45,458,725
Special Bond Reserve Funds	4,984,302	17,003,212
Wynoochee Reserve Funds	2,534,915	2,520,923
Total Special Funds	73,481,305	116,119,394
Current Assets		
Operating Funds Cash and Equity in Pooled Investments	193,804,373	287,949,952
Accounts Receivable (Net of Allowance for Doubtful Accounts of \$1,080,447 in 2015 and \$1,079,721 in 2014)	30,667,987	35,210,149
Accrued Unbilled Revenue	29,427,771	28,750,681
Materials and Supplies	6,318,431	5,544,073
Interfund Receivables	1,484,313	2,509,436
Prepayments and Other	5,757,216	5,209,061
Total Current Assets	267,460,091	365,173,352
Other Assets		
Regulatory Asset - Conservation (Net of Amortization of \$18,629,468 in 2015 and \$13,063,221 in 2014)	46,293,923	42,599,246
Net Pension Asset	3,823,476	—
Conservation Loans Receivable	1,423,037	1,877,469
Total Other Assets	51,540,436	44,476,715
Total Assets	1,395,474,757	1,504,836,787
Deferred Outflows Of Resources		
Deferred Outflow for Pensions	9,077,586	—
Unamortized Loss on Refunding Bonds	1,899,931	8,026,229
Total Deferred Outflows	10,977,517	8,026,229
Total Assets and Deferred Outflows	\$ 1,406,452,274	\$ 1,512,863,016

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

Net Position, Liabilities and Deferred Inflows

December 31,	2015	2014
Net Position		
Net Investment in Capital Assets	\$ 594,626,313	\$ 499,658,478
Restricted for:		
Wynoochee Reserve Funds	2,534,915	2,520,923
Debt Service Funds	14,669,173	32,145,520
Net Pension Asset	3,823,476	
Unrestricted	210,279,420	288,478,140
Total Net Position	825,933,297	822,803,061
Long-Term Debt		
Revenue Bonds	391,678,130	530,580,510
Revolving Line of Credit	50,250,000	—
Total Long-Term Debt	441,928,130	530,580,510
Current Liabilities		
Current Portion of Long-Term Debt	14,735,000	32,115,000
Taxes and Other Payables	20,356,768	18,321,909
Purchased Power Payable	12,013,478	11,560,184
Salaries, Wages and Compensated Absences Payable	2,487,419	5,598,198
Interest Payable	9,880,630	13,313,205
Customers' Deposits	3,108,808	2,897,268
Interfund Payables	1,324,441	2,970,410
Total Current Liabilities	63,906,544	86,776,174
Long-Term Liabilities		
Long Term Accrued Compensated Absences	9,522,650	9,434,785
Other Long Term Liabilities	13,125,264	15,268,486
Total Long Term Liabilities	22,647,914	24,703,271
Total Liabilities	528,482,588	642,059,955
Deferred Inflows of Resources		
Deferred Inflow for Pensions	4,036,389	—
Rate Stabilization	48,000,000	48,000,000
Total Deferred Inflows	52,036,389	48,000,000
Total Net Position, Liabilities and Deferred Inflows	\$ 1,406,452,274	\$ 1,512,863,016

Statements of Revenues, Expenses and Changes In Net Position

Year Ended December 31,	2015	2014
Operating Revenues		
Sales of Electric Energy	\$ 366,263,055	\$ 397,175,394
Other Operating Revenue	17,106,442	16,920,147
Click! Network Operating Revenue	27,256,718	27,150,566
Total Operating Revenue	410,626,215	441,246,107
Operating Expenses		
Operations		
Purchased and Interchanged Power	126,315,151	121,395,343
Generation	14,197,116	12,273,808
Transmission	21,928,763	21,267,033
Distribution	10,163,887	13,806,687
Other	15,025,954	14,443,310
Maintenance	27,705,373	33,298,099
Telecommunications Expense	25,304,001	19,631,153
Administrative and General	58,560,459	58,625,611
Depreciation	57,381,578	59,156,228
Taxes	19,993,833	19,276,216
Total Operating Expenses	376,576,115	373,173,488
Net Operating Income	34,050,100	68,072,619
Non-Operating Revenues (Expenses)		
Interest Income	1,796,071	3,780,834
Contribution to Family Need	(480,000)	(900,000)
Other	(1,923,329)	(728,908)
Interest on Long-Term Debt	(19,225,735)	(24,621,702)
Loss on Defeasance or Refunding of Debt and Amortization of Debt Premium	(202,938)	(2,668,319)
Total Non-Operating Expenses	(20,035,931)	(25,138,095)
Net Income Before Capital Contributions and Transfers	14,014,169	42,934,524
Capital Contributions		
Cash	5,183,295	4,024,873
Donated Fixed Assets	524,713	95,492
BABs and CREBs Interest Subsidies	3,675,836	3,667,927
Transfers		
City of Tacoma Gross Earnings Tax	(25,481,823)	(26,860,649)
Transfers to/(from) Other Funds	512,401	(137,766)
Change in Net Position	(1,571,409)	23,724,401
Total Net Position - Beginning of Year	822,803,061	799,078,660
Accumulated Adjustment for Change in Accounting Principle	4,701,645	
Net Position, Beginning of Year, As Adjusted	827,504,706	
Total Net Position - End Of Year	\$ 825,933,297	\$ 822,803,061

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

Statements Of Cash Flows

Year to Date December 31,	2015	2014
Cash Flows From Operating Activities		
Cash from Customers	\$ 414,491,290	\$ 435,728,792
Cash Paid to Suppliers	(206,195,837)	(188,794,275)
Cash Paid to Employees	(106,153,040)	(107,884,909)
Taxes Paid	(19,876,260)	(19,840,137)
Conservation Loans	454,432	(569,620)
Net Cash From Operating Activities	82,720,585	118,639,851
Cash Flows From Non-Capital Financing Activities		
Transfer Out for Gross Earnings Tax	(25,481,823)	(26,860,649)
Transfer to/from Other Funds	512,401	(137,766)
Transfer to Family Need Fund	(480,000)	(900,000)
Net Cash From Non-Capital Financing Activities	(25,449,422)	(27,898,415)
Cash Flows From Capital and Related Financing Activities		
Capital Expenditures	(77,374,831)	(76,056,034)
Proceeds from Issuance of Long-Term Debt	50,250,000	-
Debt Issuance Costs	(114,250)	-
Principal Payments on Long-Term Debt	(32,115,000)	(28,295,000)
Payments for Early Extinguishment of Debt	(122,135,000)	-
Interest Paid	(26,065,944)	(27,758,620)
BABs and CREBs Interest Subsidies	3,675,836	3,667,927
Contributions in Aid of Construction	5,183,295	4,024,873
Other Long-Term Liabilities	763,091	1,458,092
Net Cash From Capital and Related Financing Activities	(197,932,803)	(122,958,762)
Cash Flows From Investing Activities		
Interest Received	1,796,071	3,780,834
Termination of Repurchase Agreement	-	8,761,250
Other Non-Op Revenues and Deductions	2,081,901	2,252,519
Net Cash From Investing Activities	3,877,972	14,794,603
Net Change in Cash and Equity in Pooled Investments	(136,783,668)	(17,422,723)
Cash and Equity in Pooled Investments at January 1	404,069,346	421,492,069
Cash and Equity in Pooled Investments at December 31	\$ 267,285,678	\$ 404,069,346

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

Statements of Cash Flows

December 31,

2015

2014

Reconciliation of Net Operating Income to Net Cash Provided by Operating Activities:

Net Operating Income	\$ 34,050,100	\$ 68,072,619
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	57,381,578	59,156,228
Amortization of Regulatory Assets	5,566,247	4,743,698
Pension (Credits) Expenses	(4,163,028)	—
Cash provided from changes in operating assets and liabilities:		
Accounts Receivable and Accrued Unbilled Revenue	3,865,072	(5,517,318)
Conservation Loans Receivable	454,432	(569,621)
Interfund Receivables	1,025,123	(650,454)
Materials and Supplies, and Other	(1,322,513)	250,634
Taxes and Other Payables	(871,453)	(581,569)
Purchased Power Payable	453,294	(546,378)
Salaries and Wages	(3,120,542)	467,268
Accrued Compensated Absences	97,628	218,108
Customers' Deposits	211,540	116,199
Regulatory Asset - Conservation	(9,260,924)	(8,225,484)
Interfund Payables	(1,645,969)	1,705,921
Total Adjustments	48,670,485	50,567,232
Net Cash From Operating Activities	\$ 82,720,585	\$ 118,639,851

Reconciliation of Cash and Equity in Pooled Investments to

Balance Sheet:

Cash and Equity in Pooled Investments in Special Funds	\$ 73,481,305	\$ 116,119,394
Cash and Equity in Pooled Investments in Operating Funds	193,804,373	287,949,952
Cash and Equity in Pooled Investments at December 31	\$ 267,285,678	\$ 404,069,346

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2015 AND 2014

NOTE 1 OPERATIONS

Operations of Tacoma Power - The Light Division, doing business as Tacoma Power (Tacoma Power or the Division), is a division of the City of Tacoma, Washington (the City), Department of Public Utilities (the Department) and is included as an enterprise fund in the Comprehensive Annual Financial Report (CAFR) of the City. 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 setting of utility rates and charges, are initiated and executed by the Board, but also require formal City Council approval. Tacoma Power owns and operates the City's electrical generation and distribution facilities and telecommunication infrastructure. Tacoma Power serves approximately of 174,562 retail customers and has 953 employees. Tacoma Power is organized into six business units: Generation, Power Management, Transmission and Distribution, Rates, Planning and Analysis, Click! Network, and Utility Technology Services.

Generation operates four hydroelectric generating projects (Cowlitz, Cushman, Nisqually and Wynoochee) and the associated recreational facilities, fish hatcheries and other project lands.

Power Management manages the power supply portfolio, markets bulk and ancillary power supply services, schedules and dispatches division-owned generation and contract power supplies and performs power trading and risk management activities. Revenues and the cost of electric power purchases vary from year to year depending on the electric wholesale power market, which is affected by several factors including the availability of water for hydroelectric generation, marginal fuel prices and the demand for power in other areas of the country.

Transmission and Distribution plans, constructs, operates and maintains the transmission and distribution systems including substations, the underground network system, supervisory control and data acquisition (SCADA) systems, revenue metering facilities and all overhead transmission and distribution systems. Electricity use by retail customers varies from year to year primarily because of weather conditions, customer growth, the economy in Tacoma Power's service area, conservation efforts, appliance efficiency and other technology.

Rates, Planning And Analysis plans for and manages the retail rate process, financial planning, analysis and modeling, budget strategies, the capital program and risk management.

Click! Network plans, constructs, operates and maintains a hybrid fiber coaxial (HFC) telecommunications network that supports the operation of Tacoma Power's electrical transmission and distribution system, provides retail cable TV and wholesale high-speed Internet services to residential and business customers, and data transport services to retail customers.

Utility Technology Services (UTS) maintains communication networks, operational and informational technology systems, and related equipment and infrastructure to optimize utility operations and improve reliability and service quality. This includes a Project Management Office that establishes and leads Tacoma Public Utilities Information Systems project governance process and implements project portfolio management tools. UTS is responsible for all matters related to Tacoma Power's compliance with North American Electric Reliability Corporation (NERC) Reliability Standards, maintains overall responsibility for the NERC Reliability Standards and manages TacomaPower's Internal Reliability and Compliance Project.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting and Presentation - The financial statements of the Division are prepared under the accrual basis of accounting in accordance with generally accepted accounting principles (GAAP) issued by the Governmental Accounting Standards Board (GASB) applicable to governmental entities that use proprietary fund accounting. The financial statements use a flow of economic resources measurement focus to determine financial position and the change in financial position. The accounting principles used are similar to those applicable to businesses in the private sector and are maintained on the accrual basis of accounting. Revenues are recognized when earned, and costs and expenses are recognized when incurred.

The Division follows the provisions set forth in regulatory accounting guidance. In general, regulatory accounting 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.

The Division accounts are maintained substantially in accordance with the uniform system of accounts prescribed by the Federal Energy Regulatory Commission and the Division of Audits of the State Auditor's Office.

Change in Accounting Principle - In fiscal year 2015, the Division implemented GASB Statement No. 68, Accounting and Financial Reporting for Pensions and GASB Statement No. 71, Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68. The primary objective of GASB Statement No. 68 is to improve accounting and financial reporting by state and local governments for pensions. GASB Statement No. 68 establishes standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expenses. For defined benefit pension plans, this statement identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value and attribute that present value to periods of employee service. In addition, prior to implementing GASB Statement No. 68, employers participating in a cost-sharing plan recognized annual pension expense essentially equal to their contractually required contribution to the plan. Upon adoption of GASB Statement No. 68, employers participating in cost-sharing plans recognize their proportionate share of the collective pension amounts for all benefits provided through the plan based on an allocation methodology. GASB Statement No. 71 amends GASB Statement No. 68 regarding the deferred outflows of resources for governments whose current year pension contributions are reported subsequent to the measurement date. The collective financial impact resulting from the implementation of GASB Statements No. 68 and 71 is the adjustment of 2015 beginning balances by \$4,701,645 for the Division's portion of the net pension asset or liability and related deferrals incurred in prior years. See Note 9 for further details.

Cash, Special Funds and Equity in Pooled Investments - The Division's fund cash balances are a "deposit" with the City Treasurer's Tacoma Investment Pool (TIP) for the purpose of maximizing interest earnings through pooled investment activities. Cash and equity in pooled investments in the TIP are reported at fair value and changes in unrealized gains and losses are recorded in the Statements of Revenues, Expenses and Changes in Net Position. Interest earned on such pooled investments is allocated daily to the participating funds based on each fund's daily equity in the TIP.

The TIP operates like a demand deposit account in that all City departments, including the Division, have fund balances which are their equity in the TIP. Accordingly, balances are considered to be cash equivalents.

The City of Tacoma Investment Policy permits legal investments as authorized by state law including Certificates of Deposit with qualified public depositories (as defined in Chapter 39.58 of the Revised Code of Washington (RCW)), obligations of the U.S. Treasury, Government Sponsored Agencies and Instrumentalities, bonds issued by Washington State and its Local Governments with an A or better rating, general obligation bonds issue by any State or Local Government with an A or better rating, Bankers' Acceptances, Commercial Paper, Repurchase and Reverse Repurchase agreements, and the Washington State Local Government Investment Pool (LGIP). Daily liquidity requirement to meet the City's daily obligations is maintained by investing a portion of the City's Investment Pool in the LGIP and in a certificate of deposit with East West Bank.

The Division's equity in that portion of the City of Tacoma Investment Pool held in qualified public depositories at December 31, 2015 and 2014 is entirely covered by the Federal Deposit Insurance Corporation (FDIC) and the Washington State Public Deposit Protection Commission (WSPDPC).

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, longer term investments have greater exposure to changes in market interest rates. The City of Tacoma investment policy allows for authorized investments up to 60 months to maturity. One way the City manages its exposure to interest rate risk is by timing cash flows from maturities so that portions of the portfolio are maturing over time to provide cash flow and liquidity needed for operations.

Credit risk is generally the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Repurchase agreements and commercial paper are protected by the FDIC insurance up to \$250,000.

All deposits not covered by the FDIC are covered by the WSPDPC. The WSPDPC is a statutory authority established under RCW 39.58. It constitutes a fully insured or fully collateralized pool. The LGIP is authorized by RCW 43.250. The LGIP operated like a 2A7 fund and is collateralized by short-term legal investments.

Special Funds - In accordance with bond resolutions, agreements and laws, separate restricted funds have been established. These funds consist of cash and investments in pooled investments with restrictions externally imposed and legally enforceable, established by the City Council. Generally, restricted assets include bond construction, reserve and debt service funds and customer deposits.

Receivables and Unbilled Revenues - Accounts receivable consist of amounts owed by private individuals and organizations for goods delivered or services rendered in the regular course of business operations. Receivables are shown net of allowances for doubtful accounts. The Division accrues an estimated amount for services that have been provided but not billed as of December 31st.

Allowance for Doubtful Accounts - A reserve has been established for uncollectible accounts receivable based on historical write-off trends and knowledge of specific circumstances that indicate collection of an account may be unlikely. Generally accounts receivable are considered past due after 30 days.

Interfund Transactions - Unsettled transactions between funds at year end are recorded as due to or due from other funds.

Materials And Supplies - Materials and supplies consist primarily of items for maintenance and construction of Division assets and are valued at the lower of average cost or fair market value.

Bond Premium and Loss on Refunding - Bond premiums are amortized over the life of the bonds using a straight-line basis. Losses on refunding are amortized on a straight-line basis over the applicable bond period.

Regulatory Asset Conservation - The Division has deferred conservation costs to be charged to future periods matching the time when the revenues and expenses are included in rates. Conservation assets represent installation of savings measures at the properties of its customers. The deferred balance is reduced as costs are recovered and are amortized as other operating expense on the statements of revenues, expenses and changes in net position.

Utility Plant and Depreciation - Utility plant is stated at original cost, which includes both direct costs of construction or acquisition and indirect costs. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and betterments is capitalized. Assets are capitalized when costs exceed \$5,000 and the useful life exceeds one year.

Depreciation is recorded using a straight-line composite method based on FERC recommended economic asset lives from 2 to 62 years for related operating assets placed in service at the beginning of the year. The original cost of property together with removal cost, less salvage, is charged to accumulated depreciation at such time as property is retired and removed from service.

The economic lives for plant in service are as follows:

Intangible Plant	2-37 years
Hydraulic Production Plant	62 years
Transmission Plant	29 years
Distribution Plant	27 years
Regional Transmission	5-27 years
General Plant	19 years
Telecommunications Plant	5-19 years

Construction Work in Progress – Capitalizable costs incurred on projects which are not in service or ready for use are held in construction in progress. When the asset is ready for service, related costs are transferred to capital assets. Upon determining that a project will be abandoned, the related costs are charged to expense.

Asset Valuation - The Division 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 flows.

Allowance for Funds Used During Construction (AFUDC) - AFUDC represents the cost of borrowed funds used for the construction of utility plant, net of interest earned on unspent construction funds. Capitalized AFUDC is shown as part of the cost of utility plant and as a reduction of interest income and expense.

Intangible Assets - In accordance with GASB No. 51, "Accounting and Financial Reporting for Intangible Assets", land use rights such as easements and right-of-ways are recorded as intangible assets.

Capital Contributions - In accordance with GASB No. 33, "Accounting and Financial Reporting for Nonexchange Transactions", capital grants and capital contributions are recorded as capital contributions.

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 personal time off (PTO) 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. Based on historical information, 10% of compensated absences are considered short term.

Employees in the original policy accumulate sick leave at the rate of one day per month with no maximum accumulation specified. Employees receive 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.

Rate Stabilization Account - The Division has established a rate stabilization account to reduce significant year-to-year variations in rates. Amounts deposited into the account are excluded from the statement of revenues, expenses and changes in net position in accordance with regulated operations. Revenue will be recognized in subsequent periods when it is withdrawn in accordance with rate decisions.

Operating Revenue - 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 electricity. Utility revenue from power sales and power transmission is recognized when power is delivered to and received by the customer.

Non-Operating Revenues and Expenses - These are items that do not qualify as operating defined above.

Taxes - The City charges the Division a Gross Earnings Tax at the rate of 6.0% on electrical revenues and broadband revenues and 8.0% on cable television revenues. On Tacoma cable television revenues only, the City also charges the Division a franchise fee of 5.0% and a Public, Educational and Government access television (P.E.G.) fee of 1.0%. In addition, the Division pays a 3.8734% public utility tax to the State on a certain portion of revenues identified as utility revenues. The Division also pays business and occupation tax to the State at the rate of 1.5% on certain other non-utility revenues including cable television revenues, as well as 0.484% for Wholesaling and Broadcasting and 0.471% for Retailing. The Division is exempt from payment of federal income tax.

Net Position - The Statement of Net Position reports all financial and capital resources. The difference between assets and liabilities is net position. There are three components of net position: net investment in capital assets, restricted and unrestricted.

Net investment in capital assets consists of capital assets, less accumulated depreciation, reduced by the outstanding balances of any bonds, loans or other borrowings, less outstanding construction funds, that are attributable to the acquisition, construction, or improvements of those assets.

Net position components are restricted when constraints placed on net position use are either (1) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or (2) imposed by law through constitutional provisions or enabling legislation.

Unrestricted net position components are those that are not “net investment in capital assets” or “restricted”.

Arbitrage Rebate Requirement - The Division is subject to the Internal Revenue Code (“IRC”), Section 148(f), related to its tax-exempt revenue bonds. The IRC requires that earnings on gross proceeds of any revenue bonds that are in excess of the amount prescribed will be surrendered to the Internal Revenue Service. As such, the Division would record such a rebate as a liability. The Division had no liability in the current or prior year.

Shared Services - The Division receives certain services from other departments and agencies of the City, including those normally considered to be general and administrative. The Division is charged for services received from other City departments and agencies.

Use of Estimates - The preparation of the financial statements in conformity with GAAP in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. The Division used estimates in determining reported unbilled revenues, allowance for doubtful accounts, accrued compensated absences, depreciation, Other Post Employment Benefits (OPEB), pension, self-insurance liabilities and other contingencies. Actual results may differ from these estimates.

Family Need - The Family Need program is Tacoma Power's low income bill assistance program. Contributions are received from customers, employees and Tacoma Power. The Family Need program is administered by the Metropolitan Development Council and Pierce County Community Services which identify and certify the eligibility of Tacoma Power customers for the program.

Significant Risks and Uncertainties - The Division is subject to certain business risks that could have a material impact on future operations and financial performance.

These risks include, but are not limited to, water conditions, weather and natural disaster related disruptions, collective bargaining labor disputes, fish and other endangered species act issues, Environmental Protection Agency regulations, federal government regulations or orders concerning the operation, maintenance and/or licensing of facilities.

NOTE 3 UTILITY PLANT

A summary of the balances and changes in utility plant for 2015 and 2014 follows:

	Balance December 31, 2014	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2015
Intangible Plant	\$ 40,584,864	\$ 1,287,650	\$ (190,162)	\$ —	\$ 41,682,352
Hydraulic Production Plant	536,424,903	18,212,750	—	—	554,637,653
Transmission Plant	215,039,287	5,495,463	(616,709)	—	219,918,041
Distribution Plant	604,029,355	17,270,360	(2,901,740)	—	618,397,975
Regional Transmission	17,537,662	609,899	—	—	18,147,561
General Plant	197,036,437	3,204,314	—	(80,328)	200,160,423
Telecommunications Plant	207,244,967	953,617	—	—	208,198,584
Total Utility Plant In Service	1,817,897,475	47,034,053	(3,708,611)	(80,328)	1,861,142,589
Less Accumulated Depreciation	893,801,525	57,381,578	(5,130,255)	230,505	946,283,353
	924,095,950	(10,347,525)	1,421,644	(310,833)	914,859,236
Construction Work In Progress	54,789,325	80,107,465	—	(46,945,152)	87,951,638
Net Utility Plant	\$ 978,885,275	\$ 69,759,940	\$ 1,421,644	\$ (47,255,985)	\$ 1,002,810,874

	Balance December 31, 2013	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2014
Intangible Plant	\$ 39,932,284	\$ 652,709	\$ (129)	\$ —	\$ 40,584,864
Hydraulic Production Plant	530,076,778	6,440,105	(91,980)	—	536,424,903
Transmission Plant	203,001,100	12,613,236	(575,049)	—	215,039,287
Distribution Plant	586,974,920	18,262,758	(1,208,323)	—	604,029,355
Regional Transmission	16,320,490	1,217,172	—	—	17,537,662
General Plant	194,039,551	2,996,886	—	—	197,036,437
Telecommunications Plant	203,842,399	3,727,992	(11,320)	(314,104)	207,244,967
Total Utility Plant In Service	1,774,187,522	45,910,858	(1,886,801)	(314,104)	1,817,897,475
Less Accumulated Depreciation	837,709,188	59,156,228	(1,794,691)	(1,269,200)	893,801,525
	936,478,334	(13,245,370)	(92,110)	955,096	924,095,950
Construction Work In Progress	23,406,935	76,979,144	—	(45,596,754)	54,789,325
Net Utility Plant	\$ 959,885,269	\$ 63,733,774	\$ (92,110)	\$ (44,641,658)	\$ 978,885,275

Total Utility Plant in Service includes non-depreciable assets of \$75,310,858 for 2015 and \$74,763,487 for 2014. The total amount of interest cost incurred and capitalized is \$3,407,633 for 2015 and \$2,004,709 for 2014.

