
ANNUAL

TACOMA POWER

2017

**FINANCIAL
REPORT**



Public Utility Board

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DEPARTMENT OF PUBLIC UTILITIES

CITY OF TACOMA

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES

TACOMA POWER

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FINANCIAL DATA

Report of Independent Auditors

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

Report on the Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Department of Public Utilities, Power Division (the Division), which comprise the statements of net position as of December 31, 2017 and 2016, 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, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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 City of Tacoma, Department of Public Utilities, Power Division as of December 31, 2017 and 2016, and the results of its operations and 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, schedule of proportionate share of net pension liability, and schedule of employer contributions, as listed in the table of contents, 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 on pages 46 through 62 and the superintendent's report on pages 63 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 financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated April 18, 2018, on our consideration of the City of Tacoma, Department of Public Utilities, Power Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.



Tacoma, Washington
April 18, 2018

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis of Tacoma Power's (Utility) financial performance provides an overview of the financial activities for the years ended December 31, 2017, 2016 and 2015. 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, 2017 and 2016, 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.

Financial Highlights

- Tacoma Power reported an increase in total net position of \$8.2 million (307.6%) in 2017, compared to a decrease of \$3.9 million (150.6%) in 2016.
- Operating revenues increased \$27.7 million (6.6%) in 2017. Operating revenues in 2016 increased \$8.0 million (1.9%).
- Utility Plant in Service increased \$51.6 million (2.6%) in 2017 and \$143.1 million (7.7%) in 2016.
- Construction work in progress increased \$5.7 million (21.8%) in 2017 and decreased \$61.5 million (70.0%) in 2016.

Overview of Financial Statements

Tacoma Power reported net operating income of \$43.1, \$30.4 and \$34.1 million in 2017, 2016 and 2015 respectively. Operating revenues increased \$27.7 million during 2017 and operating expenses increased \$15.0 million. For 2016, operating revenues increased \$8.0 million and operating expenses increased \$11.6 million compared to 2015. Tacoma Power reported an increase in net position of \$8.2 million in 2017 compared to a decrease of \$3.9 million in 2016 and a decrease of \$1.6 million in 2015.

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

OPERATING RESULTS

(in thousands)

<u>Category</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>17/16 Increase (Decrease)</u>	<u>16/15 Increase (Decrease)</u>
Operating Revenues	\$ 446,343	\$ 418,614	\$ 410,626	\$ 27,729	\$ 7,988
Operating Expenses	403,210	388,220	376,576	14,990	11,644
Net Operating Income	43,133	30,394	34,050	12,739	(3,656)
Net Non-Operating Expenses	(13,460)	(12,716)	(20,036)	(744)	7,320
Capital Contributions	8,956	5,162	5,708	3,794	(546)
BABs and CREBs subsidies	3,688	3,684	3,676	4	8
Transfers Out	(34,142)	(30,462)	(24,969)	(3,680)	(5,493)
Change in Net Position (Net Income)	\$ 8,175	\$ (3,938)	\$ (1,571)	\$ 12,113	\$ (2,367)

MEGAWATT-HOURS BILLED

(in thousands)

<u>Type of Customer</u>	<u>2017</u>	<u>2016*</u>	<u>2015</u>	<u>17/16 Increase (Decrease)</u>	<u>16/15 Increase (Decrease)</u>
Residential	1,975	1,856	1,801	119	55
Commercial/General/Industrial	2,777	2,772	2,791	5	(19)
Wholesale	2,836	2,731	1,918	105	813
Total	7,588	7,359	6,510	229	849

*The 2016 type of customer has been updated to reflect the information in the Gross Generation report.

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.

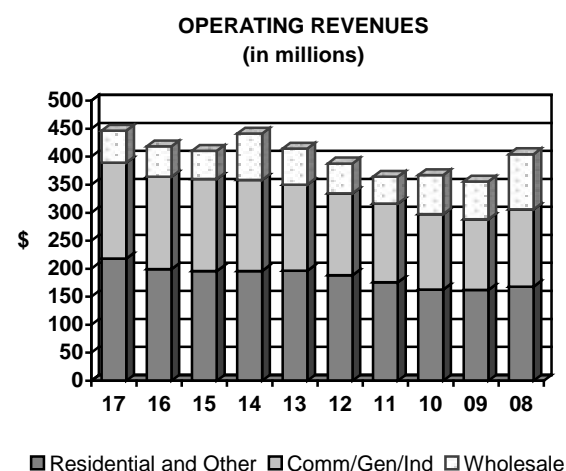
Statements of Net Position (in thousands)