NOTE 4 SPECIAL FUNDS

Cash and equity in pooled investments and investments included in Tacoma Power's Special Funds consist of:

Cash and Equity in Pooled Investments	2015	2014
Construction Funds	\$ 41,412,285	\$ 51,136,534
Debt Service Funds	24,549,803	45,458,725
Wynoochee Reserve	2,534,915	2,520,923
Special Bond Reserve	4,984,302	17,003,212
Total	\$ 73,481,305	\$ 116,119,394

NOTE 5 LONG-TERM DEBT

Tacoma Power's long-term debt is primarily for capital improvements. Long-term liability activity for the years ended December 31, 2015 and December 31, 2014 was as follows:

	Balance December 31, 2014	Additions	Reductions	Balance December 31, 2015	Due Within One Year
Revenue Bonds	\$ 540,050,000	\$ —	\$ (154,250,000)	\$ 385,800,000	\$ 14,735,000
Plus: Unamortized Premium	22,645,510	—	(2,032,380)	20,613,130	—
Net Revenue Bonds	562,695,510	—	(156,282,380)	406,413,130	14,735,000
Line of Credit	—	50,250,000	—	50,250,000	—
Total Long-Term Debt	\$ 562,695,510	\$ 50,250,000	\$ (156,282,380)	\$ 456,663,130	\$ 14,735,000

	Balance December 31, 2013	Additions	Reductions	Balance December 31, 2014	Due Within One Year
Revenue Bonds	\$ 568,345,000	\$ —	\$ (28,295,000)	\$ 540,050,000	\$ 32,115,000
Plus: Unamortized Premium	24,910,765	—	(2,265,255)	22,645,510	—
Total Long-Term Debt	\$ 593,255,765	\$ —	\$ (30,560,255)	\$ 562,695,510	\$ 32,115,000

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

	2015	2014
2005A Revenue Bonds, with interest rates ranging from 3.5% to 4.3%, due in yearly installments of \$115,000 to \$13,275,000 through 2016. Original Issue: \$93,480,000 Current Portion: \$130,000	\$ 130,000	\$ 130,000
2005B Refunding Bonds, with interest rates ranging from 3.5% to 5.0%. Original Issue: \$156,425,000 Current Portion: \$0	—	122,135,000
2007 Refunding Bonds, with interest rates ranging from 4.0% to 5.0%, due in yearly installments of \$10,485,000 to \$23,300,000 through 2015. Original Issue: \$81,130,000 Current Portion: \$0	—	21,300,000
2010A Revenue Bonds, with interest rates ranging from 2.0% to 5.0%, due in yearly installments of \$8,000,000 from 2014 to 2015. Original Issue: \$16,000,000 Current Portion: \$0	—	8,000,000
2010B Revenue Bonds, with interest rates ranging from 5.791% to 5.966%, with a Build America Bond (BAB) rebate at 35% of interest, due in yearly installments of \$27,310,000 to \$31,630,000 from 2031 to 2035. Original Issue: \$147,070,000 Current Portion: \$0	147,070,000	147,070,000
2010C Revenue Bonds, with an interest rate of 5.641%, with Clean Renewal Energy Bond rebate at 67% of interest, due in one payment of \$24,185,000 in 2027. Original Issue: \$24,185,000 Current Portion: \$0	24,185,000	24,185,000
2013A Refunding Bonds, with interest rates ranging from 4.0% to 5.0%, due in yearly installments of \$2,815,000 to \$29,165,000 through 2042. Original Issue: \$181,610,000 Current Portion: \$14,605,000	\$ 178,795,000	\$ 181,610,000

	2015	2014
2013B Refunding Bonds, with interest rates ranging from 3.05% to 5.0%, due in yearly installments of \$3,795,000 to \$5,155,000 through 2030.		
Original Issue: \$35,620,000	35,620,000	35,620,000
Current Portion: \$0		
	385,800,000	540,050,000
Unamortized Premium	20,613,130	22,645,510
Unamortized Discount	—	—
Current Portion	(14,735,000)	(32,115,000)
Long-term Portion of Revenue Bond Debt	391,678,130	530,580,510
Revolving Line of Credit	50,250,000	—
Total Long Term Debt	\$ 441,928,130	\$ 530,580,510

In 2015, Tacoma Power entered into a \$100 million line-of-credit agreement with Wells Fargo for working capital. The line matures in May 2018, and each advance will bear interest at the London Interbank Offered Rate (LIBOR). Each advance is secured by Revenues as set forth in the Note Ordinance. The balance outstanding is \$50.3 million as of December 31, 2015.

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

	Principal	Interest
2016	\$ 14,735,000	\$ 19,393,535
2017	\$ 12,730,000	\$ 18,707,560
2018	\$ 11,575,000	\$ 18,157,810
2019	\$ 10,095,000	\$ 17,698,935
2020	\$ 29,165,000	\$ 16,792,435
2021-2025	\$ 28,330,000	\$ 76,555,149
2026-2030	\$ 43,445,000	\$ 68,326,826
2031-2035	\$ 147,070,000	\$ 46,310,876
2036-2040	\$ 60,590,000	\$ 12,429,450
2041-2042	\$ 28,065,000	\$ 1,133,700
	\$ 385,800,000	\$ 295,506,276

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

As of December 31, 2015, the following outstanding bonds were considered defeased:

Issue	Amount
1964 Light & Power Bonds	\$ 1,235,000
1965 Light & Power Bonds	3,360,000
1967 Light & Power Bonds - Series A & B	2,825,000
1969 Light & Power Bonds	2,260,000
1979 Light & Power Bonds	5,475,000
2005 Electric System Revenue Bonds - Series A	230,000
2005 Electric System Revenue Bonds - Series B	27,460,000
2007 Electric System Revenue Refunding Bonds	14,540,000
	<u>\$ 57,385,000</u>

These refunded bonds constitute a contingent liability of Tacoma Power only to the extent that cash and investments presently in the control of the refunding trustees are not sufficient to meet debt service requirements, and are therefore excluded from the financial statements because the likelihood of additional funding requirements is considered remote.

NOTE 6 PURCHASED POWER

Tacoma Power purchased electric power and energy from BPA under a long-term contract that expires on September 30, 2028. The contract consists of a base rate per kWh and certain cost-recovery adjustment clauses can be invoked under particular circumstances.

On December 1, 2008, the Board authorized the execution of a twenty-year Slice/Block Power Sales and Creditworthiness Agreement with BPA. The agreement allows Tacoma Power to purchase a Slice/Block power product from BPA which began October 1, 2011 and continues through September 30, 2028. In broad terms, the agreement requires Tacoma Power to purchase a firm amount (Block) and proportionate share (Slice) of power based on a number of criteria and calculations. This is a take or pay arrangement which allows Tacoma Power to remarket excess capacity. The related Creditworthiness Agreement provides for BPA to conduct a credit review of Tacoma Power. To determine if a letter of credit or cash deposit would be required, BPA completed this review and determined that as long as Tacoma Power's credit rating remains above BBB-, no Letter of Credit or cash deposit will be required.

The power received under this contract averaged approximately 419,422 and 439,003 kilowatts per hour for 2015 and 2014, respectively. Charges for the BPA purchased power were approximately \$112 million and \$104 million for 2015 and 2014, respectively, and are based on the total amount of energy delivered and the monthly peak power demand.

Under fixed contracts with other power suppliers, Tacoma Power has agreed to purchase portions of the output of certain generating facilities. Although Tacoma Power has no investment in such facilities, these contracts require Tacoma Power to pay minimum amounts (which are based at least in part on the debt service requirements of the supplier) whether or not the facility is operating. The cost of power obtained under the contracts, including payments made when a facility is not operating, is included in operations expense in the Statements of Revenues, Expenses and Changes in Net Position.

Tacoma Power entered into an Energy Conservation Agreement (ECA) with BPA in 2009. Under this agreement, funds are collected in wholesale power rates to support regional energy efficiency programs. As utilities implement conservation programs and activities, BPA reimburses these funds per program specifications. For the years 2015 and 2014, Tacoma Power recovered \$763,356 and \$5,742,731 respectively through the ECA.

Information for the year ended December 31, 2015 pertaining to these contracts is summarized as follows:

Tacoma Power's Current Share Of	Grand Coulee Project Hydro Authority	Grant County PUD- Priest Rapids Project
Energy Output	258,679 mWh	25,360 mWh
Megawatt Capacity	-	5 mW
Operating Costs	\$ 2,188,084	\$659,731
Incentive Payments	\$ 3,880,558	-
R & R Repayment	\$ 326,559	-
Contract Expiration Date	5/9/2024	4/1/2052

On April 17, 2008, the FERC issued a new license to the Public Utility District No. 2 of Grant County (Grant PUD) for the continued operation of the Priest Rapids Hydroelectric Project which consists of the Priest Rapids Development and the Wanapum Development. The original license for the Priest Rapids Project was issued on November 4, 1955 and expired on October 31, 2005. Since then, the Project had operated under annual licenses. The renewed license issued by FERC allows Grant PUD a 44-year license for the continued operation of the Project. The term of Tacoma Power's contract with Grant PUD is for the term of the FERC license. Tacoma Power's purchase quantity and costs are tied to the actual costs of the Project.

Total expenses under the above contracts for the years 2015 and 2014 were \$6,395,201 and \$6,047,270, respectively, for Grand Coulee Project Hydro Authority, however, proceeds under the contract exceeded expenses in 2015 and 2014 for Grant County PUD - Priest Rapids resulting in a gain of \$659,731 and \$2,078,279, respectively.

In addition, Tacoma Power is required to pay its proportionate share of the variable operating expenses of these projects.

Other Power Transactions - Other power transactions include purchases under short-term agreements and interchanges of secondary power between utilities in response to seasonal resource and demand variations. Fluctuations in annual precipitation levels and other weather conditions materially affect the energy output from Tacoma Power's hydroelectric facilities. Accordingly, the net interchange of secondary power in and out may vary significantly from year to year. Tacoma Power's trading activities are limited to purchasing power to meet native loads, optimizing the value of Tacoma Power's power supply portfolio and selling energy during times of surplus.

Tacoma Power records applicable energy contracts using accrual accounting and recognizes the revenue or expense at the time of contract performance, settlement or termination. As of December 31, 2015 Tacoma Power had forward sales contracts totaling \$22.6 million dollars extending out to September 2017 with a fair market value of \$17.2 million. These contracts meet the normal purchase normal sales scope exception for derivative reporting under GASB 53.

Tacoma Power's net power purchases or sales and interchanged activities are reflected in the Statements of Revenues, Expenses and Changes in Net Position.

A breakdown of the net interchange in kilowatt-hours is as follows:

Interchange Summary	2015 (in kWh)	2014 (in kWh)
Secondary Sales	(1,917,685,000)	(2,842,694,000)
Portfolio Purchases	293,059,000	444,264,000
Miscellaneous Exchanges	(1,441,000)	(4,200,000)
Other	54,924,000	57,127,000
Net Interchange	(1,571,144,000)	(2,345,503,000)

NOTE 7 FLEET SERVICES FUND

The Department of Public Utilities has established a Fleet Services Fund to perform scheduled maintenance, repair and replacement of Department vehicles and related equipment.

Tacoma Power pays the Fleet Services Fund for its use of the vehicles and equipment to cover fleet operating expenses. Payments made by Tacoma Power in 2015 and 2014 were \$7,212,082 and \$7,475,002, 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. The solvency of the Replacement Fund allowed Fleet Services to return a portion of interest earned on fund investments for the year to their customers. In 2015 and 2014, Fleet Services returned 75% of the interest earned to Tacoma Power's replacement fund. The amount of the refund was \$107,916 and \$91,750 for 2015 and 2014, 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 Power and other divisions within the Department for certain losses arising from personal and property damage claims by third parties. The major risks to Tacoma Power 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 Power is required to make payments to the Self-Insurance Fund to cover claims incurred by Tacoma Power and administrative expenses of the Fund. Tacoma Power's premium payments totaled \$900,000 and \$810,000 in 2015 and 2014 respectively. Assets in the Self-Insurance Fund total \$6.9 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 Power's investment in the Self- Insurance Fund is more than adequate to settle all its known or estimated claims.

The City purchased a \$15 million Fiduciary Liability Policy with a \$100,000 deductible that provides for wrongful acts arising out of the administration of the City's employee benefit programs and a Crime policy with a \$1 million limit and \$75,000 deductible for employee dishonesty and for fraudulent or dishonest act by employees against the City for loss of money, securities and property.

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 property within buildings and \$10,000 per vehicle. There is a self-insured retention of \$1.5 million for general liability. The public official liability policy has a \$200,000 deductible. The Department's total liability limit is \$60 million any one occurrence and \$60 million annual aggregate.

The general government general liability and public official liability policies provide \$15 million of excess coverage with \$3 million retention. The City has a policy to cover extraordinary worker's compensation claims with a statutory limit and a self-insured retention of \$1 million per occurrence and an additional \$250,000 for each 12 month policy period.

NOTE 9 TACOMA EMPLOYEES' RETIREMENT SYSTEM FUND (TERS)

The Tacoma Employees' Retirement System (TERS), a pension trust fund of the City of Tacoma, issues a publicly available CAFR that includes financial statements and required supplementary information may be obtained by writing to:

Tacoma Employee's Retirement System
3628 South 35th Street
Tacoma, WA 98409

Or the TERS CAFR may be downloaded from the TERS website at www.cityoftacoma.org/retirement.

Administration of The System - The "Tacoma Employees' Retirement System" is a costsharing, multiple-employer, defined benefit retirement plan covering substantially all employees of the City of Tacoma, with the exception of police officers, firefighters, and Tacoma Rail employees who are covered by state and federal retirement plans. Employees of the Tacoma-Pierce County Health Department, as well as, certain employees of the Pierce Transit and Law Enforcement Support Agency who established membership in the System when these agencies were still City of Tacoma departments, are also members. The Board of Administration of the Tacoma Employees' Retirement System administers the plan and derives its authority in accordance with Chapter 41.28 RCW and Chapter 1.30 of the Tacoma City Code.

At the direction of the City Council, the System is administered by the Board of Administration (the Board) consisting of nine regular members and one alternate member. The members of the Board are: the Mayor, who serves as Chair; the Director of Finance; the City Manager (or designee); the Public Utilities Director (or designee); three elected employee representatives; one elected retired representative; and one City resident (not employed by the City) elected by the other eight members. The nine Board members appoint a TERS member, either active or retired, as an alternate Board member. The Board is required by the Tacoma Municipal Code to make annual reports to the City Council on the financial condition of the Retirement System. The Board, subject to City Council approval, appoints the Director who is responsible for managing the daily operations of the System.

The breakdown of membership as of December 31, 2014 is as follows:

Retirees and beneficiaries currently receiving benefits	2,167
Terminated vested and other terminated participants	627
Active members:	
City of Tacoma	2,622
South Sound 911	4
Pierce Transit	6
Tacoma-Pierce County Health Department	252
Total active members	2,884
Total membership	5,678

Membership - Substantially all employees of the City of Tacoma are members of the System, with the exception of police officers, firefighter, and Tacoma Rail employees, who are covered by state or federal retirement plans. Other members include employees of the Tacoma-Pierce County Health Department, and certain employees of the Pierce Transit and the South Sound 911 (formerly known as Law Enforcement Support Agency) who established membership in the System when these agencies were still City of Tacoma departments.

Benefits - There are two formulas to calculate the retirement benefits. The benefit paid will be issued on the formula which provides the higher benefit. The most commonly applied formula, “service retirement”, is a product of the member’s average monthly salary for the highest, consecutive 24-month period, the number of years of membership credit, and a percentage factor (2% maximum) that is based on the member’s age and years of service. The other formula is an annuity based on member contributions. There are several options available for the retiree to provide for their beneficiaries. The System also provides death, disability and deferred retirement. Additionally, the System provides cost of living adjustment (COLA) increases up to 2.125% as of July 1st of each year; the actual COLA granted is dependent on the Consumer Price Index (Seattle Area – all items) over the preceding calendar year.

Any active member who has not retired, and has five or more years of service as a member may purchase up to five additional years of service at the time of retirement. Total service including service purchased cannot exceed 30 years.

The System participates in the portability of public retirement benefits in Washington State public retirement. As provided under Chapter 4154 of the RCW, this allows a member to use all years of service with qualified Washington systems to determine retirement eligibility and percentage factor for benefits under the System.

Contributions - The participating employers are responsible for funding the System at a level sufficient to pay obligations and ensure the actuarial and financial soundness of the System. Contribution rates for the employer and the employee are recommended by the Board of Administration and final approval rests with the Tacoma City Council. Currently, the required contribution rate for employees is 9.20% of their regular gross pay; the employer contributes 10.80%, for a combined total of 20.00% which is sufficient to amortize the Unfunded Actuarial Accrued Liability (UAAL) of the System if future experience follows all actuarial assumptions. Changes to the contribution rate are subject to Sections 1.30.340 and 1.30.360 of the Tacoma Municipal Code.

Significant Assumptions - The following actuarial methods were used in the funding valuation.

Measurement Date	December 31, 2014
Valuation Date	January 1, 2015
Actuarial Cost Method	Entry Age Normal
	Funding is based on statutory contributions rate.
	This amount is compared to a 30-year amortization for the purposes of calculating the Actuarially Determined Contribution.
	The amortization method for the ADC is as follows:
Amortization Method	<ul style="list-style-type: none"> • Level percent • Open periods • 30 year amortization period at 01/01/2015 • 4% amortization growth rate
Asset Valuation Method	4 year smoothing period; Corridor - None
Inflation	3%
Salary Increases	4% general wage increase assumption
Investment Rate of Return	7.25%
Cost of Living Adjustment	2.13%
Retirement Age	Varies by age, gender, eligibility
Turnover	Varies by age, gender, eligibility
Mortality	RP-2000 mortality for healthy and disabled annuitants, with age adjustments

Benefit and Assumption Changes - The comparability of the data from year to year can be affected by changes in actuarial assumptions, benefit provisions, accounting policies, and other factors. Between January 1, 2014 and January 1, 2015 no assumptions were changed.

Target Allocations - The long-term expected rate of return is determined by adding expected inflation to expected long-term real returns and reflecting volatility and correlation.

The capital market assumptions are per Milliman's (the System's actuary) investment consulting practice as of June 30, 2014. The target asset allocation is based on TERS Investment Policy Statement dated February 2014.

Asset Class	Target Allocation	Long-term Expected Arithmetic Real Rate of Return
Investment grade fixed income	15.0%	2.03%
US inflation-indexed bonds	5.0	1.41
High yield bonds	9.0	4.49
Emerging market debt	5.0	5.05
Global equity	41.5	6.02
Public real estate	2.0	6.38
Private real estate	2.5	3.72
Private equity	10.0	9.02
Master limited partnerships	4.0	4.46
Timber	2.0	3.84
Infrastructure	2.0	5.88
Agriculture	2.0	4.38
Assumed inflation - mean		3.00
Assumed inflation - standard deviation		1.85
Portfolio arithmetic real mean return		5.11
Portfolio median nominal geometric return		7.21
Portfolio standard deviation		12.02
Long-term expected rate of return, net of investment expenses		7.25

Sensitivity Analysis - The following presents the net pension liability of the System, calculated using the discount rate of 7.25%, as well as what the System's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.25%) or 1 percentage point higher (8.25%) than the current rate

	1% Decrease 6.25%	Current Discount Rate 7.25%	1% Increase 8.25%
Net pension liability (asset)	\$ 65,783,976	\$ (3,823,476)	\$ (62,408,975)

As of December 31, 2015, the deferred inflows and outflows of resources are as follows:

	Deferred Inflows of Resources	Deferred Outflows of Resources
Difference between expected and actual experience	\$ (1,450,314)	\$ —
Changes in proportionate share	—	24,245
Net difference between projected and actual earnings	(2,586,075)	—
Contributions made subsequent to the measurement date	—	9,053,341
Total	\$ (4,036,389)	\$ 9,077,586

The net amount of deferred inflows and outflows, other than contributions made subsequent to the measurement date, will be recognized as pension expense in each of the next four years. Contributions made subsequent to the measurement date will offset net pension liability in the following year.

Amounts will be recognized in pension expense as follows:

Year-ended December 31,	
2016	(1,255,023)
2017	(1,255,023)
2018	(1,255,023)
2019	(247,075)

The proportionate share of the Power Division is 39.8%. The proportionate share was based on the actual contributions for the year.

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 active employees and retirees rather than based on the claims experience of retirees only. This difference is a benefit to the retirees, since health claims costs generally increase with age. GAAP 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. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and are subject to continual revision as results are compared to past expectation and new estimates are made about the future.

Funding Policy - The City uses pay as you go funding; contributions to a separate trust are not required.

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 (3.75%).

The Actuarial Accrued Liability (AAL) is the portion of the present value of benefits attributed to past service only. The portion attributed to future employee service is excluded. For inactive employees, the AAL is equal to the present value of benefits. For active employees, the actuarial present value of the projected benefits of each individual 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 attributed to service between entry age and the valuation date is the actuarial accrued liability.

The Normal Cost is that portion of the City provided benefit attributable to employee service in the current year.

The Annual Required Contribution (ARC) is the amount the City is required to report as an expense for the year. The ARC is equal to the Normal Cost plus an amount to amortize the UAAL on a closed basis of 30 years, beginning January 1, 2007. The amortization period for 2015 is 22 years.

The ARC represents an accounting expense, but the City is not required to contribute the ARC to a separate trust. If the City does not set aside funds equal to the ARC (less current year benefit payments) each year, then the ARC (less benefit payments) will accumulate as a noncurrent liability (Net OPEB Obligation) on the statements of net position. The City has a Net OPEB Obligation as of December 31, 2015 as the City has not set aside funds for OPEB.

Excise Tax For High Cost or “Cadillac” Health Plans in 2018 and Beyond– An excise tax for high cost health coverage or “Cadillac” health plans was included in the Affordable Care Act (ACA) passed into law in March 2010. The provision levies a 40% tax on the value of health plan costs that exceed certain thresholds for single coverage or family coverage. The 2018 annual thresholds are \$10,200 for single coverage and \$27,500 for a family plan. If, between 2010 and 2018, the cost of health care insurance rises more than 55%, the threshold for the excise tax will be adjusted.

The City believes that the current provisions of ACA should be reflected in the projection of benefits and therefore, the value of the excise tax is included in the valuation. It is assumed that there will be no changes to the current law and that there will be no changes in plan design to help mitigate the impact of the tax.

GASB Statement No. 45 indicates that the projection of benefits should include all benefits to be provided to retirees in accordance with the current “substantive” plan. The substantive plan refers to the plan terms as understood by the employer and plan members at the time of the valuation. For this reason, the City believes that the current provisions of PPACA should be reflected in the projection of benefits and therefore, the value of the excise tax is included in this valuation. It is assumed that there will be no changes to the current law and that there will be no changes in plan design to help mitigate the impact of the tax.

Summary of Changes – As of the January 1, 2015 valuation the total AAL was \$208,814,312, 20% lower than expected primarily due to clarification in spouse benefits, medical costs, demographic experience and a change to the assumption for future medical trends.

The following table is a summary of valuation results with a comparison to the results from the last valuation.

	January 1, 2013	January 1, 2013
Active employees	3,335	3,404
Terminated vested employees	394	442
Retired employees & dependents	846	744
Total	4,575	4,590
Annual Benefit Payments	\$ 9,887,335	\$ 8,963,089
Discount rate	3.75%	3.75%
Present Value of Benefits (PVB)	\$ 326,742,538	\$ 262,184,195
Actuarial Accrued Liability (AAL)	\$ 251,839,846	\$ 208,814,312
Assets	\$ –	\$ –
Unfunded Actuarial Accrued Liability (UAAL)	\$ 251,839,846	\$ 208,814,312
Normal Cost	\$ 5,484,587	\$ 3,832,131
Annual Required Contribution (ARC)	\$ 20,058,760	\$ 16,966,964

The following table shows the total value of the benefits provided, the member paid premiums and the City paid benefits as of January 1, 2015.

Value of Subsidy at 3.75% Interest Rate	Total Value of Benefits	Member Paid Premiums	City Paid Benefits
Present Value of Benefits (PVB)	\$ 420,832,932	\$ 158,648,737	\$ 262,184,195
Actuarial Accrued Liability (AAL)	\$ 291,228,295	\$ 82,413,983	\$ 208,814,312
Normal Cost	\$ 9,501,758	\$ 5,669,627	\$ 3,832,131
Annual Benefit Payments	\$ 12,325,369	\$ 3,362,280	\$ 8,963,089

The following table shows the calculation of the Annual Required Contribution and Net OPEB Obligation for the City and for Tacoma Power as of December 31, 2015.

	City	Division
Determination of Annual Required Contribution:		
Normal Cost at Year-end	\$ 3,832,131	\$ 858,656
Amortization of UALL	13,134,833	398,368
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 1,257,024
Determination of Net OPEB Obligation:		
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 1,257,024
Interest on prior year Net OPEB Obligation	2,480,183	344,936
Adjustments to ARC	(3,492,760)	(407,624)
Annual OPEB Cost	15,954,387	1,194,337
Actual benefits paid	8,963,089	324,146
Increase in Net OPEB Obligation	6,991,298	870,191
Net OPEB Obligation - beginning of year	66,138,204	9,198,300
Net OPEB Obligation - end of year	\$ 73,129,502	\$ 10,068,491

The Division has included the liability in the other long term liabilities on the Statement of Net Position.

Funded Status and Funding Progress - The following table shows the annual OPEB costs and net OPEB obligation for three years. This table is based upon a 3.75% interest rate.

Year Ended	Annual OPEB Cost		Benefits Paid		Net OPEB Obligation	
	City	Tacoma Power	City	Tacoma Power	City	Tacoma Power
12/31/2013	\$ 19,528,767	\$ 2,103,280	\$ 9,887,334	\$ 577,629	\$ 56,110,801	\$ 7,806,683
12/31/2014	\$ 19,319,944	\$ 2,084,511	\$ 9,292,539	\$ 692,894	\$ 66,138,206	\$ 9,198,300
12/31/2015	\$ 15,954,387	\$ 1,194,337	\$ 8,963,089	\$ 324,146	\$ 73,129,502	\$ 10,068,491

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 for non-LEOFF 1 groups. For LEOFF 1, the UAAL is amortized as a level dollar amount. The amortization period was 30 years in 2007 and is now 22 years.

Actuarial Methods and Significant Actuarial Assumptions

Valuation Date	January 1, 2015
Census Date	January 1, 2015
Actuarial Cost Method	Entry Age
Amortization Method	Combination of level percentage and level dollar amount, see note above.
Remaining Amortization Period	22 years, closed
Demographic Assumptions	Demographic assumptions regarding retirement, disability, and turnover are based upon pension valuations for the various pension plans.

Actuarial Assumptions:

Discount Rate	3.75% for pay-as-you-go funding
Medical Cost Trend	2015 6.9%
	2016 6.6%
	2017 5.9%
	2020 5.5%
	2030 5.9%
	2040 5.7%

The medical cost rate is assumed to continue grading downward until achieving the ultimate rate of 4.8% in 2071 and beyond. The first year trend reflects assumed increases based on ACA fees. These trend rates assume that, over time, deductibles and out-of-pocket maximums will be periodically increased as medical trends increase. The trends above do not reflect the increases in costs due to the excise tax.

Economic Assumptions -

Discount Rate (Liabilities) 3.75%

Demographic Assumptions

Eligibility:

Disability - Five years of service are required for non-service connected disability.

Retirement - 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
- Age 40 with 20 years of service

NOTE 11 COMMITMENTS AND CONTINGENCIES

Capital Improvements - The financial requirement for Tacoma Power's 2015/2016 biennial Capital Improvement Program is approximately \$182.7 million. At December 31, 2015, the remaining financial requirement was approximately \$102.6 million. The remaining financial requirement for Capital Improvement Programs relating to prior biennium is approximately \$10.7 million.

General Legal Matters - Tacoma Public Utilities has received several other miscellaneous claims that either do not allege significant amounts or that the Legal Department has determined do not pose a risk to liability to the utilities.

TACOMA **WATER**



2015

**HIGH CUSTOMER DEMANDS AND
RIVER FLOWS LOWER** THAN PREVIOUSLY
RECORDED IN THE GREEN RIVER

TACOMA | WATER

There's no doubt that 2015 was a milestone year for Tacoma Water, one marked by a declared drought that affected all operational areas. The year also proved that, whatever comes its way, the utility can flex and adapt to any circumstance while still completing its vital, daily work serving customers.

The year started with no snowpack and was followed by an early end to spring rains. Historic high temperatures in May, June and July resulted in high customer demands and river flows lower than previously recorded in the Green River, Tacoma's primary water supply. The utility is fortunate to have abundant groundwater supplies, and those resources were used extensively from early spring through late fall. Fortunately, Tacoma Water had recently installed new water treatment systems at the groundwater sources. Improvements to a spring source were made by mid-summer, bringing another 10 million gallons per day of much-needed supply into the system. Tacoma Water also found ways to access new supply sources such as pumping water from a lake in the upper watershed into the Green River system and buying water from an adjacent utility to meet short-term high demands. Those solutions will set the stage for improved resilience in future drought conditions.

Customers, too, proved their adaptability and support for the utility in 2015. When Tacoma Water asked them to voluntarily reduce their water use by 10% to stretch water supplies until fall rains returned, they did.

This was also the year that the utility's biggest capital project ever, the \$185 million Green River Filtration Facility, began operations. It was challenging to switch from an unfiltered to fully filtered system without interrupting water service to customers. The process required intensive training and staff commitment, but staff members were able to make the needed changes without so much as a hiccup in water delivery. When the drought hit, modifications were required to operate the filtration plant at a lower flow rate than was anticipated in design, but Tacoma Water staff accomplished the change successfully. Now, with filtration, the water the utility provides to customers is of a much higher quality, with 100 times less sediment. Without the sediment, much less chlorine is required to treat the water.

THE UTILITY CAN **FLEX
AND ADAPT TO ANY
CIRCUMSTANCE WHILE
STILL COMPLETING ITS
VITAL, DAILY WORK
SERVING CUSTOMERS.**

The financial picture

Planning for the long-term financial health of Tacoma Water, the utility sold \$23 million in bonds to refund 2005 bonds at lower interest rates. The total interest cost of 1.9% for the bond refunding will deliver a net present value savings of \$2.7 million over the remaining life of the bonds, which have a final maturity in 2025.

Thinking further about the future, Tacoma Water published its demand forecast, which provides the utility with a documented, repeatable and transparent process for conducting forecasting on 10- and 60-year horizons, and will enhance the ability to account for uncertainty in financial, system and supply planning.

Tacoma Water developed a business case analytical tool tailored to its needs, along with updated long- and short-form reporting templates. Workshops provided to capital planning staff offered training on the new tools as well as practice using concepts around risk, reference groups and planning assumptions. Discussions from the workshops were used to enhance the business case tools and create user manuals and documentation.

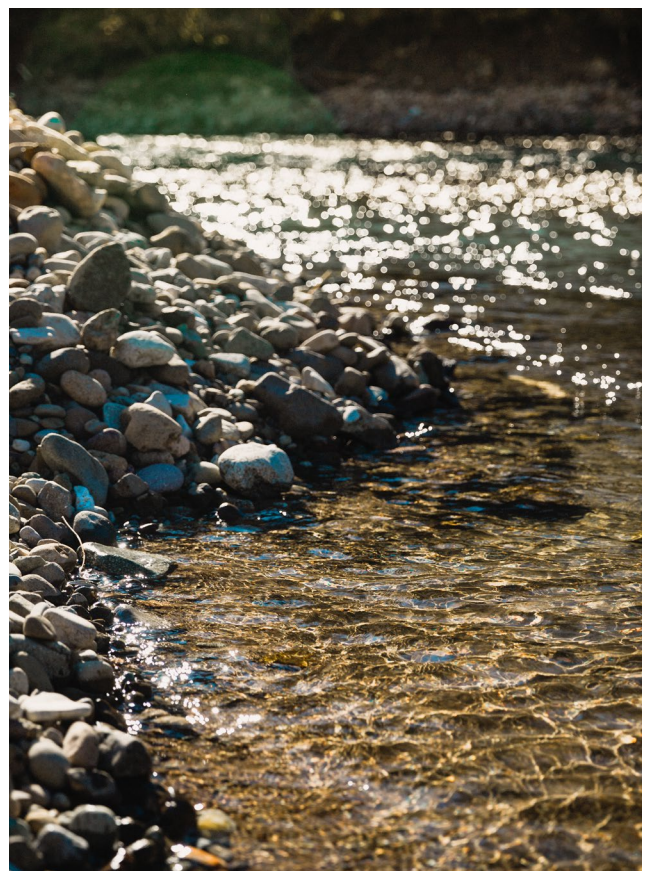
The Tacoma Public Utility Board and City Council approved a 4% overall rate increase that took effect in April.

MANY OF THE TEMPORARY
WATER SUPPLY SOLUTIONS
DEPLOYED IN 2015 WILL BE
**A GREAT VALUE IN FUTURE
DROUGHTS.**

Managing the work with strategy

2015 was year three of using a Balanced Scorecard approach to manage Tacoma Water's strategic work. That discipline was put to the test in 2015 with the drought. The utility used its strategy management tools to review priorities and capacity for both strategic initiatives and vital work. As a result, resources and timelines were shifted, ensuring an effective response to an unprecedented water supply situation while still making progress on strategic initiatives.

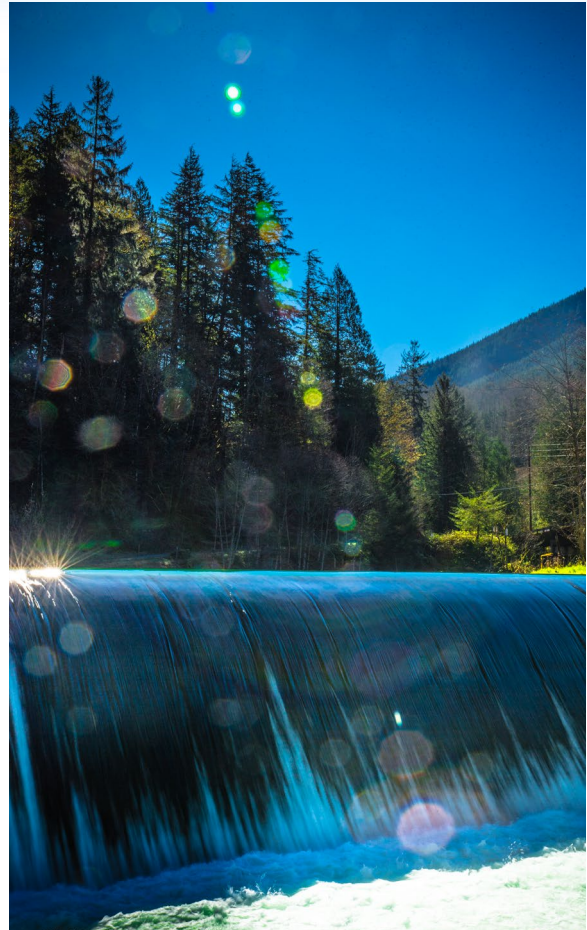
The vulnerability assessment that Tacoma Water began in 2014 remained a priority over the course of the year. The assessment uses a new standard of analyzing impacts of service delivery to hazards of a grand scale, such as earthquakes. The assessment was completed in 2015, and implementation of its recommendations will begin in 2016.



In 2015, Tacoma Water negotiated a new 15-year franchise with Pierce County to allow operation of the water system in unincorporated areas. The agreement replaces a 50-year franchise and covers infrastructure within county rights of way, such as a transmission main carrying water to Tacoma, and distribution systems serving customers in unincorporated Pierce County. With the new franchise, Tacoma Water remains a utility in good standing, which affords access to reduced permitting requirements and fees. The franchise terms are favorable and result in ongoing positive coordination with the county, which benefits all of Tacoma Water's customers. The utility also negotiated successful four-year contracts with the largest unions representing Tacoma Water staff and a five-year extension of the water supply contract for the utility's largest customer, WestRock.

After nearly two years of planning, the 115th U.S. Open Championship was played in June at Chambers Bay in University Place. Tacoma Water ensured temporary water service connections were reliably and safely providing water for the approximately 235,000 spectators who attended the event. The event is estimated to have made a \$140 million economic impact to the region, and the utility is pleased to have been a part of it.

Customer service has long been a high priority for Tacoma Water, and 2015 was no different. The utility has a goal that at least 98.5% of all customers who call in with a water quality concern receive a call back the same business day. That goal was exceeded, with 100% of the calls returned in that timeframe. That action speaks to strong employee dedication and a sincere desire for the well-being of customers.



DAM AT TACOMA WATER HEADWORKS ON THE GREEN RIVER

To close the chapter on 2015's drought story, it should be noted that long-range forecasts did not turn out as had been predicted, and fall rains did return as usual in October.

That resolved the water supply issue, and the year ended with normal snowpack and full groundwater recharge. Tacoma Water's comprehensive approach to meeting customer demands and river flow commitments during the drought was very effective and minimized customer impacts. Many of the temporary water supply solutions deployed in 2015 will be a great value in future droughts, providing the utility with a roadmap to increased resiliency.

FINANCIAL HIGHLIGHTS

In millions, for the years ended
December 31,

2015

2014

2013

2012

2011

Tacoma Water

Total Income	\$92.2	\$86.1	\$77.7	\$77.5	\$72.2
Operating Expenses	48.4	43.7	41.7	37.8	38.0
Income Available for Debt Service	\$43.8	\$42.4	\$36.0	\$39.7	\$34.2
Debt Service	\$18.8	\$19.9	\$21.0	\$25.1	\$25.1
Debt Service Coverage	2.33x	2.14x	1.72x	1.58x	1.36x
Plant Additions	\$223.4	\$95.2	\$138.0	\$106.7	\$87.0
Number of Customers	99,943	98,608	97,856	96,333	96,734
Average Rates (per 100 cubic feet)					
Residential	\$4.254	\$4.185	\$3.937	\$3.717	\$3.556
Commercial/Industrial	\$3.818	\$3.634	\$3.373	\$3.179	\$3.025

Water Sales (dollars in millions)

2015

2014

Residential	48.20	44.58
Commercial	14.76	12.81
Special	5.95	5.80
Other	7.73	6.39
Unbilled Revenue	0.32	0.12

Water Consumption (gallons in billions)

2015

2014

Residential	8.49	7.96
Commercial	3.21	2.63
Special	5.79	6.03
Other	1.95	2.19

Operating Expenses

2015

Depreciation	\$ 17,102,664	29%
Distribution	11,880,985	20%
Production	12,992,883	17%
Administration	8,930,064	15%
Other Operating Expenses	4,327,441	7%
Taxes	4,681,114	6%
Power & Transmission	3,672,860	6%

REPORT OF INDEPENDENT AUDITORS

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

Report on the Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Washington Department of Public Utilities, Water Division (the Division), which comprise the statements of net position as of December 31, 2015 and 2014, and the related statements of revenue, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Division as of December 31, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

Change in Accounting Principle

As discussed in Note 2 to the financial statements, effective January 1, 2015, the Division adopted requirements of Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*, and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68*. The beginning net position has been adjusted for this change. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis on pages 5 through 12, schedule of proportionate share of net pension liability on page 46, and schedule of the city of Tacoma's contributions employer contributions on page 46 be presented to supplement the basic financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The statistical data presented on pages 48 through 67 and the superintendent's report presented on pages 68 through 80 are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on it.

Miss Adams LLP

Tacoma, Washington
April 1, 2016

MANAGEMENT'S DISCUSSION & ANALYSIS

The following discussion and analysis of Tacoma Water's financial performance provides an overview of the financial activities for the years ended December 31, 2015 and 2014. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues, provide an overview of the financial activities, and identify changes in the 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 (GAAP) in the United States of America, 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, 2015 and 2014, include Statements of Net Position, Statements of Revenues, Expenses and Changes in Net Position, and Statements of Cash Flows. The Statements of Net Position present information on all of Tacoma Water's assets, deferred outflows of resources, liabilities, and deferred inflows of resources with the difference being reported as net position. The Statements of Revenues, Expenses and Changes in Net Position 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, non-capital financing, capital and related financing, and investing activities.

The Notes to 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 Tacoma Water's presentation of financial position, results of operations and changes in cash flows.

With implementation of Governmental Accounting Standards Board (GASB) Statement No. 68, the Division's 2015 beginning net position has been adjusted to conform to the new reporting and accounting requirements (See Note 2 to the Financials Statements). The year of 2014 has not been restated due to the unavailability of the historic information from the plan.

Financial Highlights

- The net position of Tacoma Water was \$542.5 million in 2015, \$516.7 million in 2014 and \$480.3 million in 2013. Of these amounts, \$53.8 million in 2015, \$46.7 million in 2014, and \$37.9 million in 2013 were available to meet Tacoma Water's ongoing obligations to citizens and creditors.
- Tacoma Water's total net positions increased by \$24.7 (32.0%) million in 2015, \$36.4 (7.6%) million in 2014 and \$30.4 (6.8%) million in 2013.
- Operating revenues were \$98.1 million in 2015, a decrease of \$0.2 million (0.2%) compared to 2014. While sales revenue increased by \$7.3 million, contract resource obligation revenue decreased by (\$7.5) million because the Green River Filtration Facility is complete and the partners were billed less. Operating revenues were \$98.3 million in 2014, an increase of \$2.2 million (2.3%) compared to \$96.1 million in 2013. This increase is due to an average rate increase of 6.0% that went into effect January 1, 2014.
- In 2015, Tacoma Water's net utility plant of \$884.7 million represented an increase of \$12.6 million (1.4%) over the 2014 \$872.1 million balance. In 2014, net utility plant was \$59.0 million (7.3%) more than 2013's \$813.1 million balance. Major projects contributing to the increases include the Green River Water Filtration Facility and Main Replacements.

Overview of the Financial Statements

Tacoma Water reported net operating income of \$34.6, \$39.8 and \$40.2 million in 2015, 2014 and 2013 respectively. In 2015, operating revenues increased by \$0.2 million and operating expenses increased \$5.0 million. For 2014, operating revenues increased \$2.2 million and operating expenses increased \$2.7 million compared to 2013.

The following tables highlight Tacoma Water's past three years' operating results and gallons billed.

Operating Results (in thousands)

Category	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Operating Revenues	\$ 98,139	\$ 98,320	\$ 96,119	\$ (181)	\$ 2,201
Operating Expenses	63,588	58,557	55,897	5,031	2,660
Net Operating Income	34,551	39,763	40,222	(5,212)	(459)
Net Non-Operating Income (Expense)	(15,595)	(9,657)	(14,580)	(5,938)	4,923
Capital Contributions	9,053	8,671	7,139	382	1,532
Federal BAB Subsidies and Grants	3,610	3,959	3,572	(349)	387
Transfers Out	(6,874)	(6,352)	(5,922)	(522)	(430)
Change in Net Position	\$ 24,745	\$ 36,384	\$ 30,431	\$ (11,639)	\$ 5,953

Gallons Billed (in millions)

Type of Customer	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Residential	8,486.7	7,968.7	7,761.2	518.0	207.5
Commercial & Industrial	8,994.1	9,118.6	8,787.8	(124.5)	330.8
Municipal & Wholesale	1,959.0	1,256.2	1,278.8	702.8	(22.6)
Total	19,439.8	18,343.5	17,827.8	1,096.3	515.7

Net Position

Net position may serve over time as a useful indicator of an entity's financial position. The analysis highlights net position for the last three years.

Statements of Net Position (in thousands)

Description	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Net Utility & Non-Utility Plant	\$ 885,214	\$ 872,576	\$ 813,543	\$ 12,638	\$ 59,033
Current & Other Assets	212,475	208,947	225,068	3,528	(16,121)
Total Assets	\$ 1,097,689	\$ 1,081,523	\$ 1,038,611	\$ 16,166	\$ 42,912
Deferred Outflows	4,003	1,588	1,814	2,415	(226)
Total Assets & Deferred Outflows	\$ 1,101,692	\$ 1,083,111	\$ 1,040,425	\$ 18,581	\$ 42,686
Net Position:					
Net Investment in Capital Assets	\$ 485,977	\$ 468,209	\$ 409,638	\$ 17,768	\$ 58,571
Restricted	2,733	1,797	32,703	936	(30,906)
Unrestricted	53,792	46,667	37,948	7,125	8,719
Total Net Position	542,502	516,673	480,289	25,829	36,384
Long-Term Debt	478,401	483,542	455,877	(5,141)	27,665
Current and Other LT Liabilities	44,283	47,321	68,684	(3,038)	(21,363)
Total Liabilities	522,684	530,863	524,561	(8,179)	6,302
Deferred Inflows	36,506	35,575	35,575	931	-
Total Net Position, Liabilities & Deferred Inflows	\$ 1,101,692	\$ 1,083,111	\$ 1,040,425	\$ 18,581	\$ 42,686

Revenues

Tacoma Water's operating revenues were \$98.1 million in 2015, a decrease of (\$0.2) million (0.2%) compared to 2014. Sales of water increased in 2015 by \$7.3 million of which \$1.2 million is due to an average rate increase of 4.0% effective April 1, 2015 and \$6.0 million is due to an increase in usage. This is offset by a decrease in contract resource obligations of \$7.5 million. The construction of the Green River Filtration Facility is complete and the partners were billed less.

Operating revenues were \$98.3 million in 2014, an increase of \$2.2 million (2.3%) compared to 2013. This is primarily due to an increase in sales of water of \$5.6 million of which \$4.2 million is due an average rate increase of 6.0% effective January 1, 2014 and \$1.4 million is due to an increase in usage. However, this is offset by a decrease in contract resource obligations of \$3.6 million. As the construction of the Green River Filtration Facility approaches completion the partners were billed less accordingly.

The following table highlights water sales by type of customer for 2015, 2014 and 2013.

Water Sales (in thousands)

Type of Customer	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Residential & Domestic	\$ 48,258	\$ 44,585	\$ 40,928	\$ 3,673	\$ 3,657
Commercial & Industrial	16,751	15,022	13,508	1,729	1,514
Special Rate	5,951	5,802	5,242	149	560
Municipal	488	455	446	33	9
Wholesale	5,192	3,718	3,520	1,474	198
Unbilled Revenue	319	121	468	198	(347)
Total	\$ 76,959	\$ 69,703	\$ 64,112	\$ 7,256	\$ 5,591

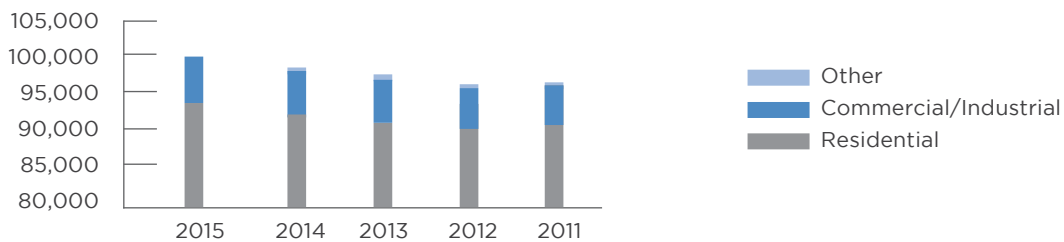
Approximately 62.7%, 64.0% and 63.8% of water sales were to residential and domestic customers in 2015, 2014 and 2013 respectively. Commercial and industrial sales were 21.8%, 21.6% and 21.1% of total sales for each year. Special rate sales were 7.7%, 8.3%, 8.2% of sales respectively.

Customers

Over the last five years, the overall number of customers has remained relatively stable. In 2015, 93.6% of all customers were residential compared to 93.5% in 2014 and 93.6% in 2013. Commercial and industrial customers were 6.2% of all customers in 2015 and 2014 and 5.8% in 2013. The remaining customer classes were 0.2% of all customers in 2015, 0.3% in 2014 and 0.6% in 2013.

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

Number of Customers

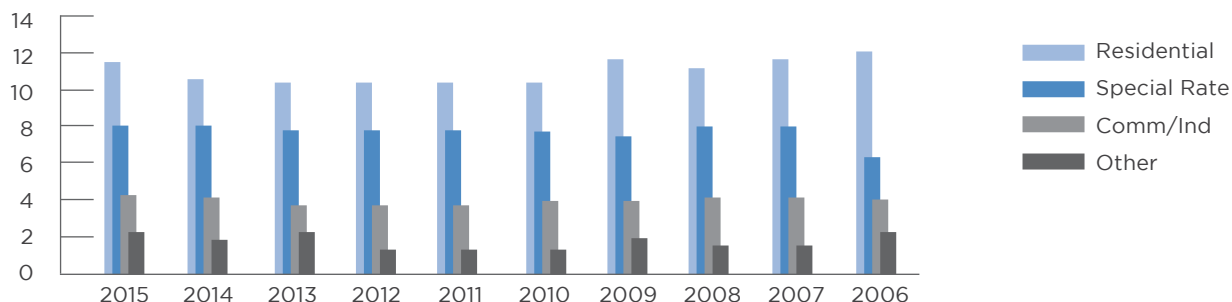


Water Users

Tacoma Water generates the majority of its revenues from its residential and domestic customer base. Consumption is measured in 100 cubic feet (CCF). In the years 2015, 2014 and 2013 residential customers used 11.3 million CCF (43.5%), 10.7 million CCF (43.4%) and 10.4 million CCF (43.5%) of total sales respectively. Special Rate customers used approximately 7.7 million CCF (29.7%), 8.1 million CCF (33.0%) and 7.8 million CCF (32.7%) respectively. Commercial and industrial customers used 4.4 million CCF (16.8%), 4.1 million CCF (16.8%) and 3.4 million CCF (14.2%) respectively. The remaining 2.6 million CCF (10.0%), 1.7 million CCF (6.8%) and 2.3 million CCF (9.6%) respectively was consumed by other customers.

Below is a graphical representation of the annual water usage by customer type for the last 10 years.

Annual Water Usage (In millions of CCF)



Expenses

In 2015, operating expenses increased \$5.0 million (8.6%), compared to an increase of \$2.7 million (4.8%) in 2014. Not only did the Green River Filtration Facility come online in 2015 but a statewide drought was declared as well. Source of Supply experienced the largest increase, \$1.7 million (26.6%). Two major projects during the drought were the purchase of water from Lakehaven, \$0.6 million, and the pumping of Eagle Lake, \$0.3 million. Source of Supply also experienced an increase in labor, approximately \$0.7 million, as labor was shifted from Transmission to Source.

Treatment saw an increase this year of \$1.1 million (28.3%) compared to 2014. Most of this increased cost of treatment can be attributed to the Green River Filtration Facility coming online. This shift in focus from capital to maintenance caused labor to increase by \$0.9 million. The drought also played a part by causing the need to purchase additional chemicals, \$0.2 million, to treat well water.

Power Pumping experienced an increase of \$0.3 million largely due to increased electricity expense due to the drought.

Administrative and General expense increased \$0.7 million (8.1%). In 2015, the department filled previously vacant positions causing a \$0.5 million increase in labor expense. Insurance expense also increased by \$0.2 million because Tacoma Water is now insuring the Plant and other facilities in the Headworks.

Due to the shift in focus from capital to maintenance, Distribution saw an increase of \$0.3 million. However, Transmission experienced a decrease of (\$0.2) million because labor was shifted from Transmission to Source of Supply.

Depreciation expense increased by \$0.3 million (1.9%) in 2015 due to an increase in depreciable assets of \$17.8 million during 2014.

In 2014, operating expenses increased \$2.7 million (4.8%), compared to an increase of \$4.5 million in 2013. Source of Supply increased \$0.9 million compared to 2013 primarily due to less labor charged out to the Regional Water Supply System and capital projects. Water Treatment increased by \$0.2 million due to additional employees assigned to the Headworks that previously worked for Supply.

Depreciation expense increased by \$0.7 million (4.4%) in 2014 due to an increase in depreciable assets of \$28.3 million during 2013.

Administrative and General expense increased \$0.6 million (5.3%). Of this, \$0.2 million was related to Customer Accounting and Consumer Services expense. These increases are largely due to higher assessments for services provided by internal departments.

The following table highlights Tacoma Water's operating expenses for 2015 – 2013.

Operating Expenses (in thousands)

Category	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Production Expense					
Source of Supply	\$ 8,015	\$ 6,333	\$ 5,483	\$ 1,682	\$ 850
Water Treatment	4,978	3,879	3,674	1,099	205
Total Production Expense	12,993	10,212	9,157	2,781	1,055
Power Pumping Expense	847	568	426	279	142
Transmission & Storage Expense	2,826	2,979	2,793	(153)	186
Distribution Expense	11,881	11,540	11,476	341	64
Customer Accounting & Service	4,327	4,435	3,930	(108)	505
Taxes	4,681	3,779	3,919	902	(140)
Depreciation	17,103	16,784	16,072	319	712
Administrative & General	8,930	8,259	8,124	671	135
Total Operating Expenses	\$ 63,588	\$ 58,556	\$ 55,897	\$ 5,032	\$ 2,659

Capital Assets

Tacoma Water invests in a broad range of utility assets and at the end of 2015 had \$884.7 million in net utility plant, an increase of \$12.6 million from 2014. Plant in Service increased \$192.3 million primarily due to the completion and capitalization of the Green River Filtration Facility. The capitalization of the new facility also attributed to the decrease of \$165.7 million in construction work in progress. In 2014, Tacoma Water had \$872.1 million in net utility plant, an increase of \$59.0 million compared to 2013 which was primarily the filtration plant still considered as construction work in progress. In 2015, 11.7 miles of water main were added or replaced compared to 11.5 miles in 2014, and 12.8 miles in 2013. Construction was completed on 17 private contracts in 2015, resulting in 5.87 miles; 18 private contracts in 2014, added 7.55 miles; and 14 private contracts in 2013, added 4.86 miles.

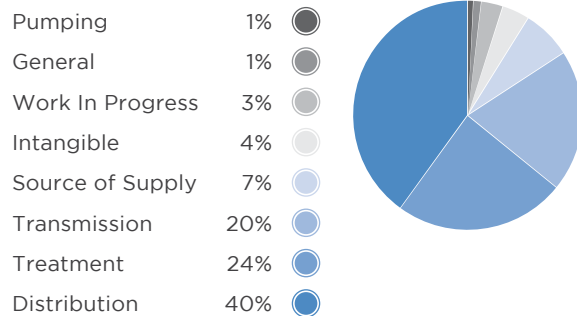
The following table summarizes Tacoma Water's capital assets, net of accumulated depreciation, for 2015 – 2013.

Capital Assets, Net of Accumulated Depreciation (in thousands)

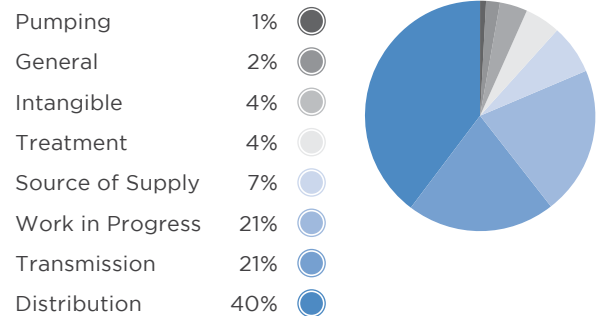
Net Utility Plant	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Intangible Plant	\$ 36,368	\$ 36,006	\$ 35,484	\$ 362	\$ 522
Source of Supply Plant	60,534	62,218	59,653	(1,684)	2,565
Pumping Plant	5,542	5,748	5,862	(206)	(114)
Water Treatment Plant	213,512	36,260	37,963	177,252	(1,703)
Transmission Plant	180,209	183,974	186,959	(3,765)	(2,985)
Distribution Plant	355,557	348,655	340,470	6,902	8,185
General Plant	12,368	12,868	13,987	(500)	(1,119)
Construction Work In Progress	20,631	186,354	132,673	(165,723)	53,681
Total	\$ 884,721	\$ 872,083	\$ 813,051	\$ 12,638	\$ 59,032

The following graphs provide a visual presentation of the allocation of Tacoma Water's capital investments in 2015 and 2014.

2015 Net Utility Plant



2014 Net Utility Plant



Additional information on capital assets can be found in Note 3 of the financial statements.

Debt Administration

At December 31, 2015 Tacoma Water had outstanding revenue bond obligations of \$399.9 million (net of unamortized bond premiums), a decrease of \$7.4 million compared to 2014. Tacoma Water issued \$23.0 million of Water System Refunding Bonds in May 2015. As of year-end 2014, the Utility had outstanding revenue bond obligations of \$407.3 million (net of unamortized bond premiums); a decrease of \$8.3 million compared to 2013.

All outstanding bonds are rated Aa2 by Moody's Investors Service and AA by Standard & Poor's.

Tacoma Water is required by bond covenants to maintain a debt service coverage ratio of 1.25 for principle and interest. Debt service coverage ratios (excluding RWSS) were 2.33, 2.14, and 1.72 in 2015, 2014 and 2013 respectively.

At the end of 2015, Tacoma Water had an outstanding State loan balance of \$89.0 million compared to \$86.7 million in 2014 and \$51.0 million in 2013. During 2015, Tacoma Water received \$6.4 million in Drinking Water State Revolving Fund (DWSRF) Loans. In 2015, Tacoma Water received \$6.3 million against the 2013 Fall DWSRF Loan and the \$0.1 million fee was recognized for the 2015 DWSRF Loan. These loans were specifically for the Green River Filtration Facility.

Additional information on Tacoma Water's long-term debt can be found in Note 5 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 accompanying financial statements and for their integrity. We prepared the financial statements according to GAAP in the United States of America, and they fairly portray Tacoma Water's financial position and operating results. The Notes to Financial Statements are an integral part of the basic financial statements and provide additional financial information.

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/CEO



Andrew Cherullo
Finance Director

2015 FINANCIAL REPORTS

Statements of Net Position

	December 31,	
Assets and Deferred Outflows	2015	2014
Utility Plant		
In Service, at Original Cost	\$ 1,058,533,815	\$ 866,279,607
Less - Accumulated Depreciation	(194,443,324)	(180,549,889)
Total	864,090,491	685,729,718
Construction Work in Progress	20,630,616	186,353,639
Net Utility Plant	884,721,107	872,083,357
Non-Utility Property	492,963	492,963
Special Funds		
Construction Funds	33,587,187	39,509,127
Debt Service Funds	3,633,933	3,597,672
Bond Reserve Funds	22,037,730	22,110,124
System Development Charge Fund	55,889,603	53,255,060
Other Cash & Equity in Pooled Investments	28,161,316	27,968,224
Total Special Funds	143,309,769	146,440,207
Current Assets		
Operating Funds Cash and Equity in Pooled Investments	49,778,192	45,768,035
Accounts Receivable (Net of Allowance for Doubtful Accounts of \$287,805 in 2015 and \$258,344 in 2014)	5,321,184	4,632,733
BABs Interest Subsidies Receivable	298,300	320,064
Accrued Unbilled Revenues	4,935,000	4,616,056
Materials and Supplies	2,487,075	2,401,523
Interfund Receivable	686,030	292,294
Prepayments	970,331	706,564
Total Current Assets	64,476,112	58,737,269
Other Assets		
Regulatory Asset-Public Fire Protection Fees	2,124,573	2,940,674
Regulatory Asset-Surcharges	1,683,348	828,534
Net Pension Asset	881,279	—
Total Other Assets	4,689,200	3,769,208
Total Assets	\$ 1,097,689,151	\$ 1,081,523,004
Deferred Outflows of Resources		
Unamortized Losses on Refunding Bonds	1,910,392	1,587,851
Deferred Outflows for Pensions	2,092,307	—
Total Deferred Outflows of Resources	4,002,699	1,587,851
Total Assets and Deferred Outflows	\$ 1,101,691,850	\$ 1,083,110,855

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

Net Position, Liabilities and Deferred Inflows	December 31,	
	2015	2014
Net Position		
Net Investment in Capital Assets	\$ 446,537,863	\$ 434,283,342
Restricted for:		
Water Capital and System Development Charge	39,439,003	33,925,829
Debt Service Funds	1,852,099	1,797,057
Net Pension Asset	881,279	—
Unrestricted	53,791,579	46,667,017
Total Net Position	542,501,823	516,673,245
Long-Term Debt		
Revenue Bonds	393,841,093	400,991,813
Public Works Trust Fund Loans	25,404,777	28,101,548
Drinking Water State Revolving Fund Loan	59,154,872	54,448,644
Total Long-Term Debt	478,400,742	483,542,005
Current Liabilities		
Current Maturities of Long-Term Debt	10,490,543	10,442,544
Current Maturities of Long-Term Liabilities	190,536	195,299
Accrued Taxes	1,863,652	1,405,334
Accrued Expenses and Contracts Payable	1,418,870	4,015,959
Salaries, Wages and Fringe Benefits Payable	584,328	1,293,035
Interest Payable	1,781,834	1,800,615
Customers' Deposits	348,793	275,591
Interfund Payables	1,582,992	1,339,199
Total Current Liabilities	18,261,548	20,767,576
Long-Term Liabilities		
Muckleshoot Agreements	7,129,695	7,320,231
Customer Advances for Construction	4,502,578	4,338,242
Unearned Revenue	7,905,152	8,573,685
Long-Term Accrued Compensated Absences	2,340,426	2,300,497
Other Long-Term Liabilities	4,144,086	4,019,927
Total Long-Term Liabilities	26,021,937	26,552,582
Total Liabilities	522,684,227	530,862,163
Deferred Inflows of Resources		
Rate Stabilization	35,575,447	35,575,447
Deferred Inflows for Pensions	930,353	—
Total Deferred Inflows of Resources	36,505,800	35,575,447
Total Net Position, Liabilities, and Deferred Inflows	\$ 1,101,691,850	\$ 1,083,110,855

**Statements of Revenues, Expenses and
Changes in Net Position**

Year Ended December 31,

2015

2014

Operating Revenues

Sale of Water	\$ 76,959,187	\$ 69,702,657
Other Operating Revenues	9,487,934	9,454,498
Contract Resource Obligation Revenues	11,691,703	19,162,799
Total Operating Revenues	98,138,824	98,319,954

Operating Expenses

Operations	15,553,845	15,087,555
Production	12,992,883	10,212,403
Administrative and General	13,257,505	12,693,605
Depreciation	17,102,664	16,783,698
Taxes	4,681,114	3,779,373
Total Operating Expenses	63,588,011	58,556,634

Net Operating Income	34,550,813	39,763,320
----------------------	------------	------------

Non-Operating Revenues (Expenses)

Interest Income	1,112,850	1,718,226
Other	(30,042)	537,052
Interest on Long-Term Debt	(20,022,582)	(20,363,130)
Amortization of Premium and Loss on Refunding	1,678,959	1,115,369
Interest Charged to Construction	1,665,978	7,335,911
Total Non-Operating Expenses	(15,594,837)	(9,656,572)

Net Income Before Capital Contributions and Transfers	18,955,976	30,106,748
---	------------	------------

Capital Contributions

Cash	6,442,694	5,002,301
Donated Fixed Assets	2,609,980	3,668,338
Federal BAB Subsidies	3,548,228	3,562,311
Grants	61,478	397,135
Transfers		
City of Tacoma Gross Earnings Tax	(6,778,140)	(6,274,494)
Transfers to/from Other Funds	(95,327)	(78,067)

Change in Net Position

24,744,889	36,384,272
------------	------------

Net Position - Beginning Of Year

516,673,245	480,288,973
-------------	-------------

**Accumulated Adjustment for Change in
Accounting Principle**

1,083,689

Total Net Position - Beginning of Year, As Adjusted

517,756,934

Total Net Position - End of Year

\$ 542,501,823	\$ 516,673,245
----------------	----------------

The accompanying notes are an integral part of these financial statements

Statements of Cash Flows

Year Ended December 31,

2015

2014

Cash Flows From Operating Activities

Cash from Customers	\$ 97,165,918	\$ 101,860,957
Cash Paid to Suppliers	(20,972,089)	(28,543,337)
Cash Paid to Employees	(25,556,817)	(22,288,493)
Taxes Paid	(4,222,796)	(4,003,959)
Net Cash From Operating Activities	46,414,216	47,025,168

Cash Flows From Non-Capital Financing Activities

Transfer to Other Funds	(95,327)	(78,067)
Transfer Out for Gross Earnings Tax	(6,778,140)	(6,274,494)
Net Cash From Non-Capital Financing Activities	(6,873,467)	(6,352,561)

Cash Flows From Capital and Related Financing Activities

Capital Expenditures, net	(25,464,456)	(64,812,288)
Proceeds from State Drinking Water Loan	6,420,000	39,570,473
Proceeds from Sale of Bonds	23,010,000	-
Debt Issuance Costs	(986,513)	(299,999)
Premium on Sale of Bonds	2,921,513	-
Principal Payments on Long-Term Debt	(10,442,545)	(10,814,544)
Principal Payments on Muckleshoot LT Liability	(195,300)	(200,182)
Payments on Refunding of Bonds	(25,065,000)	-
Interest Paid	(20,041,363)	(20,355,144)
BABs Federal Interest Subsidies	3,569,992	3,562,311
Grants Received	61,478	397,135
Contributions in Aid of Construction	6,442,694	5,002,301
System Development Charges, and Other LT Liabilities	(380,032)	488,922
Net Cash From Capital and Related Financing Activities	(40,149,532)	(47,461,015)

Cash Flows From Investing Activities

Interest Received on Investments	1,112,850	1,718,226
Other Net Non-Op Revenues and Expenses	375,652	837,053
Net Cash From Investing Activities	1,488,502	2,555,279

Net Change in Cash and Equity in Pooled Investments	879,719	(4,233,129)
Cash & Equity in Pooled Investments at January 1	192,208,242	196,441,371
Cash & Equity in Pooled Investments at December 31	\$ 193,087,961	\$ 192,208,242

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

**Reconciliation of Net Operating Income to Net Cash
From Operating Activities**

	Year Ended December 31,	
	2015	2014
Net Operating Income	\$ 34,550,813	\$ 39,763,320
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	17,102,664	16,783,698
Pension (Credits) Expense	(959,544)	—
Cash from changes in operating assets and liabilities:		
Accounts Receivable and Unbilled Revenue	(1,007,395)	2,669,667
Interfund Receivables	(393,736)	8,523,668
Regulatory Asset-Public Fire Protection Fees	816,101	815,351
Regulatory Asset-Hyada Surcharges	(854,814)	95,040
Materials and Supplies	(85,552)	(64,875)
Prepayments	(263,767)	(151,374)
Unearned Rental Revenues	—	(32,802)
Accrued Taxes	458,318	(224,586)
Salaries, Wages and Fringe Benefits Payable	(713,143)	74,315
Accrued Compensated Absences	44,365	60,588
Customers' Deposits	73,202	(6,253)
Accrued Expenses and Contracts Payable	(2,597,089)	(12,862,458)
Interfund Payables	243,793	(8,418,131)
Total Adjustments	\$ 11,863,403	\$ 7,261,848
Net Cash From Operating Activities	\$ 46,414,216	\$ 47,025,168

**Reconciliation of Cash and Equity in Pooled Investments to
Balance Sheet:**

Cash and Equity in Pooled Investments in Special Funds	\$ 143,309,769	\$ 146,440,207
Cash and Equity in Pooled Investments in Operating Funds	49,778,192	45,768,035
Cash and Equity in Pooled Investments at December 31	\$ 193,087,961	\$ 192,208,242

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2015 AND 2014

NOTE 1 OPERATIONS

Operations of Tacoma Water – The Division, doing business as Tacoma Water, is a division of the City of Tacoma, Washington (the City), Department of Public Utilities (the Department) and is included as an enterprise fund in the Comprehensive Annual Financial Report (CAFR) of the City. 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 99,945 customers and had 234 employees as of December 31, 2015. 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 and multiple other cities. Tacoma Water is organized functionally as Water Distribution Engineering, Water Distribution Operations, Water Quality, Water Supply, Asset and Information Management, and Water Rates and Financial Planning.

Water Distribution Engineering – To plan, forecast and model distribution system expansion and renewal and replacements; engineer, design, and oversee construction of mains, hydrants, services, meters, pressure reducing valves and pressure zones; provide excellent customer service and key account management; support growth and development through coordination, permitting and contracting; promote water conservation through outreach and customer programs.

Water Distribution Operations – To effectively operate and maintain the various components of the distribution system including mains, hydrants, valves, services and meters; to respond to and repair main breaks and leaks; to install new services and hydrants as need for development; to manage the warehouse and materials purchasing; to provide customer service for outages and all other water service issues; to oversee and manage the apprenticeship program; and to provide effective leadership for Tacoma Water's safety program.

Water Quality – To manage, operate and maintain the Green River Headworks and Watershed; to assure natural resource management of Water utility lands including the Watershed; to provide for fish and wildlife habitat management; to install, operate and maintain water treatment equipment within the system; to respond to all matters relating to water quality from the source to the customer; to monitor for contaminants and assure regulatory compliance; to participate in shaping water quality legislation and regulations; to be aware of changes in water system security needs and to coordinate as needed; to support wholesale water customers.

Water Supply – To design, construct, operate and maintain the City's water supply structures, wells, pump stations, reservoirs, standpipes, transmission mains, Tacoma Water buildings and associated property, and electrical and mechanical equipment; to maintain pressure reducing stations and pipeline rights-of-way; to administer water rights; to track water system security issues and coordinate as needed; to oversee and manage Tacoma Water emergency preparedness and coordination with outside agencies.

Water Asset and Information Management – To prepare system and strategic plans for Tacoma Water, to support strategy and performance management; to provide GIS, SAP, Hydraulic Modeling and other technology support for Tacoma Water, and to manage strategic maintenance management, and incorporate risk and lifecycle costs into how Tacoma Water makes decisions.

Water Rates And Financial Planning – To construct financial planning scenarios, develop and implement rates and charges to recover utility costs, forecast demands, lead the development of capital and operating budgets, develop and ensure compliance with rate and financial policies, provide financial and customer statistic reporting to management team, policymakers, and RWSS Partners, develop and administer the financial features of water supply agreements, and maintain cost objects in SAP.

Regional Water Supply System – The Regional Water Supply System (RWSS) is a partnership formed by Tacoma, the City of Kent, Covington Water District and Lakehaven Utility District (the “Participants”) to permit, design, finance, construct, operate, maintain and receive delivery of water from the Second Supply Project. The Second Supply Project consists of the following components: (i) water from the exercise of Tacoma Water’s Second Diversion Water Right, (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) associated Treatment Facilities. Participants’ rights and obligations with regard to the Second Supply Project are called out in the Second Supply Project Agreement. Tacoma has a 15/36 Participant Share and each of the others have a 7/36 Participant Share. A Participant Share represents a Participant’s proportional right to receive water delivered by the Second Supply Project and represents a Participant’s obligation to pay project costs, including Fixed and Variable Operation & Maintenance Costs, Initial Project Construction Costs and ongoing Capital Expenditures. Tacoma, consistent with the Project Agreement, is the owner and operator of the Second Supply Project.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting and Presentation – The financial statements of the Division are prepared under the accrual basis of accounting in accordance with GAAP issued by the Governmental Accounting Standards Board (GASB) applicable to governmental entities that use proprietary fund accounting. The financial statements use a flow of economic resources measurement focus to determine financial position and the change in financial position. The accounting principles used are similar to those applicable to business in the private sector and are maintained on the accrual basis of accounting. Revenues are recognized when earned, and costs and expenses are recognized when incurred.

The Division follows the provisions set forth in regulatory accounting guidance. In general, regulatory accounting 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.

The Division 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.

Change in Accounting Principle – In fiscal year 2015, the Division implemented GASB Statement No. 68, Accounting and Financial Reporting for Pensions and GASB Statement No. 71, Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68. The primary objective of GASB Statement No. 68 is to improve accounting and financial reporting by state and local governments for pensions. GASB Statement No. 68 establishes standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expenses. For defined benefit pension plans, this statement identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value and attribute that present value to periods of employee service. In addition, prior to implementing GASB Statement No. 68, employers participating in a cost-sharing plan recognized annual pension expense essentially equal to their contractually required contribution to the plan. Upon adoption of GASB Statement No. 68, employers participating in cost-sharing plans recognize their proportionate share of the collective pension amounts for all benefits provided through the plan based on an allocation methodology. GASB Statement

No. 71 amends GASB Statement No. 68 regarding the deferred outflows of resources for governments whose current year pension contributions are reported subsequent to the measurement date. The collective financial impact resulting from the implementation of GASB Statements No. 68 and 71 is the adjustment of 2015 beginning balances by \$1.08 million for the Division's portion of the net pension asset or liability and related deferrals incurred in prior years. See Note 10 for further details.

Cash and Equity in Pooled Investments – The Division's fund cash balances are a "deposit" with the City Treasurer's Tacoma Investment Pool (TIP) for the purpose of maximizing interest earnings through pooled investment activities. Cash and equity in pooled investments in the TIP are reported at fair value and changes in unrealized gains and losses are recorded in the Statements of Revenues, Expenses and Changes in Net Position. Interest earned on such pooled investments is allocated daily to the participating funds based on each fund's daily equity in the TIP.

The TIP operates like a demand deposit account in that all City departments, including the Division, have fund balances which are their equity in the TIP. Accordingly, balances are considered to be cash equivalents.

The City of Tacoma Investment Policy permits legal investments as authorized by state law including Certificates of Deposit with qualified public depositories (as defined in Chapter 39.58 of the Revised Code of Washington (RCW)), obligations of the U.S. Treasury, Government Sponsored Agencies and Instrumentalities, bonds issued by Washington State and its Local Governments with an A or better rating, general obligation bonds issued by any State or Local Government with an A or better rating, Bankers' Acceptances, Commercial Paper, Repurchase and Reverse Repurchase agreements, and the Washington State Local Government Investment Pool (LGIP). Daily liquidity requirement to meet the City's daily obligations is maintained by investing a portion of the City's Investment Pool in the LGIP and in a certificate of deposit with East West Bank.

The Division's equity in that portion of the City of Tacoma Investment Pool held in qualified public depositories at December 31, 2015 and 2014 is entirely covered by the Federal Deposit Insurance Corporation (FDIC) and the Washington State Public Deposit Protection Commission (WSPDPC).

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, longer term investments have greater exposure to changes in market interest rates. The City of Tacoma investment policy allows for authorized investments up to 60 months to maturity. One way the City manages its exposure to interest rate risk is by timing cash flows from maturities so that portions of the portfolio are maturing over time to provide cash flow and liquidity needed for operations.

Credit risk is generally the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Repurchase agreements and commercial paper are protected by the Federal Deposit Insurance Corporation (FDIC) insurance up to \$250,000. All deposits not covered by the FDIC are covered by the WSPDPC. The WSPDPC is a statutory authority established under RCW 39.58. It constitutes a fully insured or fully collateralized pool. The WA State Treasures LGIP is authorized by RCW 43.250. The LGIP is operated like a 2A7 fund and is collateralized by short-term legal investments.

Accounts Receivable and Accrued Unbilled Revenues – Accounts receivable consist of amounts owed by private individuals and organizations for goods delivered or services rendered in the regular course of business operations. Receivables are shown net of allowances for doubtful accounts. The Division accrues an estimated amount for services that have been provided but not billed as of December 31st.

Allowance for Doubtful Accounts – A reserve has been established for uncollectible accounts receivable based on historical write-off trends and knowledge of specific circumstances that indicate collection of an account may be unlikely. Generally accounts receivable are considered past due after 30 days.

Interfund Transactions – Unsettled transactions between City funds at year end are recorded as due to or due from other funds.

Materials and Supplies Inventory – Materials and supplies consist primarily of items for maintenance of Division assets and are valued at the lower of average cost or fair market value.

Restricted Assets – In accordance with bond resolutions, agreements and laws, separate restricted funds have been established. These funds consist of cash and investments in pooled investments with restrictions externally imposed and legally enforceable, established by the City Council. Generally, restricted assets include bond construction, reserve and debt service funds, system development charges funds, notes and contracts receivable, and customer deposits.

Bond Premium and Loss on Refunding – Bond premiums are amortized over the life of the bonds using the weighted average of the bonds outstanding. Losses on refunding are amortized on a straight-line basis over the applicable bond period.

Rate Stabilization – The Division has established a rate stabilization account to reduce significant year-to-year variations in rates. Amounts deposited into the account are excluded from the statement of revenues, expenses and changes in net position in accordance with regulated operations. Revenue will be recognized in subsequent periods when it is withdrawn in accordance with rate decisions and debt service covenants.

Utility Plant and Depreciation – Utility plant is stated at original cost, which includes both direct costs of construction or acquisition and indirect costs. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and betterments is capitalized. Assets are capitalized when costs exceed \$5,000 and the useful life exceeds one year.

Depreciation is recorded using a straight-line composite method based on National Association of Regulatory Utility Commissioners recommended economic asset lives from 13 to 60 years for related operating assets placed in service at the beginning of the year. The original cost of property together with removal cost, less salvage, is charged to accumulated depreciation at such time as property is retired and removed from service.

The economic lives for plant in service are as follows:

Source of Supply Plant	34 years
Pumping Plant	40 years
Water Treatment Plant	28 years
Transmission Plant	60 years
Distribution Plant	53 years
General Plant	13 years

Construction Work in Progress – Capitalizable costs incurred on projects which are not in service or ready for use are held in construction in progress. When the asset is ready for service, related costs are transferred to capital assets. Upon determining that a project will be abandoned, the related costs are charged to expense.

Asset Valuation – The Division 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 flows.

Allowance for Funds Used During Construction (AFUDC) – AFUDC represents the cost of borrowed funds used for the construction of utility plant, net of interest earned on unspent construction funds. Capitalized AFUDC is shown as part of the cost of utility plant and as a reduction of interest income and expense.

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 change in net position. 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 the Division's net position. System development charges on uncompleted projects are recorded in other long term liabilities.

Regulatory Assets – The Division has deferred Public Fire Protection Fees and Hyada Surcharges to future periods matching the time when the revenues and expenses are included in rates. The deferred balance is reduced as fees and surcharges are recovered and amortized as expenses on the statements of revenues, expenses and changes in net position.

Intangible Assets – In accordance with GASB No. 51, "Accounting and Financial Reporting for Intangible Assets", land use rights such as easements and right-of-ways are recorded as intangible assets.

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. Based on historical information, 10% of compensated absences are considered short term.

Employees in the original policy accumulate sick leave at the rate of one day per month with no maximum accumulation specified. Employees receive 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.

Operating Revenue – 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.

Non-Operating Revenues and Expenses – These are items that do not qualify as operating defined above such as interest and gain (loss) on disposition of property.

Taxes – The City charges the Division a Gross Earnings Tax at the rate of 8.0%. In addition, the Division pays a 5.029% public utility tax to the State on a certain portion of revenues identified as utility revenues. The Division also pays business and occupation tax to the State at the rate of 1.8% on certain other non-utility revenues. The Division is exempt from payment of federal income tax.

Net Position – The Statement of Net Position reports all financial and capital resources. The difference between assets and liabilities is net position. There are three components of net position: net investment in capital assets, restricted or unrestricted.

Net investment in capital assets consists of capital assets, less accumulated depreciation, reduced by the outstanding balances of any bonds, loans or other borrowings, less outstanding construction funds that are attributable to the acquisition, construction, or improvements of those assets.

Net position components are restricted when constraints placed on net position use are either (1) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or (2) imposed by law through constitutional provisions or enabling legislation.

Unrestricted net position components are those that are not “net investment in capital assets” or “restricted” so that it can be used for daily operation of the Water Utility.

Arbitrage Rebate Requirement – The Division is subject to the Internal Revenue Code (“IRC”), Section 148(f), related to its tax-exempt revenue bonds. The IRC requires that earnings on gross proceeds of any revenue bonds that are in excess of the amount prescribed will be surrendered to the Internal Revenue Service. As such, the fund would record such a rebate as a liability. The Division had no liability in the current or prior year.

Shared Services – The Division receives certain services from other departments and agencies of the City, including those normally considered to be general and administrative. The Division is charged for services received from other City departments and agencies.

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

Significant Risks and Uncertainties – The Division is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include, but are not limited to, 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.

Reclassifications – Changes have been made to the prior year account classifications as needed to conform to the current year presentation format.

NOTE 3 UTILITY PLANT

A summary of the balances and changes in utility plant for 2015 and 2014 follows:

	Balance December 31, 2014	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2015
Intangible Plant	\$ 36,006,378	\$ 556,588	\$ (195,300)	\$ —	\$ 36,367,666
Source of Supply Plant	83,383,567	287,929	—	—	83,671,496
Pumping Plant	9,388,535	32,123	(20,616)	—	9,400,042
Water Treatment Plant	50,736,258	179,028,769	(156)	—	229,764,871
Transmission Facilities	230,964,809	22,097	—	—	230,986,906
Distribution Facilities	422,055,694	13,647,713	(1,969,022)	—	433,734,385
General Plant	33,744,366	1,106,582	(29,300)	(213,199)	34,608,449
Total Water Plant In Service	866,279,607	194,681,801	(2,214,394)	(213,199)	1,058,533,815
Less Accumulated Depreciation	180,549,889	17,102,664	(2,019,094)	(1,190,135)	194,443,324
	685,729,718	177,579,137	(195,300)	976,936	864,090,491
Construction Work In Progress	186,353,639	28,745,579	—	(194,468,602)	20,630,616
Net Utility Plant	\$ 872,083,357	\$ 206,324,716	\$ (195,300)	\$ (193,491,666)	\$ 884,721,107

	Balance December 31, 2013	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2014
Intangible Plant	\$ 35,484,224	\$ 739,974	\$ (217,820)	\$ —	\$ 36,006,378
Source of Supply Plant	79,208,344	4,432,850	(257,627)	—	83,383,567
Pumping Plant	9,278,296	118,293	(8,054)	—	9,388,535
Water Treatment Plant	50,663,085	73,173	—	—	50,736,258
Transmission Facilities	230,252,015	725,956	(13,162)	—	230,964,809
Distribution Facilities	409,827,797	14,379,945	(2,152,048)	—	422,055,694
General Plant	33,789,018	348,794	(315,379)	(78,067)	33,744,366
Total Water Plant In Service	848,502,779	20,818,985	(2,964,090)	(78,067)	866,279,607
Less Accumulated Depreciation	168,125,255	16,783,698	(2,746,082)	(1,612,982)	180,549,889
	680,377,524	4,035,287	(218,008)	1,534,915	685,729,718
Construction Work In Progress	132,672,994	74,421,563	—	(20,740,918)	186,353,639
Net Utility Plant	\$ 813,050,518	\$ 78,456,850	\$ (218,008)	\$ (19,206,003)	\$ 872,083,357

Total Water Plant in Service includes non-depreciable assets of \$58,149,481 for 2015 and \$57,953,220 for 2014. The total amount of interest incurred and capitalized is \$1,665,979 for 2015 and \$7,335,913 for 2014.

NOTE 4 SPECIAL FUNDS

Cash and equity in pooled investments included in Tacoma Water's Special Funds consist of:

Cash and Equity in Pooled Investments	2015	2014
Construction Funds	\$ 33,587,187	\$ 39,509,127
Debt Service Funds	3,633,933	3,597,672
Bond Reserve Funds	22,037,730	22,110,124
System Development Charge Fund	55,889,603	53,255,060
Other Cash and Equity in Pooled Investments	28,161,316	27,968,224
Total	\$ 143,309,769	\$ 146,440,207

NOTE 5 LONG-TERM DEBT

The Division's Long-term Liabilities are primarily for the purpose of capital improvements. Long-term debt activities for 2015 and 2014 were as follows:

	Balance December 31, 2014	Additions	Reductions	Balance December 31, 2015	Due Within One Year
Revenue Bonds	\$ 393,065,000	\$ 23,010,000	\$ (31,370,000)	\$ 384,705,000	\$ 6,080,000
Plus: Unamortized Premium	14,231,813	2,921,513	(1,937,233)	15,216,093	—
Net Revenue Bonds	407,296,813	25,931,513	(33,307,233)	399,921,093	6,080,000
Public Works Trust Fund Loans	30,798,319	—	(2,696,771)	28,101,548	2,696,771
Drinking Water State Revolving Fund Loans	55,889,417	6,420,000	(1,440,773)	60,868,644	1,713,772
Total Long-Term Debt	\$ 493,984,549	\$ 32,351,513	\$ (37,444,777)	\$ 488,891,285	\$ 10,490,543

	Balance December 31, 2013	Additions	Reductions	Balance December 31, 2014	Due Within One Year
Revenue Bonds	\$ 400,015,000	\$ —	\$ (6,950,000)	\$ 393,065,000	\$ 6,305,000
Plus: Unamortized Premium	15,573,188	—	(1,341,375)	14,231,813	—
Net Revenue Bonds	415,588,188	—	(8,291,375)	407,296,813	6,305,000
Public Works Trust Fund Loans	33,495,090	—	(2,696,771)	30,798,319	2,696,771
Drinking Water State Revolving Fund Loans	17,486,717	39,570,473	(1,167,773)	55,889,417	1,440,773
Total Long-Term Debt	\$ 466,569,995	\$ 39,570,473	\$ (12,155,919)	\$ 493,984,549	\$10,442,544

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

SENIOR LIEN BONDS	2015	2014
2005 Water System Revenue and Refunding Bonds, with interest rate of 5.0%, due in 2025. Original Issue: \$46,550,000 Current Portion: \$0	\$ 5,000	\$ 29,365,000
2009 Water System Revenue Bonds, with interest rate at 5.751%, with Build America Bond (BAB) rebate ranging from 31.95% to 35.0%, due in yearly installments starting in 2033 ranging from \$9,800,000 to \$12,210,000 through 2039. Original Issue: \$76,775,000 Current Portion: \$0	76,775,000	\$ 76,775,00
2010A Water System Revenue Refunding Bonds, with interest rates ranging from 3.0% to 5.0%, due in yearly installments ranging from \$555,000 to \$4,655,000 through 2023. Original Issue: \$29,100,000 Current Portion: \$555,000	26,950,000	27,505,000
2010B Water System Revenue Bonds, with interest rates ranging from 4.581% to 5.621%, with Build America Bond (BAB) Rebate ranging from 31.95% to 35% of interest, due in yearly installments starting in 2024 ranging from \$2,115,000 to \$15,390,000 through 2040. Original Issue: \$74,985,000 Current Portion: \$0	74,985,000	74,985,000
2010A Regional Water Supply System Revenue Bonds, with interest rates ranging from 3.0% to 4.0%, due in yearly intsallements starting ranging from \$275,000 to to \$355,000 through 2024. (See Note 6) Original Issue: \$3,595,000 Current Portion: \$275,000	2,800,000	3,070,000
2010B Regional Water Supply System Revenue Bonds, with interest rates ranging from 5.371% to 5.621%, with Build America Bond (BAB) rebate ranging from 31.95% to 35% of interest, due in yearly installments starting in 2025 ranging from \$370,000 to \$5,775,000 through 2040. (See Note 6) Original Issue: \$44,245,000 Current Portion: \$0	44,245,000	44,245,000
2013 Water System Revenue and Refunding Bonds, with interest rates ranging from 2.0% to 4.0%, due in installments of \$980,000 in 2014 and yearly installments starting in 2041 ranging from \$23,820,000 to \$25,765,000 through 2043. Original Issue: \$78,305,000 Current Portion: \$0	74,355,000	74,355,000
2013 Regional Water Supply System Revenue and Refunding Bonds, with interest rates ranging from 4.0% to 5.0%, due in yearly installments ranging from \$670,000 to \$6,425,000 through 2032. Original Issue: \$64,795,000 Current Portion: \$670,000	61,580,000	62,765,000

SENIOR LIEN BONDS (CONT.)**2014****2014**

2015A Water System Refunding Bonds with interest rates ranging from 4.0% to 5.0%, due in yearly installments ranging from \$1,460,000 to \$2,845,000 through 2025.

Original Issue: \$16,645,000

Current Portion: \$0

\$ 16,645,000 \$ —

2015B Water System Refunding Bonds with interest rates ranging from 0.8% to 1.15%, due in yearly installments ranging from \$1,785,000 to \$4,580,000 through 2017.

Original Issue: \$6,365,000

6,365,000 —

Subtotal Sr. Lien Debt	\$ 384,705,000	\$393,065,000
Unamortized Premium	15,216,093	14,231,813
Less Current Portion of Revenue Bond Debt	(6,080,000)	(6,305,000)
Long-term Portion of Revenue Bond Debt	\$ 393,841,093	\$ 400,991,813

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

Year	Principal	Interest
2016	\$ 6,080,000	\$ 18,983,037
2017	6,225,000	18,887,997
2018	6,450,000	18,690,919
2019	7,610,000	18,428,169
2020	7,950,000	18,094,669
2021-2025	44,660,000	84,428,154
2026-2030	56,350,000	72,218,935
2031-2035	76,500,000	56,413,938
2036-2040	98,525,000	32,040,850
2041-2043	74,355,000	6,026,200
	\$ 384,705,000	\$ 344,212,868

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.

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

JUNIOR LIEN DEBT**Public Works Trust Fund Loans**

	2015	2014
2001 Public Works Trust Fund pre-construction loan for the Second Supply Project (SSP) Howard Hanson Dam Additional Storage Project, with interest of .5% per annum, due in yearly installments of \$52,631 through 2021.	\$ 315,789	\$ 368,421
2001 Public Works Trust Fund construction loan for the SSP, with interest of .5% per annum, due in yearly installments of \$533,333 through 2021.	3,200,000	3,733,333
2002 Public Works Trust Fund pre-construction loan for Middle and Headworks section of the SSP, with interest of .5% per annum, due in yearly installments of \$54,180 through 2021.	325,077	379,257
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.	3,718,750	4,250,000
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.	480,263	533,626
2006 Public Works Trust Fund construction loan for the Green River Ozone Treatment Plant, with interest of .5% per annum, due in yearly installments of \$370,588 through 2026.	4,076,471	4,447,059
2008 Public Works Trust Fund construction loan for the McMillin Reservoir Reconstruction, with interest of .5% per annum, due in yearly installments of \$545,870 through 2028.	7,096,308	7,642,178
2012 Public Works Trust Fund construction loan for the Green River Filtration Facility, with interest of .5% per annum, due in yearly installments of \$555,556 through 2031.	8,888,889	9,444,445

Drinking Water State Revolving Fund Loans

2002 construction loan for the Portland Avenue Reservoir, with interest of 2.5% per annum, due in yearly installments of \$161,053 through 2021.	\$ 966,316	\$ 1,127,369
2008 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.5% per annum, due in yearly installments of \$215,108 through 2028.	2,796,409	3,011,517
2009 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.0% per annum, due in yearly installments of \$367,088 through 2032.	6,240,494	6,607,582
2010 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.5% per annum, due in yearly installments of \$303,000 through 2032.	5,151,000	5,454,000
2010 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$273,000 through 2034.	5,187,000	5,460,000
2011 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.5% per annum, due in yearly installments of \$121,523 through 2033.	2,187,426	2,308,949
2011 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$273,000 from 2016 through 2035.	5,460,000	5,460,000
2012 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$546,000 from 2017 through 2036.	10,920,000	10,920,000

JUNIOR LIEN DEBT (CONT.)

	2015	2014
2013 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$546,000 from 2018 through 2037.	\$ 10,920,000	\$ 10,920,000
2013 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$546,000 from 2018 through 2037.	10,920,000	4,620,000
2015 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$6,000 from 2017 through 2036.	120,000	—
Subtotal Junior Lien Debt	88,970,192	86,687,736
Less Current Portion of Debt	(4,410,543)	(4,137,544)
Long-term Portion of Junior Lien Debt	\$ 84,559,649	\$ 82,550,192

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

Year	Principal	Interest
2016	\$ 4,410,543	\$ 644,331
2017	4,962,543	1,038,288
2018	6,054,543	1,842,812
2019	6,054,543	882,072
2020	6,054,543	818,446
2021-2025	25,420,815	3,189,178
2026-2030	20,339,358	1,851,502
2031-2035	12,937,302	715,388
2035-2037	2,736,000	57,420
	\$ 88,970,192	\$ 11,039,435

NOTE 6 SECOND SUPPLY PROJECT AGREEMENT

Four Washington municipalities are the 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 7 SIGNIFICANT CUSTOMER

In October of 2015, RockTenn CP LLC changed their name to WestRock CP LLC. In 2015 this customer accounted for 7.7% of Tacoma Water's total water sales. In May of 2014, Simpson Tacoma Kraft Company (Simpson) was sold to RockTenn CP LLC. Combined, these two customers accounted for 8.3% of Tacoma Water's total water sales in 2014. There were no outstanding accounts receivables from these customers at year-end 2015 or 2014.

Tacoma Water has contracted with WestRock to supply certain quantities of water at a specified rate through July 31, 2020.

NOTE 8 FLEET SERVICES FUND

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 2015 and 2014 were \$2,305,433 and \$2,517,992, 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. The solvency of the Replacement Fund allowed Fleet Services to return a portion of interest earned on Fund investments for the year to their customers. In 2015 and 2014, Fleet Services returned 75% of the interest earned on the capital replacement reserve to Tacoma Water's replacement fund. The amounts refunded in 2015 and 2014 were \$36,966 and \$32,345, respectively, which was used to offset the corresponding year's fleet expenses.

NOTE 9 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 were \$240,000 in 2015 and \$180,000 in 2014. Assets in the Self-Insurance Fund total \$6.9 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.

The City purchased a \$15 million Fiduciary Liability Policy with a \$100,000 deductible that provides for wrongful acts arising out of the administration of the City's employee benefit programs and a Crime policy with a \$1 million limit and \$75,000 deductible for employee dishonesty and for fraudulent or dishonest act by employees against the City for loss of money, securities and property.

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 property within buildings and \$10,000 per vehicle. There is a self-insured retention of \$1.5 million for general liability. The public official liability policy has a \$200,000 deductible. The Department's total liability limit is \$60 million any one occurrence and \$60 million annual aggregate. The general government general liability and public official liability policies provide \$15 million of excess coverage with \$3 million retention. The City has a policy to cover extraordinary worker's compensation claims with a statutory limit and a self-insured retention of \$1 million per occurrence and an additional \$250,000 for each 12 month policy period.

NOTE 10 TACOMA EMPLOYEES' RETIREMENT SYSTEM FUND (TERS)

The Tacoma Employees' Retirement System (TERS), a pension trust fund of the City of Tacoma, issues a publicly available CAFR that includes financial statements and required supplementary information may be obtained by writing to:

Tacoma Employee's Retirement System
3628 South 35th Street
Tacoma, WA 98409

Or the TERS CAFR may be downloaded from the TERS website at www.cityoftacoma.org/retirement.

Administration of The System – The “Tacoma Employees' Retirement System” is a cost-sharing, multiple-employer, defined benefit retirement plan covering substantially all employees of the City of Tacoma, with the exception of police officers, firefighters, and Tacoma Rail employees who are covered by state and federal retirement plans. Employees of the Tacoma-Pierce County Health Department, as well as, certain employees of the Pierce Transit and Law Enforcement Support Agency who established membership in the System when these agencies were still City of Tacoma departments, are also members. The Board of Administration of the Tacoma Employees' Retirement System administers the plan and derives its authority in accordance with Chapter 41.28 RCW and Chapter 1.30 of the Tacoma City Code.

At the direction of the City Council, the System is administered by the Board of Administration (the Board) consisting of nine regular members and one alternate member. The members of the Board are: the Mayor, who serves as Chair; the Director of Finance; the City Manager (or designee); the Public Utilities Director (or designee); three elected employee representatives; one elected retired representative; and one City resident (not employed by the City) elected by the other eight members. The nine Board members appoint a TERS member, either active or retired, as an alternate Board member. The Board is required by the Tacoma Municipal Code to make annual reports to the City Council on the financial condition of the Retirement System. The Board, subject to City Council approval, appoints the Director who is responsible for managing the daily operations of the System.

The breakdown of membership as of December 31, 2014 is as follows:

Retirees and beneficiaries currently receiving benefits	2,167
Terminated vested and other terminated participants	627
Active members:	
City of Tacoma	2,622
South Sound 911	4
Pierce Transit	6
Tacoma-Pierce County Health Department	252
Total active members	2,884
Total membership	5,678

Membership – Substantially all employees of the City of Tacoma are members of the System, with the exception of police officers, firefighter, and Tacoma Rail employees, who are covered by state or federal retirement plans. Other members include employees of the Tacoma-Pierce County Health Department, and certain employees of the Pierce Transit and the South Sound 911 (formerly known as Law Enforcement Support Agency) who established membership in the System when these agencies were still City of Tacoma departments.

Benefits – There are two formulas to calculate the retirement benefits. The benefit paid will be issued on the formula which provides the higher benefit. The most commonly applied formula, “service retirement”, is a product of the member’s average monthly salary for the highest, consecutive 24-month period, the number of years of membership credit, and a percentage factor (2% maximum) that is based on the member’s age and years of service. The other formula is an annuity based on member contributions. There are several options available for the retiree to provide for their beneficiaries. The System also provides death, disability and deferred retirement. Additionally, the System provides cost of living adjustment (COLA) increases up to 2.125% as of July 1st of each year; the actual COLA granted is dependent on the Consumer Price Index (Seattle Area – all items) over the preceding calendar year.

Any active member who has not retired, and has five or more years of service as a member may purchase up to five additional years of service at the time of retirement. Total service including service purchased cannot exceed 30 years.

The System participates in the portability of public retirement benefits in Washington State public retirement. As provided under Chapter 4154 of the RCW, this allows a member to use all years of service with qualified Washington systems to determine retirement eligibility and percentage factor for benefits under the System.

Contributions – The participating employers are responsible for funding the System at a level sufficient to pay obligations and ensure the actuarial and financial soundness of the System. Contribution rates for the employer and the employee are recommended by the Board of Administration and final approval rests with the Tacoma City Council. Currently, the required contribution rate for employees is 9.20% of their regular gross pay; the employer contributes 10.80%, for a combined total of 20.00% which is sufficient to amortize the Unfunded Actuarial Accrued Liability (UAAL) of the System if future experience follows all actuarial assumptions. Changes to the contribution rate are subject to Sections 1.30.340 and 1.30.360 of the Tacoma Municipal Code.

Significant Assumptions – The following actuarial methods were used in the funding valuation.

Measurement Date	December 31, 2014
Valuation Date	January 1, 2015
Actuarial Cost Method	Entry Age Normal Funding is based on statutory contributions rate.
Amortization Method	This amount is compared to a 30-year amortization for the purposes of calculating the Actuarially Determined Contribution. The amortization method for the ADC is as follows: <ul style="list-style-type: none"> • Level percent • Open periods • 30 year amortization period at 01/01/2015 • 4% amortization growth rate
Asset Valuation Method	4 year smoothing period; Corridor - None
Inflation	3%
Salary Increases	4% general wage increase assumption
Investment Rate of Return	7.25%
Cost of Living Adjustment	2.13%
Retirement Age	Varies by age, gender, eligibility
Turnover	Varies by age, gender, eligibility

Benefit and Assumption Changes – The comparability of the data from year to year can be affected by changes in actuarial assumptions, benefit provisions, accounting policies, and other factors. Between January 1, 2014 and January 1, 2015 no assumptions were changed.

Target Allocations – The long-term expected rate of return is determined by adding expected inflation to expected long-term real returns and reflecting volatility and correlation.

The capital market assumptions are per Milliman's (the System's actuary) investment consulting practice as of June 30, 2014. The target asset allocation is based on TERS Investment Policy Statement dated February 2014.

Asset Class	Target Allocation	Long-term Expected Arithmetic Real Rate of Return
Investment grade fixed income	15.0%	2.03%
US inflation-indexed bonds	5.0	1.41
High yield bonds	9.0	4.49
Emerging market debt	5.0	5.05
Global equity	41.5	6.02
Public real estate	2.0	6.38
Private real estate	2.5	3.72
Private equity	10.0	9.02
Master limited partnerships	4.0	4.46
Timber	2.0	3.84
Infrastructure	2.0	5.88
Agriculture	2.0	4.38
Assumed inflation - mean		3.00
Assumed inflation - standard deviation		1.85
Portfolio arithmetic real mean return		5.11
Portfolio median nominal geometric return		7.21
Portfolio standard deviation		12.02
Long-term expected rate of return, net of investment expenses		7.25

Sensitivity Analysis – The following presents the net pension liability of the System, calculated using the discount rate of 7.25%, as well as what the System's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.25%) or 1 percentage point higher (8.25%) than the current rate.

	1% Decrease 6.25%	Current Discount Rate 7.25%	1% Increase 8.25%
Net Pension Liability (asset)	\$ 15,162,650	\$ (881,279)	\$ (14,384,741)

As of December 31, 2015, the deferred inflows and outflows of resources are as follows:

	Deferred Inflows of Resources	Deferred Outflows of Resources
Difference between expected and actual experience	\$ (334,285)	\$ —
Changes in proportionate share	—	5,588
Net difference between projected and actual earnings	(596,068)	—
Contributions made subsequent to the measurement date	—	2,086,719
Total	\$ (930,353)	\$ 2,092,307

The net amount of deferred inflows and outflows, other than contributions made subsequent to the measurement date, will be recognized as pension expense in each of the next four years. Contributions made subsequent to the measurement date will offset net pension liability in the following year.

Amounts will be recognized in pension expense as follows:

Year-ended December 31,	
2016	\$ 289,272
2017	\$ 289,272
2018	\$ 289,272
2019	\$ 56,949

The proportionate share of the Water Division is 9.17%. The proportionate share was based on the actual contributions for the year.

NOTE 11 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 active employees and retirees rather than based on the claims experience of retirees only. This difference is a benefit to the retirees, since health claims costs generally increase with age. GAAP 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. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and are subject to continual revision as results are compared to past expectation and new estimates are made about the future.

Funding Policy – The City uses pay as you go funding; contributions to a separate trust are not required.

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 (3.75%).

The Actuarial Accrued Liability (AAL) is the portion of the present value of benefits attributed to past service only. The portion attributed to future employee service is excluded. For inactive employees, the AAL is equal to the present value of benefits. For active employees, the actuarial present value of the projected benefits of each individual 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 attributed to service between entry age and the valuation date is the actuarial accrued liability.

The Normal Cost is that portion of the City provided benefit attributable to employee service in the current year.

The Annual Required Contribution (ARC) is the amount the City is required to report as an expense for the year. The ARC is equal to the Normal Cost plus an amount to amortize the UAAL on a closed basis of 30 years, beginning January 1, 2007. The remaining amortization period for 2015 is 22 years.

The ARC represents an accounting expense, but the City is not required to contribute the ARC to a separate trust. If the City does not set aside funds equal to the ARC (less current year benefit payments) each year, then the ARC (less benefit payments) will accumulate as a liability or Net OPEB Obligation on the balance sheet. The City has a Net OPEB Obligation as of December 31, 2015 as the City has not set aside funds for OPEB.

Excise Tax for High Cost or “Cadillac” Health Plans in 2018 and Beyond – An excise tax for high cost health coverage or “Cadillac” health plans was included in the Affordable Care Act (ACA) passed into law in March 2010. The provision levies a 40% tax on the value of health plan costs that exceed certain thresholds for single coverage or family coverage. The 2018 annual thresholds are \$10,200 for single coverage and \$27,500 for a family plan. If, between 2010 and 2018, the cost of health care insurance rises more than 55%, the threshold for the excise tax will be adjusted.

The City believes that the current provisions of ACA should be reflected in the projection of benefits and therefore, the value of the excise tax is included in the valuation. It is assumed that there will be no changes to the current law and that there will be no changes in plan design to help mitigate the impact of the tax.

GASB released two new statements for Post Employment Benefits Other than Pension Plans, or OPEB. The new GASB Statements 74 and 75 were released in June 2015 and will replace GASB 43 and 45. The statements are available via the GASB website. GASB 74 is effective for fiscal years beginning after June 15, 2016, and GASB 75 is effective for fiscal years beginning June 15, 2017. These statements will mean fundamental changes in financial reporting for OPEB.

Summary of Changes – As of January 1, 2013 valuation, the total AAL was \$251.840 million. The expected value as of January 1, 2015, based on the 2013 valuation, was \$262.388 million. The total AAL of \$208.814 million was 20% lower than expected. The City experienced a liability gain since the last valuation caused by numerous factors, including a clarification in spouse benefits, which cease once a member attains age 65. It was also caused by smaller than expected changes in medical costs, demographic experience, and a change to the assumption for future medical trends.

The following table is a summary of valuation results with a comparison to the results from the last valuation.

	January 1, 2013	January 1, 2015
Total membership:		
Active employees	3,335	3,404
Terminated vested employees	394	442
Retired employees & dependents	846	744
Total	4,575	4,590
Annual Benefit Payments	\$ 9,887,335	\$ 8,963,089
Discount Rate	3.75%	3.75%
Present Value of Benefits (PVB)	\$ 326,742,538	\$ 262,184,195
Actuarial Accrued Liability (AAL)	\$ 251,839,846	\$ 208,814,312
Assets	\$ —	\$ —
Unfunded Actuarial Accrued Liability (UAAL)	\$ 251,839,846	\$ 208,814,312
Normal Cost	\$ 5,484,587	\$ 3,832,131
Annual Required Contribution (ARC)	\$ 20,058,760	\$ 16,966,964

The following table shows the total value of the benefits provided, the member paid premiums and the City paid benefits as of January 1, 2015.

Value of Subsidy at 3.75% Interest Rate	Total Value of Benefits	Member Paid Premiums	City Paid Benefits
Present Value of Benefits (PVB)	\$ 420,832,932	\$ 158,648,737	\$ 262,184,195
Actuarial Accrued Liability (AAL)	\$ 291,228,295	\$ 82,413,983	\$ 208,814,312
Normal Cost	\$ 9,501,758	\$ 5,669,627	\$ 3,832,131
Annual Benefit Payments	\$ 12,325,369	\$ 3,362,280	\$ 8,963,089

The following table shows the calculation of the Annual Required Contribution and Net OPEB Obligation for the City and for the Division as of December 31, 2015.

	City	Water
Determination of Annual Required Contribution:		
Normal Cost at Year-end	\$ 3,832,131	\$ 263,819
Amortization of UAAL	13,134,833	113,394
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 377,213
Determination of Net OPEB Obligation:		
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 377,213
Interest on prior year Net OPEB Obligation	2,480,183	109,055
Adjustments to ARC	(3,492,760)	(128,875)
Annual OPEB Cost	15,954,387	357,393
Actual benefits paid	(8,963,089)	(115,102)
Increase in Net OPEB Obligation	6,991,298	242,291
Net OPEB Obligation - beginning of year	66,138,204	2,908,139
Net OPEB Obligation - end of year	\$ 73,129,502	\$ 3,150,430

The Division has included the liability in the other long term liabilities on the Statement of Net Position.

Funding Status and Funding Progress - The following table shows the annual OPEB cost and net OPEB obligation for three years. This table is based upon a 3.75% interest rate.

Year Ended	Annual OPEB Cost		Benefits Paid		Net OPEB	
	City	Water	City	Water	City	Water
12/31/2013	\$ 19,528,767	\$ 581,617	\$ 9,887,335	\$ 139,219	\$ 56,110,801	\$ 2,497,707
12/31/2014	\$ 19,319,944	\$ 575,750	\$ 9,292,539	\$ 165,318	\$ 66,138,206	\$ 2,908,139
12/31/2015	\$ 15,954,387	\$ 357,394	\$ 8,963,089	\$ 115,102	\$ 73,129,502	\$ 3,150,430

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 the 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 UAAL. In determining the Annual Required Contribution, the UAAL is amortized as a level percentage of expected payrolls for non-LEOFF 1 groups. For LEOFF 1, the UAAL is amortized as a level dollar amount. The amortization period was 30 years in 2007 and the remaining is now 22 years.

Actuarial Methods and Significant Actuarial Assumptions:

Valuation Date	January 1, 2015												
Census Date	January 1, 2015												
Actuarial Cost Method:	Entry Age												
Amortization Date:	Combination of level percentage and level dollar amount, see note above.												
Remaining Amortization Period:	22 years, closed												
Demographic Assumptions:	Demographic assumptions regarding retirements, disability, and turnover are based upon pension valuations for the various pension plans.												
Actuarial Assumptions:													
Discount Rate	3.75% for pay-as-you-go funding												
Medical Cost Trend	<table> <tr><td>2015</td><td>6.90%</td></tr> <tr><td>2016</td><td>6.60%</td></tr> <tr><td>2017</td><td>5.90%</td></tr> <tr><td>2020</td><td>5.50%</td></tr> <tr><td>2030</td><td>5.90%</td></tr> <tr><td>2040</td><td>5.70%</td></tr> </table> <p>The medical cost rate is assumed to continue grading downward until achieving the ultimate rate of 4.8% in 2071 and beyond. These trend rates assume that, over time, deductibles and out-of-pocket maximums will be periodically increased as medical trends increase. The trends above do not reflect increases in costs due to the excise tax.</p>	2015	6.90%	2016	6.60%	2017	5.90%	2020	5.50%	2030	5.90%	2040	5.70%
2015	6.90%												
2016	6.60%												
2017	5.90%												
2020	5.50%												
2030	5.90%												
2040	5.70%												
Economic Assumptions:													
Discount Rate (Liabilities)	3.75%												
Demographic Assumptions:	<p>Eligibility:</p> <p>Disability - Five years of service are required for non-service connected disability.</p> <p>Retirement - TERS members are eligible for retiree medical benefits after becoming eligible for service retirement pension benefits (either reduced or full pension benefits):</p> <ul style="list-style-type: none"> • Age 55 with 10 years of service • Age 40 with 20 years of service 												

NOTE 12 COMMITMENTS AND CONTINGENCIES

Capital Improvements – The financial requirement for Tacoma Water’s 2015-2016 biennial Capital Improvement program is approximately \$32.9 million and Tacoma Water has substantial contractual commitments relating to the program. At December 31, 2015 the remaining financial requirement for Capital Improvement Programs relating to all prior biennia is approximately \$4.1 million.

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.

General Legal Matters – The Utility has received several other miscellaneous claims or litigation that either do not allege material amounts or that the Legal Department has determined do not pose a risk of liability to the Utility.

TACOMA **RAIL**



2015

THE SALE OF A 1.3-MILE SEGMENT OF THE MOUNTAIN DIVISION IN JANUARY 2015 **NETTED \$4 MILLION FOR THE CITY OF TACOMA** AND EFFECTIVELY **RETIRED NEARLY TWO-THIRDS OF THE OUTSTANDING DEBT** OF THE DIVISION.

TACOMA | RAIL

It was a challenging year for Tacoma Rail as revenues lagged in the first quarter due to a labor dispute in West Coast ports that was not resolved until March. A fire at U.S. Oil & Refining Co.'s facility in Tacoma led to its premature shutdown in May, a full three weeks ahead of a scheduled month-long maintenance outage in June. And, while line haul count was up by almost 2,000 units in 2015 over 2014, the traffic mix of more intermodal platforms and fewer commercial railcars led to a decline in total revenue of approximately \$1.1 million.

Still, Tacoma Rail helped build some significant successes in 2015. For the first time in 10 years, all of Tacoma Rail's labor organizations started operating under current contracts following four years of negotiations, 18 months of federal mediation and the ratification of a conductors' agreement. And, the ports of Tacoma and Seattle announced the formation of the Northwest Seaport Alliance, joining the freight operations of both entities to compete more effectively against other West Coast ports for international intermodal container and breakbulk business. Tacoma Rail is playing an active role in optimizing the Alliance's use of marine terminals and rail infrastructure by participating on planning committees and in its operations control center.

Tacoma Rail continues to fund a volume incentive program to attract more intermodal business as part of its operating agreement with the Port of Tacoma. It has also modified its unit train rate structure for crude oil to allow U.S. Oil to source product on Union Pacific Railroad and the BNSF Railway. An ethanol unit train rate was also established for Targa Sound Terminals as that product began to move in large quantities to the customer's blending facilities on the Hylebos Waterway.

TACOMA RAIL
**CONTINUES TO FUND
A VOLUME INCENTIVE
PROGRAM TO ATTRACT
MORE INTERMODAL
BUSINESS AS PART
OF ITS OPERATING
AGREEMENT WITH THE
PORT OF TACOMA.**



THE YEAR SAW **TACOMA RAIL** WEATHERING SOME CHALLENGING CIRCUMSTANCES AS WELL AS CONTINUING TO MEET ITS CORE GOAL OF **PROVIDING EFFICIENT, COST-EFFECTIVE RAIL SERVICE.**

The crash in crude oil prices in 2015 brought ceramic sand shipments out of the Port of Olympia to a virtual halt. The man-made sand, imported from China, is used in the drilling process that extracts oil and gas from shale formations. From a record high of 3,171 carloads in 2014, total traffic on the Capital Division declined 45% to 1,748 carloads. BNSF Railway also lowered the handling charges it paid Tacoma Rail to deliver cars to interchange at the beginning of the year, further eroding the division's financial condition. Unable to negotiate a compensatory rate for traffic moving on the Belmore and Quadlock Lines, Tacoma Rail opted not to renew its lease with BNSF and will cease serving these branch lines in March 2016.

The Mountain Division, administered by Tacoma Rail on behalf of the City of Tacoma, operated again at near breakeven in 2015. The sale of a 1.3-mile segment of the Mountain Division in January 2015 netted \$4 million for the City of Tacoma and effectively retired nearly two-thirds of the outstanding debt of the division. The number of carloads handled fell from 1,303 in 2014 to 1,167 in 2015. An interlocal agreement with Lewis County and the City of Chehalis to explore the sale of 20 miles of line on the south end of the Mountain Division to these two entities is in place through the end of 2016. A study commissioned to ascertain the value of, and determine potential uses for, the line is underway.

The year saw Tacoma Rail weathering some challenging circumstances as well as continuing to meet its core goal of providing efficient, cost-effective rail service.

FINANCIAL HIGHLIGHTS

In Millions, For the Years Ended December 31,	2015	2014	2013	2012	2011
Total Income	\$30.3	\$30.5	\$27.9	\$24.1	\$20.1
Operating Expenses	24.6	25.5	22.8	19.4	16.5
Income Available for Debt Service	\$5.7	\$5.0	\$5.1	\$4.7	\$3.6
Debt Service	\$0.3	\$0.3	\$0.3	\$0.3	\$0.3
Debt Service Coverage	21.75x	19.16x	19.73x	18.14x	14.05x
Plant Additions	\$5.9	\$7.9	\$4.8	\$7.4	\$10.7
Number of Cars Switched	102,173	108,137	99,366	92,117	68,953
Average Rates (per car)					
Line Haul Car	\$245.12	\$237.29	\$239.48	\$222.36	\$246.77
Local & Miscellaneous Car	\$468.28	\$510.59	\$662.72	\$343.33	\$340.07

Switching Revenues (in millions)	2015	2014
Line Hauls - Intermodal	11.44	11.32
Line Hauls - Commercial	12.15	12.21
Line Hauls - Capital Division	0.75	1.40
Miscellaneous	1.34	1.56

Switching Activities	2015	2014
Line Hauls - Intermodal	68,453	69,872
Line Hauls - Commercial	29,091	32,096
Line Hauls - Capital Division	1,733	3,111
Miscellaneous	2,896	3,058

Operating Expenses	2015	
Operations	11,425,661	44%
Administration	5,594,322	22%
Mechanical	4,640,554	18%
Construction	2,507,631	10%
Depreciation	1,220,882	5%
Taxes	417,135	2%

REPORT OF INDEPENDENT AUDITORS

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

Report on the Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Washington Department of Public Utilities, Rail Division (the Division), which comprise the statements of net position as of December 31, 2015 and 2014, and the related statements of revenue, expenses and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Division as of December 31, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis on pages 5 through 10 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the

required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The statistical data presented on pages 32 through 42 and the superintendent's report presented on pages 43 through 44 are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on it.

Miss Adams LLP

Tacoma, Washington
April 1, 2016

MANAGEMENT'S DISCUSSION & ANALYSIS

The following discussion and analysis of Tacoma Rail's financial performance provides an overview of the financial activities for the years ended December 31, 2015 and 2014. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues, provide an overview of the financial activities, and identify changes in the 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 (GAAP) in the United States of America, 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, 2015 and 2014, include Statements of Net Position, Statements of Revenues, Expenses and Changes in Net Position, and Statements of Cash Flows. The Statements of Net Position present information on all of Tacoma Rail's assets and liabilities, with the difference between the two reported as net position. The Statements of Revenues, Expenses and Changes in Net Position 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, capital and related financing, non-capital financing and investing activities.

The Notes to 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 Tacoma Rail's presentation of financial position, results of operations and changes in cash flow.

Financial Highlights

Tacoma Rail continued to meet its goal of providing efficient, cost-effective rail service to the Ports of Tacoma and Olympia as well as Tacoma's industrial areas. Doing so required adding operating staff, a continued investment in infrastructure and enforcing a disciplined tactical plan to respond to growth in local, national and world economies as they pertain to the rail industry.

The operating results for Tacoma Rail in 2015 indicate a slight increase in intermodal platform traffic and a small decrease in non-intermodal traffic. The intermodal coincides with the formation of the Northwest Seaport Alliance; a partnership between the Port of Tacoma and the Port of Seattle. Non-intermodal traffic decreased after some commodities lost profitability margin due to the fall of oil prices. Locomotive servicing and related revenue increased dramatically due to the addition of the Burlington Northern Santa Fe (BNSF) into the program in late 2014 and increased services to Union Pacific (UP) in 2015.

Overview of the Financial Statements

Tacoma Rail is reporting a change in net position of \$2.8 in 2015, compared to \$2.0 million in 2014, an increase of \$0.8 million. The increase in net position is due to a decrease of \$0.3 million in operating revenues, a decrease of \$0.8 million in operating expenses, and a decrease in transfers of \$0.3 million.

In 2014, Tacoma Rail realized a change in net position of \$2.0 million, compared to \$1.9 million in 2013, an increase of \$0.1 million. The increase in net position was due to an increase of \$2.5 million in operating revenues, an increase of \$2.8 million in operating expenses, an increase of \$0.9 million in contributions, and an increase of \$0.5 million in transfers out.

The following table highlights Tacoma Rail's past three years' operating results.

Operating Results (in thousands)

Description	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Operating Revenues	\$ 29,165	\$ 29,457	\$ 26,943	\$ (292)	\$ 2,514
Operating Expenses	25,806	26,563	23,782	(757)	2,781
Operating Income	3,359	2,894	3,161	465	(267)
Net Non-Operating Revenues	1,061	991	980	70	11
Contributions	846	878	—	(32)	878
Transfers Out	(2,455)	(2,751)	(2,273)	296	(478)
Change in Net Position	\$ 2,811	\$ 2,012	\$ 1,868	\$ 799	\$ 144

Net position may serve over time as a useful indicator of an entity's financial position.

The following analysis highlights net position for the last three years.

Statements of Net Position (in thousands)

Description	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Capital Assets (Net)	\$ 24,748	\$ 21,059	\$ 18,016	\$ 3,689	\$ 3,043
Current and Other Assets	\$ 14,909	\$ 16,029	\$ 13,027	\$ (1,120)	\$ 3,002
Total Assets	\$ 39,657	\$ 37,088	\$ 31,043	\$ 2,569	\$ 6,045
Net Investments in Capital Assets	\$ 18,246	\$ 16,023	\$ 14,797	\$ 2,223	\$ 1,226
Restricted Net Position	65	65	65	—	—
Unrestricted Net Position	8,731	8,142	7,356	589	786
Total Net Position	27,042	24,230	22,218	2,812	2,012
Long-Term Debt, net of current maturities	5,556	4,483	2,765	1,073	1,718
Current and Long Term Liabilities	7,059	8,375	6,060	(1,316)	2,315
Total Liabilities	12,615	12,858	8,825	(243)	4,033
Total Net Position & Liabilities	\$ 39,657	\$ 37,088	\$ 31,043	\$ 2,569	\$ 6,045

Revenues

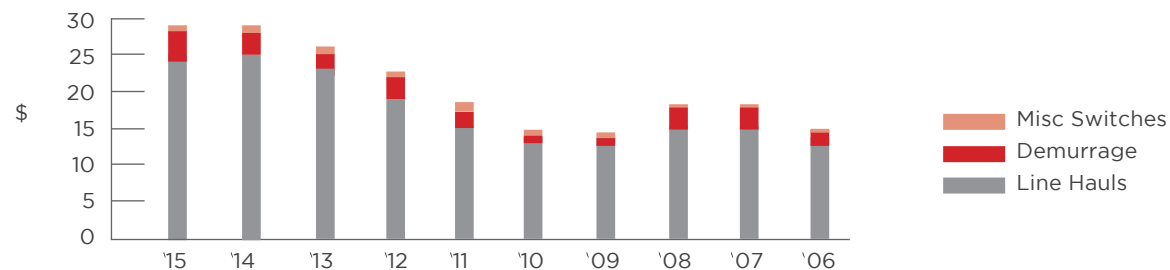
2015 Compared to 2014

In 2015, Tacoma Rail operating revenues of \$29.2 million were \$292,000 lower than the \$29.5 million in 2014. Overall switching revenues decreased \$804,000 (3.0%), from 2014. The following table summarizes the switching revenues by activity type for the last two years.

Activity Types	Rail Cars				Switching Revenues (in thousands)			
	2015	2014	Var	% Chg	2015	2014	Var	% Chg
Intermodal Line Hauls	68,453	69,872	(1,419)	(2.0%)	\$ 11,440	\$ 11,324	\$ 116	1.0%
Commercial Line Hauls	29,091	32,096	(3,005)	(9.4%)	12,147	12,215	(68)	(0.6%)
Capital Div. Line Hauls	1,733	3,111	(1,378)	(44.3%)	748	1,395	(647)	(46.4%)
Miscellaneous Switches	2,896	3,058	(162)	(5.3%)	1,356	1,561	(205)	(13.1%)
Total Line Hauls	102,173	108,137	(5,964)	(5.5%)	\$ 25,691	\$ 26,495	\$ (804)	(3.0%)

Demurrage and other operating revenues increased \$512,000. Demurrage revenue decreased by \$58,000 and locomotive servicing revenue and other revenue increased \$570,000. This was due to both the addition of the BNSF to locomotive servicing program and an increase in the locomotive services rendered to UP.

Operating Revenues (in millions)



2014 Compared to 2013

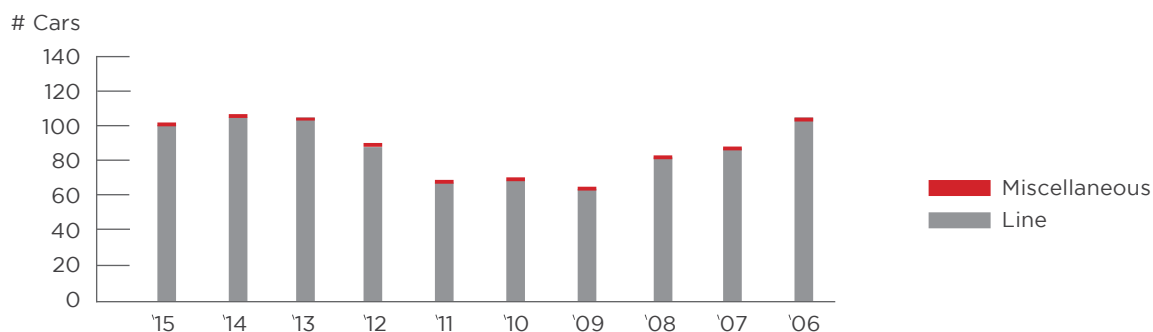
In 2014, Tacoma Rail operating revenues of \$29.5 million were \$2.5 million higher than the \$26.9 million in 2013. Overall switching revenues increased \$1.9 million (7.8%), from 2013.

Switching Activities

Switching activities decreased in 2015 by 5,964 cars (5.5%) to 102,173, from 108,137 in 2014. The most significant decrease in switching activity can be seen in commercial line-hauls which were down by 3,005 cars (9.4%) due to a decrease in commercial line haul rail traffic. The average number of cars switched over the last ten years is 86,553.

During 2014, total switching activities increased by 8,771 cars (8.8%) from 2013. The increase in intermodal rail traffic was the dominant factor. Intermodal line-hauls were up by 4,891 cars (7.5%) in 2014.

Switching Activities (in thousands)



The table below shows the changes in switching volumes for the last three years.

Switching Activities

Description	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Line Hauls	99,277	105,079	97,536	(5,802)	7,543
Miscellaneous Switches	2,896	3,058	1,830	(162)	1,228
Total Cars Switched	102,173	108,137	99,366	(5,964)	8,771

Expenses

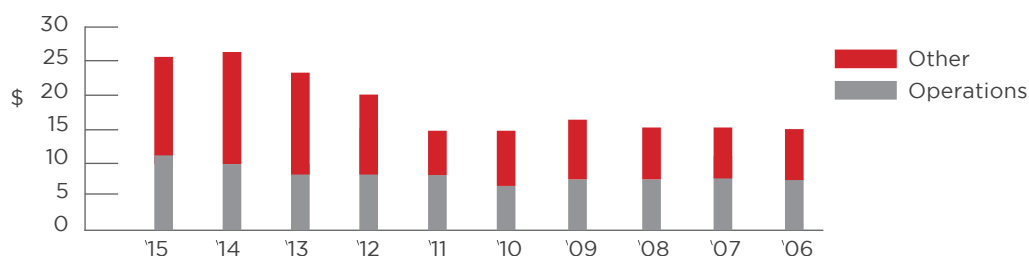
2015 Compared to 2014

In 2015, Tacoma Rail operating expenses of \$25.8 million were \$0.8 million lower than the \$26.6 million in 2014. Salaries and wages increased \$2.0 million and supplies and expenses decreased \$2.9 million.

Salaries and wages were higher due to an increase in personnel, an increase in cost of benefits and a new labor agreement with the largest union at Tacoma Rail. Supplies and expenses decreased \$2.9 million. The decrease in supplies was mainly attributable to incurred but not reported (IBNR) claims decrease of \$2.4 million and a decrease of \$0.4 million of capitalized administrative and general (A&G) expenses.

The capitalized A&G rate was changed in 2015 to 7.97% from 12.43% in 2014.

Operating Expenses (in millions)



2014 Compared to 2013

In 2014, Tacoma Rail operating expenses of \$26.6 million were \$2.8 million higher than the \$23.8 million in 2013. This was primarily due to an increase of \$1.4 million in salaries and wages and increase of \$1.4 million in supplies and expenses. Salaries and wages were higher in 2014 due to 8 new personnel and an increase in overtime in response to increased traffic volume and for the new BNSF locomotive servicing agreement. The increase in supplies and expenses was mainly attributable to an increase in external services of \$0.7 million and an increase of \$0.4 million in equipment and supplies. Incurred but not reported (IBNR) claims increased \$0.3 million in 2014 from \$1.1 million in 2013.

Capital Assets

Total Capital Assets increased \$4.9 million during 2015. This increase was reflected primarily in road property plant which increased by \$4.7 million due to track upgrades and rehabilitation projects such as the SR-509 track rebuild, Port of Tacoma RR crossing, Taylor Way and West Loop. Machinery and equipment increased \$0.4 million for the purchase of a Ballast Regulator.

During 2014, total Capital Assets increased \$3.8 million. This increase was reflected primarily in road property plant which increased by \$3.7 million due to track upgrades, switch replacements and the installation of the U.S. Oil WYE track. Buildings increased \$0.1 million due to camera security system upgrade, lighting facility upgrade and parking lot asphalt relay.

The following table summarizes Tacoma Rail's capital assets, net of accumulated depreciation, for the last three years.

Capital Assets, Net of Accumulated Depreciation (in thousands)

Description	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Land	\$ 160	\$ 160	\$ 160	\$ —	\$ —
Road Property Plant	14,951	10,926	7,687	4,025	3,239
Building	1,614	1,711	1,754	(97)	(43)
Machinery Equipment	7,051	7,102	7,693	(51)	(591)
Office and Fixture	156	160	21	(4)	139
Construction Work in Progress	816	1,000	701	(184)	299
Total Net Capital Assets	\$ 24,748	\$ 21,059	\$ 18,016	\$ 3,689	\$ 3,043

Additional information on Tacoma Rail's capital assets can be found in Note 3 to the Financial Statements.

Debt Administration

In 2015, Tacoma Rail obtained five new Washington State loans from the Department of Transportation for the following capital track projects: Tyler Wye rehabilitation \$311,457, Edwards Crossover rehabilitation \$156,997, East Lead Low Side rebuild \$469,270, West Lead High Side rebuild \$369,518 and Transfer Yard connection \$150,000. No funds have been drawn on these projects. Draws were taken in 2015 on Taylor Way Track Rehabilitation & Extension, West Loop and SR509 track improvement in the amounts of \$594,793, \$515,770 and \$908,632 respectively.

In 2014, Tacoma Rail obtained one new Washington State loan from the Department of Transportation for SR-509 Track Rebuild in the amount of \$1,037,012 from which no funds have been drawn. Draws were taken in 2014 on Yard Tracks 8 & 9, N. Intermodal Yard Lead Track, East Loop 17th St and Taylor Way in the amounts of \$618,626, \$366,387, \$773,070 and \$510,265 respectively.

The following table shows the outstanding long-term debt balances for the past three years. Additional information on Tacoma Rail's long-term debt can be found in Note 4 to the Financial Statements.

Long-Term Debt (in thousands)

	2015	2014	2013	15/14 Increase (Decrease)	14/13 Increase (Decrease)
Long-Term Debt Balance, December 31	\$ 6,502	\$ 5,036	\$ 3,219	\$ 1,466	\$ 1,817

Debt Service Coverage

Tacoma Rail is required by its bond covenants to maintain a 1.25 times debt service coverage. In 2015, principal and interest were covered 21.75 times compared to 19.16 times in 2014 and 19.73 times in 2013.

Summary

The management of the Finance Department of the City of Tacoma is responsible for preparing the accompanying financial statements and for their integrity. We prepared the financial statements according to GAAP in the United States of America, and they fairly portray Tacoma Rail's financial position and operating results. The Notes to Financial Statements are an integral part of the basic financial statements and provide additional financial information.

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 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/CEO



Andrew Cherullo
Finance Director

2015 FINANCIAL REPORTS

Statements of Net Position

December 31,

Assets	2015	2014
Capital Assets		
Road and Equipment Property	\$ 41,306,956	\$ 36,412,953
Less Accumulated Depreciation	(17,374,337)	(16,354,584)
Total	23,932,619	20,058,369
Construction Work in Progress	815,769	1,000,440
Net Capital Assets	24,748,388	21,058,809
Special Funds		
Debt Service Funds	64,861	65,104
Total Special Funds	64,861	65,104
Current Assets		
Cash and Equity in Pooled Investments	9,095,985	10,043,524
Customer Accounts Receivable (Net of Allowance for Doubtful Accounts of \$182,772 in 2015 and \$86,940 in 2014)	2,839,515	2,861,792
Grants Receivable	—	81,966
Interfund Receivable	53,051	103,243
Prepayments	1,917,733	1,988,311
Materials and Supplies Inventory	937,461	885,400
Total Current Assets	14,843,745	15,964,236
Total Assets	\$ 39,656,994	\$ 37,088,149

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

Net Position and Liabilities**December 31,****2015****2014****Net Position**

Net Investment in Capital Assets	\$ 18,246,395	\$ 16,023,002
Restricted for:		
Debt Service	64,861	65,104
Unrestricted	8,730,405	8,142,084
Total Net Position	27,041,661	24,230,190

Long-Term Debt, Net of Current Maturities

2006 Senior Lien Revenue Bond	64,238	312,763
State Loans	5,492,064	4,170,038
Total Long-Term Debt	5,556,302	4,482,801

Current Liabilities

Accounts Payable	536,827	1,244,449
Customer Deposits	45,900	45,900
Wages Payable and Compensated Absences	243,713	547,113
Unemployment and Other Tax Payables	273,464	281,435
Volume Incentive Payable	1,208,334	916,666
Current Portion of Long-Term Debt	945,691	553,006
Interest Payable	4,214	7,389
Interfund Payable	185,446	500,287
Total Current Liabilities	3,443,589	4,096,245

Long-Term Liabilities

On the Job Injury Reserve	721,029	696,783
Long-Term Portion of Compensated Absences	1,018,056	912,353
Other Post Employment Benefits	695,629	363,064
Incurred but not Reported Claims	1,180,728	2,306,713
Total Long-Term Liabilities	3,615,442	4,278,913
Total Liabilities	12,615,333	12,857,959

Total Net Position and Liabilities

\$ 39,656,994

\$ 37,088,149

**Statements of Revenues, Expenses and Changes
in Net Position**

	Year Ended December 31,	
	2015	2014
Operating Revenues		
Switching Revenues	\$ 25,690,797	\$ 26,495,108
Demurrage and Other Operating Revenues	3,474,443	2,962,289
Total Operating Revenues	29,165,240	29,457,397
Operating Expenses		
Maintenance of Way and Structures	2,507,631	2,745,664
Mechanical	4,640,554	4,116,105
Operations	11,425,661	10,810,206
Administration	5,594,322	7,391,559
Taxes - State	417,135	429,875
Depreciation	1,220,882	1,069,265
Total Operating Expenses	25,806,185	26,562,674
Net Operating Income	3,359,055	2,894,723
Non-Operating Revenues (Expenses)		
Interest Income	51,379	72,535
Miscellaneous	1,032,046	952,326
Interest Expense	(21,678)	(34,122)
Total Non-Operating Revenues	1,061,747	990,739
Contributions - Grants	587,480	81,966
Contributions - Others	258,583	795,741
Total Contributions	846,063	877,707
Transfers		
City of Tacoma Gross Earnings Tax	(2,410,016)	(2,440,631)
Transfers to Other Funds	(45,378)	(310,527)
Total Transfers	(2,455,394)	(2,751,158)
Change in Net Position	2,811,471	2,012,011
Total Net Position - Beginning Of Year	24,230,190	22,218,179
Total Net Position - End Of Year	\$ 27,041,661	\$ 24,230,190

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

Statements Of Cash Flows**Year Ended December 31,****2015****2014****Cash Flows From Operating Activities**

Cash from Customers	\$ 29,319,675	\$ 28,962,712
Cash Paid to Suppliers	(9,938,384)	(9,313,504)
Cash Paid to Employees	(15,908,933)	(13,420,062)
Taxes Paid	(425,106)	(378,498)
Net Cash Provided by Operating Activities	3,047,252	5,850,648

Cash Flows From Non-Capital Financing Activities

Transfers to Other Funds	(2,455,394)	(2,751,158)
Net Cash Used in Non-Capital Financing Activities	(2,455,394)	(2,751,158)

Cash Flows From Capital And Related Financing Activities

Capital Expenditures, Net	(4,910,461)	(4,112,399)
Principal Payments on Long-Term Debt	(553,009)	(453,862)
Interest Paid	(24,853)	(37,131)
Proceeds from Capital Contributions	846,063	877,707
Proceeds from Long-Term Debt	2,019,195	2,270,848
Proceeds from Other Non-Operating Revenues	1,032,046	952,326
Net Cash Used in Capital and Related Financing Activities	(1,591,019)	(502,511)

CASH FLOWS FROM INVESTING ACTIVITIES

Interest on Investments	51,379	72,535
Net Cash Provided by Investing Activities	51,379	72,535

Net Increase in Cash and Equity in Pooled Investments	(947,782)	2,669,514
---	-----------	-----------

Cash and Equity in Pooled Investments at January 1	10,108,628	7,439,114
---	-------------------	------------------

Cash and Equity in Pooled Investments at December 31	\$ 9,160,846	\$ 10,108,628
---	---------------------	----------------------

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

**Reconciliation of Operating Income to
Net Cash Provided by Operating Activities:**

	Year Ended December 31,	
	2015	2014
Operating Income	\$ 3,359,055	\$ 2,894,723
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:		
Depreciation	1,220,882	1,069,265
Cash provided from changes in operating assets and liabilities:		
Accounts and Grants Receivable	104,243	(464,497)
Interfund Receivable	50,192	(21,788)
Materials and Supplies Inventory	(52,061)	(45,730)
Prepayments	70,578	199,117
Accounts Payable	(707,622)	137,883
Customer Deposits	—	(8,400)
Unemployment and Other Tax Payables	(7,971)	51,377
Wages Payable	(315,145)	72,472
Volume Incentive Payable	291,668	124,998
Interfund Payable	(314,841)	365,634
Accrued Compensated Absences	117,448	238,674
Other Long-Term Liabilities & OJI Reserve	(769,174)	1,236,920
Total Adjustments	(311,803)	2,955,925
Net Cash Provided by Operating Activities	\$ 3,047,252	\$ 5,850,648

**Reconciliation of Cash and Equity in Pooled Investments to
Balance Sheet:**

Cash and Equity in Pooled Investments in Special Funds	\$ 64,861	\$ 65,104
Cash and Equity in Pooled Investments in Operating Funds	9,095,985	10,043,524
Cash and Equity in Pooled Investments at December 31	\$ 9,160,846	\$ 10,108,628

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2015 AND 2014

NOTE 1 OPERATIONS

Operations of Tacoma Rail - Tacoma Rail (the Division) is a division of the City of Tacoma, Department of Public Utilities, which also operates the Light and the Water Divisions and is included as an enterprise fund in the Comprehensive Annual Financial Report (CAFR) of the City. Tacoma Rail provides rail switching services to the Port of Tacoma and major Tacoma industries under its Tidelands Division. Tacoma Rail also provides rail service from its Capital Division. The Capital Division interchanges rail cars with BNSF in East Olympia. No traffic for the Capital Division enters Tacoma Rail's Tidelands infrastructure. In addition, Tacoma Rail manages the Mountain Division which is a reporting unit within Public Works and is included in the CAFR. Tacoma Rail is reimbursed for direct expenses. An operating agreement between Tacoma Rail and the Mountain Division is in place through 2016.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting and Presentation - The financial statements of the Division are prepared under the accrual basis of accounting in accordance with GAAP issued by the Governmental Accounting Standards Board (GASB) applicable to governmental entities that use proprietary fund accounting. The financial statements use a flow of economic resources measurement focus to determine financial position and the change in financial position. The accounting principles used are similar to those applicable to businesses in the private sector and are maintained on the accrual basis of accounting. Revenues are recognized when earned, and costs and expenses are recognized when incurred.

Cash and Equity in Pooled Investments - The Division's cash balances are a "deposit" with the City Treasurer's Tacoma Investment Pool (TIP) for the purpose of maximizing interest earnings through pooled investment activities. Cash and equity in pooled investments in the TIP are reported at fair value and changes in unrealized gains and losses are recorded in the Statements of Revenues, Expenses and Changes in Net Position. Interest earned on such pooled investments is allocated daily to the participating funds based on each fund's daily equity in the TIP.

The TIP operates like a demand deposit account in that all City departments, including the Division, have fund balances which are their equity in the TIP. Accordingly, balances are considered to be cash equivalents.

The City of Tacoma Investment Policy permits legal investments as authorized by state law including Certificates of Deposit with qualified public depositories (as defined in Chapter 39.58 RCW), obligations of the U.S. Treasury, Government Sponsored Agencies and Instrumentalities, bonds issued by Washington State and its Local Governments with an A or better rating, general obligation bonds issued by any State or Local Government with an A or better rating, Bankers' Acceptances, Commercial Paper, Repurchase and Reverse Repurchase agreements, and the Washington State Local Government Investment Pool (LGIP). Daily liquidity requirement to meet the City's daily obligations is maintained by investing a portion of the City's Investment Pool in the LGIP and in a certificate of deposit with East West Bank.

The Division's equity in that portion of City Tacoma Investment Pool held in qualified public depositories at December 31, 2015 and 2014 is entirely covered by the Federal Deposit Insurance Corporation (FDIC) and the Washington State Public Deposit Protection Commission (WSPDPC).

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, longer term investments have greater exposure to changes in market interest rates. The City of Tacoma investment policy allows for authorized investments up to 60 months to maturity. One way the City manages its exposure to interest rate risk is by timing cash flows from maturities so that portions of the portfolio are maturing over time to provide cash flow and liquidity needed for operations.

Credit risk is generally the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Repurchase agreements and commercial paper are protected by the FDIC insurance up to \$250,000. All deposits not covered by the FDIC are covered by the WSPDPC. The WSPDPC is a statutory authority established under RCW 39.58. It constitutes a fully insured or fully collateralized pool. The LGIP is authorized by RCW 43.250. The LGIP is operated like a 2A7 fund and is collateralized by short-term legal investments.

Customer Accounts Receivable - Accounts receivable consist of amounts owed by private individuals and organizations for goods delivered or services rendered in the regular course of business operations. Receivables are shown net of allowances for doubtful accounts.

Allowance for Doubtful Accounts - A reserve has been established for uncollectible accounts receivable based on historical write-off trends and knowledge of specific circumstances that indicate collection of an account may be unlikely. Generally accounts receivable are considered past due after 30 days.

Interfund Transactions - Unsettled transactions between funds at year-end are recorded as due to or due from other funds.

Materials and Supplies Inventory - Materials and supplies consist primarily of items for maintenance of Division assets and are valued at the lower of average cost or fair market value.

Special Funds - In accordance with bond resolutions, agreements and laws, separate restricted funds have been established. These funds consist of cash and investments in pooled investments with restrictions externally imposed and legally enforceable, established by the City Council.

Capital Assets and Depreciation - Capital assets are stated at original cost, which includes both direct costs of construction or acquisition and indirect costs. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and betterments is capitalized. Assets are capitalized when costs exceed \$5,000 and the useful life exceeds one year.

Depreciation is recorded using the straight-line method at the beginning of the year and based on estimated economic lives of operating assets placed in service as follows:

Roads RR & bridges	7 – 20 years
Building	10 – 25 years
Machinery Equipment	10 – 25 years
Office and Fixture	5 – 20 years

Construction Work in Progress - Capitalizable costs incurred on projects which are not in service or ready for use are held in construction work in progress. When the asset is ready for service, related costs are transferred to capital assets. Upon determining that a project will be abandoned, the related costs are charged to expense.

Contributions - In accordance with GASB No. 33, Accounting and Financial Reporting for Nonexchange Transactions, grants and contributions are recorded as contribution revenue.

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. Based on historical information, 10% of compensated absences are considered short term.

Employees in the original policy accumulate sick leave at the rate of one day per month with no maximum accumulation specified. Employees receive 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.

Operating 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. Revenues are based on services rendered through the end of the year.

Non-Operating Revenues and Expenses - These are items that do not qualify as operating defined above.

Taxes - The City charges the Division Gross Earnings Tax at the rate of 8.0%. In addition, the Division pays business and occupation tax to the State at the rate of 1.8% on service revenues. The Division is exempt from payment of federal income tax.

Net Position - The Statement of Net Position reports all financial and capital resources. The difference between assets and liabilities is net position. There are three components of net position: net investment in capital assets, restricted and unrestricted.

Net investment in capital assets consists of capital assets less accumulated depreciation reduced by the outstanding balances of any bonds, loans or other borrowings that are attributable to the acquisition, construction, or improvements of those assets.

Net position components are restricted when constraints placed on net position use are either (1) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or (2) imposed by law through constitutional provisions or enabling legislation.

Unrestricted net position components are those that are not “net investment in capital assets” or “restricted”.

Shared Services - The Division receives certain services from other departments and agencies of the City including those normally considered to be general and administrative. The Division is charged for services received from other City departments and agencies.

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

On the Job Injury Reserve - Liabilities for claims are initially recorded when the expected loss is both probable and reasonably estimated. Subsequent adjustments to initial estimates are recorded as necessary based upon additional information developed in subsequent periods. Liabilities recorded for unasserted on the job injury claims are based on information currently available. Estimates of liabilities for on the job injury claims are undiscounted.

Significant Risks and Uncertainties - The Division is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include, but are not limited to, general economic conditions, fuel supply availability and rising fuel prices, weather and natural disaster-related disruptions, collective bargaining labor disputes, federal government regulations such as Federal Railroad Administration and Environmental Protection Agency or orders concerning the operation, maintenance and/or licensing of facilities, transportation of chemicals and other hazardous materials, acts of terrorism, war, or risk of war.

NOTE 3 CAPITAL ASSETS

A summary of the balances and changes in capital assets for 2015 and 2014 follows:

	Balance December 31, 2014	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2015
Land	\$ 160,456	\$ —	\$ —	\$ —	\$ 160,456
Road Property Plant	21,139,870	4,678,194	—	—	25,818,064
Building	3,896,587	19,693	—	—	3,916,280
Machinery Equipment	10,353,086	373,815	—	—	10,726,901
Office and Fixture	862,954	23,430	(201,129)	—	685,255
Total Capital Assets In Service	36,412,953	5,095,132	(201,129)	—	41,306,956
Less Accumulated Depreciation	(16,354,584)	(1,220,882)	201,129	—	(17,374,337)
	20,058,369	3,874,250	—	—	23,932,619
Construction Work In Progress	1,000,440	4,910,461	—	(5,095,132)	815,769
Net Capital Assets	\$ 21,058,809	\$ 8,784,711	\$ —	\$ (5,095,132)	\$ 24,748,388

	Balance December 31, 2013	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2014
Land	\$ 160,456	\$ —	\$ —	\$ —	\$ 160,456
Road Property Plant	17,433,535	3,706,335	—	—	21,139,870
Building	3,789,678	106,909	—	—	3,896,587
Machinery Equipment	10,353,086	—	—	—	10,353,086
Office and Fixture	862,954	—	—	—	862,954
Total Capital Assets In Service	32,599,709	3,813,244	—	—	36,412,953
Less Accumulated Depreciation	(15,285,319)	(1,069,265)	—	—	(16,354,584)
	17,314,390	2,743,979	—	—	20,058,369
Construction Work In Progress	701,285	4,112,398	—	(3,813,243)	1,000,440
Net Capital Assets	\$ 18,015,675	\$ 6,856,377	\$ —	\$ (3,813,243)	\$ 21,058,809

NOTE 4 LONG-TERM DEBT

Long-term debt activities for 2015 and 2014 were as follows:

	Balance December 31, 2014	Additions	Reductions	Balance December 31, 2015	Due Within One Year
Revenue Bonds	\$ 548,332	\$ —	\$ 235,569	\$ 312,763	\$ 248,525
Department of Transportation State Loans	4,487,475	2,019,195	317,440	6,189,230	697,166
Total Long-Term Debt	\$ 5,035,807	\$ 2,019,195	\$ 553,009	\$ 6,501,993	\$ 945,691

	Balance December 31, 2013	Additions	Reductions	Balance December 31, 2014	Due Within One Year
Revenue Bonds	\$ 771,620	\$ —	\$ 223,288	\$ 548,332	\$ 235,569
Department of Transportation State Loans	2,447,201	2,270,848	230,574	4,487,475	317,437
Total Long-Term Debt	\$ 3,218,821	\$ 2,270,848	\$ 453,862	\$ 5,035,807	\$ 553,006

Senior Lien Bond: City Council Substitute Ordinance No. 27545, passed in November 2006, authorized the issuance of a Senior Lien Revenue Bond 2006 in the amount of \$2,000,000 to provide financing for capital projects included in the approved 2007-2008 Biennium budget for the Rail System. This Bond bears interest at the rate of 5.39% per annum (computed on the basis of a 360-day year of twelve 30-day months), with a maturity date of January 1, 2017. Equal installment payments of \$65,104 representing principal and interest on this Bond are payable quarterly on the first day of each January, April, July and October, commencing April 1, 2007, up to and including the Maturity Date of the Bond.

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

	Principal	Interest
2016	\$ 248,525	\$ 11,891
2017	\$ 64,238	\$ 866
	\$ 312,763	\$ 12,757

JUNIOR LIEN DEBT

Washington State Department of Transportation Loans (WADOT)	2015	2014
2009 WADOT loan for locomotive idling improvement, with 0% interest, due in yearly installments of \$1,759 from 2010 through 2024.	\$ 15,831	\$ 17,590
2009 WADOT loan for locomotive servicing facility upgrades, with 0% interest, due in yearly installments of \$16,630 from 2011 through 2025.	166,301	182,932
2011 WADOT loan for locomotive repower, with 0% interest, due in yearly installments of \$45,000 from 2013 through 2022.	315,000	360,000
2012 WADOT loan for Tacoma Rail Annie Tracks 1&2 Rail Relay, with 0% interest, due in yearly installments of \$61,200 from 2013 through 2022.	428,400	489,600
2012 WADOT loan for Yard Tracks 2,3 & 4, with 0% interest, due in yearly installments of \$34,859 from 2013 through 2022.	244,014	278,873

JUNIOR LIEN DEBT (CONTINUED)	2015	2014
2013 WADOT loan for East 11th Street Crossing, with 0% interest, due in yearly installments of \$34,732 from 2014 through 2023.	277,856	312,588
2013 WADOT loan for Yard Tracks 5 & 6, with 0% interest, due in yearly installments of \$36,394 from 2014 through 2023.	291,150	327,544
2013 WADOT loan for Yard Tracks 8 & 9, with 0% interest, due in yearly installments of \$61,863 from 2015 through 2024.	556,763	618,626
2013 WADOT loan for Port Pass West, with 0% interest, due in yearly installments of \$25,000 from 2015 through 2024.	224,997	250,000
2013 WADOT loan for N. Intermodal Yard lead track, with 0% interest, due in yearly installments of \$36,639 from 2016 through 2025.	366,387	366,387
2013 WADOT loan for East Loop 17th St, with 0% interest, due in yearly installments of \$77,307 from 2016 through 2025.	773,070	773,070
2013 WADOT loan for Taylor Way Track Rehabilitation, with 0% interest, due in yearly installments of \$110,506 from 2016 through 2025.	1,105,058	510,265
2013 WADOT loan for West Loop, with 0% interest, due in yearly installments of \$51,577 from 2016 through 2025.	515,770	—
2014 WADOT loan for SR509 Track Improvements, with 0% interest, due in yearly installments of \$103,701 from 2016 through 2025.	908,632	—
Subtotal Junior Lien Debt	6,191,244	4,489,489
Less Current Portion of Debt	(697,166)	(317,437)
Long-term Portion of Junior Lien Debt	\$ 5,494,078	4,172,052

Scheduled principal maturities on junior lien debts and interest payments are as follows:

	Principal	Interest
2016	\$ 697,166	\$ —
2017	697,166	\$ —
2018	697,166	—
2019	697,166	—
2020	697,166	\$ —
2021-2025	2,705,414	—
	\$ 6,191,244	\$ —

Tacoma Rail's revenue bonds are secured by the net revenue of Tacoma Rail and all cash and investments held in the bond fund. The bonds as well as junior liens are subject to certain financial and non-financial covenants.

NOTE 5 SIGNIFICANT CUSTOMER

Tacoma Rail's predominate sources of revenue are Union Pacific (UP) and Burlington Northern Santa Fe (BNSF). Revenue from UP and BNSF represented 26% and 47% of total revenues, respectively, in 2015. Revenue in 2014 was 26% and 48%, respectively. Accounts receivable from UP and BNSF in 2015 represented 23% and 48% of total customer accounts receivable, respectively. Accounts receivable in 2014 was 21% and 45%, respectively.

NOTE 6 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.

Tacoma Rail pays the Fleet Services Fund for the use of the vehicles and equipment to cover fleet operating expenses. Payments made by Tacoma Rail in 2015 and 2014 were \$543,305 and \$502,723, respectively.

NOTE 7 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 Rail and other divisions within the Department for certain losses arising from personal and property damage claims by third parties. The major risks to Tacoma Rail 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 Rail is required to make payments to the Self-Insurance Fund to cover claims incurred by Tacoma Rail and administrative expenses of the Fund. Tacoma Rail's premium payments totaled \$100,000 in 2015 and \$50,004 in 2014. Assets in the Self-Insurance Fund total \$6.9 million which exceeds accrued and incurred but not reported (IBNR) liabilities. Equity in the Self-Insurance Fund is transferred to the appropriate operating divisions in accordance with GASB 10. Management believes Tacoma Rail's investment in the Self-Insurance Fund is more than adequate to settle all its known or estimated claims.

The City purchased a \$15 million Fiduciary Liability Policy with a \$100,000 deductible that provides for wrongful acts arising out of the administration of the City's employee benefit programs and a Crime policy with a \$1 million limit and \$75,000 deductible for employee dishonesty and for fraudulent or dishonest act by employees against the City for loss of money, securities and property.

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 property within buildings and \$10,000 per vehicle. There is a self-insured retention of \$1.5 million for general liability. The public official liability policy has a \$200,000 deductible. The Department's total liability limit is \$60 million any one occurrence and \$60 million annual aggregate. The general government general liability and public official liability policies provide \$15 million of excess coverage with \$3 million retention. The City has a policy to cover extraordinary worker's compensation claims with a statutory limit and a self-insured retention of \$1 million per occurrence and an additional \$250,000 for each 12 month policy period.

NOTE 8 PENSION PLAN

Employees of Tacoma Rail are members of the United States Railroad Retirement System, in lieu of participating in Social Security and Tacoma Employees' Retirement System. The Railroad Retirement System is a payroll-based system. In 2015 and 2014, Tacoma Rail contributed \$2,145,824 and \$1,859,639 respectively, per structures set forth by the United States Railroad Retirement Board shown as follows:

Earnings Base		
	2015	2014
Employer Tier I	\$ 118,500	\$ 117,000
Employer Tier II	88,200	87,000
Employer Medicare	No Limit	No Limit

Tax Rate		
	2015	2014
Employer Tier I	6.20%	6.20%
Employer Tier II	13.10%	12.60%
Employer Medicare	1.45%	1.45%

Information was unavailable to determine if an actuarial liability exists for the City, but the entire Federal system has an unfunded actuarial liability of \$51.7 billion as of December 31, 2013. There is currently no schedule to amortize the unfunded liability and the system is currently functioning on a pay-as-you-go basis. Rates are determined based on actuarial valuations, which occur every three years. The City's obligation is to pay, in full, the payroll withholdings to the system.

NOTE 9 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 active employees and retirees rather than based on the claims experience of retirees only. This difference is a benefit to the retirees, since health claims costs generally increase with age. GAAP 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. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and are subject to continual revision as results are compared to past expectation and new estimates are made about the future.

Funding Policy - The City uses pay as you go funding; contributions to a separate trust are not required.

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 (3.75%).

The Actuarial Accrued Liability (AAL) is the portion of the present value of benefits attributed to past service only. The portion attributed to future employee service is excluded.

For inactive employees, the AAL is equal to the present value of benefits. For active employees, the actuarial present value of the projected benefits of each individual 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 attributed to service between entry age and the valuation date is the actuarial accrued liability.

The Normal Cost is that portion of the City provided benefit attributable to employee service in the current year.

The Annual Required Contribution (ARC) is the amount the City is 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 (UAAL) on a closed basis of 30 years, beginning January 1, 2007. The amortization period for 2015 is 22 years.

The ARC represents an accounting expense, but the City is not required to contribute the ARC to a separate trust. If the City does not set aside funds equal to the ARC (less current year benefit payments) each year, then the ARC (less benefit payments) will accumulate as a non-current liability (Net OPEB Obligation) on the statements of net position. The City has a Net OPEB Obligation as of December 31, 2015 as the City has not set aside funds for OPEB.

Excise Tax For High Cost or “Cadillac” Health Plans in 2018 and Beyond – An excise tax for high cost health coverage or “Cadillac” health plans was included in the Affordable Care Act (ACA) passed into law in March 2010. The provision levies a 40% tax on the value of health plan costs that exceed certain thresholds for single coverage or family coverage. If, between 2010 and 2018, the cost of health care insurance rises more than 55%, the threshold for the excise tax will be adjusted.

The City believes that the current provisions of ACA should be reflected in the projection of benefits and therefore, the value of the excise tax is included in the valuation. It is assumed that there will be no changes to the current law and that there will be no changes in plan design to help mitigate the impact of the tax.

GASB Statement No. 45 indicates that the projection of benefits should include all benefits to be provided to retirees in accordance with the current “substantive” plan. The substantive plan refers to the plan terms as understood by the employer and plan members at the time of the valuation. For this reason, the City believes that the current provisions of PPACA should be reflected in the projection of benefits and therefore, the value of the excise tax is included in this valuation. It is assumed that there will be no changes to the current law and that there will be no changes in plan design to help mitigate the impact of the tax.

Summary of Changes – As of the January 1, 2015 valuation the total AAL was \$208,814,312, 20% lower than expected primarily due to clarification in spouse benefits, medical costs, demographic experience and a change to the assumption for future medical trends.

The following table is a summary of valuation results with a comparison to the results from the last valuation.

	<u>January 1, 2013</u>	<u>January 1, 2015</u>
Total membership:		
Active employees	3,335	3,404
Terminated vested employees	394	442
Retired employees & dependents	846	744
Total	4,575	4,590
Annual Benefit Payments	\$ 9,887,335	\$ 8,963,089
Discount rate	3.75%	3.75%
Present Value of Benefits (PVB)	\$ 326,742,538	\$ 262,184,195
Actuarial Accrued Liability (AAL)	\$ 251,839,846	\$ 208,814,312
Assets	\$ -	\$ -
Unfunded Actuarial Accrued Liability (UAAL)	\$ 251,839,846	\$ 208,814,312
Normal Cost	\$ 5,484,587	\$ 3,832,131
Annual Required Contribution (ARC)	\$ 20,058,760	\$ 16,966,964

The following table shows the total value of the benefits provided, the member paid premiums and the City paid benefits as of January 1, 2015.

Value of Subsidy at 3.75% Interest Rate	Total Value of Benefits	Member Paid Premiums	City Paid Benefits
Present Value of Benefits (PVB)	\$ 420,832,932	\$ 158,648,737	\$ 262,184,195
Actuarial Accrued Liability (AAL)	\$ 291,228,295	\$ 82,413,983	\$ 208,814,312
Normal Cost	\$ 9,501,758	\$ 5,669,627	\$ 3,832,131
Annual Benefit Payments	\$ 12,325,369	\$ 3,362,280	\$ 8,963,089

The following table shows the calculation of the Annual Required Contribution and Net OPEB Obligation for the City and for the Division as of December 31, 2015.

	City	Division
Determination of Annual Required Contribution		
Normal Cost at Year-end	\$ 3,832,131	\$ 285,047
Amortization of UAAL	13,134,833	128,541
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 413,588
Determination of Net OPEB Obligation		
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 413,588
Interest on prior year Net OPEB Obligation	2,480,183	13,615
Adjustments to ARC	(3,492,760)	(16,089)
Annual OPEB Cost	15,954,387	411,114
Actual benefits paid	(8,963,089)	(78,549)
Increase in Net OPEB Obligation	6,991,298	332,565
Net OPEB Obligation - beginning of year	66,138,206	363,064
Net OPEB Obligation - end of year	\$ 73,129,504	\$ 695,629

The Division has included the liability in other long-term liabilities on the statement of Net Position.

Funded Status and Funding Progress - The following table shows the annual OPEB cost and net OPEB obligation for three years. This table is based upon a 3.75% interest rate.

	Annual OPEB Cost		Benefits Paid		Net OPEB	
Year Ended	City	Division	City	Division	City	Division
12/31/2013	\$19,528,767	\$ 153,838	\$ 9,887,334	\$ 74,972	\$ 56,110,801	\$ 261,551
12/31/2014	\$19,319,944	\$ 153,125	\$ 9,292,539	\$ 51,612	\$ 66,138,206	\$ 363,064
12/31/2015	\$15,954,387	\$ 411,114	\$ 8,963,089	\$ 78,549	\$ 73,129,502	\$ 695,629

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 the 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 for non-LEOFF 1 groups. For LEOFF 1, the UAAL is amortized as a level dollar amount. The amortization period was 30 years in 2007 and the remaining is now 22 years.

Actuarial Methods and Significant Actuarial Assumptions:

Valuation Date	January 1, 2015												
Census Date	January 1, 2015												
Actuarial Cost Method:	Entry Age												
Amortization Method:	Combination of level percentage and level dollar amount, see note above.												
Remaining Amortization Period:	22 years, closed												
Demographic Assumptions:	Demographic assumptions regarding retirement, disability, and turnover are based upon pension valuations for the various pension plans.												
Actuarial Assumptions:													
Discount Rate	3.75% for pay-as-you-go funding												
Medical Cost Trend	<table> <tr><td>2015</td><td>6.9%</td></tr> <tr><td>2016</td><td>6.6%</td></tr> <tr><td>2017</td><td>5.9%</td></tr> <tr><td>2020</td><td>5.5%</td></tr> <tr><td>2030</td><td>5.9%</td></tr> <tr><td>2040</td><td>5.7%</td></tr> </table>	2015	6.9%	2016	6.6%	2017	5.9%	2020	5.5%	2030	5.9%	2040	5.7%
2015	6.9%												
2016	6.6%												
2017	5.9%												
2020	5.5%												
2030	5.9%												
2040	5.7%												

The medical cost rate is assumed to continue grading downward until achieving the ultimate rate of 4.8% in 2071 and beyond. These trend rates assume that, over time, deductibles and out-of-pocket maximums will be periodically increased as medical trends increase. The trends above do not reflect increases in costs due to the excise tax.

Economic Assumptions-Discount Rate (Liabilities)	3.75%
Demographic Assumptions	<p>Eligibility:</p> <p>Disability - Five years of service are required for non-service connected disability.</p> <p>Retirement - TERS members are eligible for retiree medical benefits after becoming eligible for service retirement pension benefits (either reduced or full pension benefits):</p> <ul style="list-style-type: none"> • Age 55 with 10 years of service • Age 40 with 20 years of service

NOTE 10 COMMITMENTS AND CONTINGENCIES

Link Petroleum Project Customer Deposit And Refund Agreement - A contractual agreement was entered in 2009 between Tacoma Rail and Link Petroleum, Inc. Link Petroleum agreed to advance Tacoma Rail \$75,000 for track improvements on Tacoma Rail's property to efficiently and safely handle shipments leading to this customer's service facility. In return, Tacoma Rail agreed to refund the advance to the customer at a rate of \$150 per carload for each of the first 500 carloads handled at the facility, or through December 31, 2015, whichever event first occurs. As of December 31, 2015, the remaining deposit is \$45,900.

General Legal Matters - Tacoma Rail 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 Tacoma Rail's financial position beyond amounts already accrued as of December 31, 2015.

Tacoma Rail Operation of City of Tacoma, Department of Public Works ("Public Works"), Mountain Division - Public Works owns approximately 142 miles of track, called Mountain Division, that connects to Tacoma Rail track in Tacoma, Washington. Tacoma Rail is under contract with Public Works to perform as its operator through 2016. The agreement states that Public Works would fund Tacoma Rail for any operations on the Mountain Division.



3628 S. 35th St. / Tacoma, WA 98409 / 253.502.8000 / MyTPU.org