<u>Description</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>17/16 Increase (Decrease)</u>	<u>16/15 Increase (Decrease)</u>
Net Utility and Non-Utility Plant	\$ 1,037,958	\$ 1,033,591	\$ 1,002,993	\$ 4,367	\$ 30,598
Current Assets, Other Assets and Special Funds	357,561	384,884	392,482	(27,323)	(7,598)
Total Assets	1,395,519	1,418,475	1,395,475	(22,956)	23,000
Deferred Outflows	38,427	39,469	10,977	(1,042)	28,492
Total Assets and Deferred Outflows	\$ 1,433,946	\$ 1,457,944	\$ 1,406,452	\$ (23,998)	\$ 51,492
Net Position:					
Net Investment in Capital					
Assets	\$ 613,307	\$ 581,629	\$ 594,626	\$ 31,678	\$ (12,997)
Restricted	14,032	15,225	21,028	(1,193)	(5,803)
Unrestricted	202,832	225,142	210,279	(22,310)	14,863
Total Net Position	830,171	821,996	825,933	8,175	(3,937)
Long-Term Debt	417,800	457,602	441,928	(39,802)	15,674
Other Liabilities	130,070	128,058	86,555	2,012	41,503
Total Liabilities	547,870	585,660	528,483	(37,790)	57,177
Deferred Inflows	55,905	50,288	52,036	5,617	(1,748)
Total Net Position, Liabilities and Deferred Inflows	\$ 1,433,946	\$ 1,457,944	\$ 1,406,452	\$ (23,998)	\$ 51,492

Revenues

2017 Compared to 2016

Operating revenues totaled \$446.3 million in 2017 compared to \$418.6 million in 2016, an increase of \$27.7 million (6.6%). Revenues from residential customers increased \$15.5 million (10.1%). There was a 5.9% rate increase effective April 16, 2017 coupled with an increase in consumption of 121,000 in MWh billed. Revenues from commercial, general, and industrial customers increased \$6.3 million (3.8%) primarily due to the rate increase effective April 16, 2017.



Wholesale revenues increased \$2.6 million (4.7%) as compared to 2016. The majority of the increase was due to higher volume.

In 2017 residential sales accounted for 43.2% of electric revenues, commercial and industrial revenues accounted for 42.6% and wholesale power revenues accounted for 14.2%.

2016 Compared to 2015

Operating revenues totaled \$418.6 million in 2016 compared to \$410.6 million in 2015, an increase of \$8.0 million (1.9%). Revenues from residential customers increased \$4.9 million (3.3%). Wholesale revenues increased \$4.1 million (8.2%) as compared to 2015. The majority of the increase was due to higher volume. Streamflows were up 116% over 2015, and were 113% of average for 2016. Generation was up 27%, while purchases were down, which left more power to sell.

In 2016 residential sales accounted for 41.4% of electric revenues, commercial and industrial revenues accounted for 44.0% and wholesale power revenues accounted for 14.6%.

Expenses

2017 Compared to 2016

Total operating expenses increased \$15.0 million or 3.9% compared to 2016.

Purchased power increased \$9.0 million (7.1%). In 2016 Energy Conservation Agreement (ECA) credits were received in the amount of \$7.1 million. In 2017 only \$1.3 million in credits were received resulting in an increase of purchased power expense of \$5.8 million. The ECA credits are available in 2 year allotments beginning October 1 of odd years. In even years more is received than odd years. Other portfolio purchases also increased \$2.7 million to support the increased load and wholesale sales.

Generation expenses increased \$3.8 million (20.0%). Fish operations costs have had a sizable increase in 2017 as a result of operating two newly constructed fish hatcheries and expanded operations at three fish collection facilities. Also associated with the fish facilities are new studies to determine performance and identify necessary improvements.

Other expenses increased \$1.4 million (7.5%) primarily due an increase of the amortization of deferred conservation costs. These costs are amortized over a 10 year period and year 8 of 10 was added to the 2017 schedule.

Maintenance expenses decreased \$2.3 million (7.0%). Extraordinary maintenance projects were completed in 2016 that did not carry over into 2017 accounted for \$1.5 million of the change. A decrease of \$0.8 million was due to the discontinuation of contributions to the Fleet Internal Service Fund during 2017. An analysis of future purchase needs is currently underway.

Administration and general expenses increased \$2.5 million (6.2%). These were primarily due to an increase in assessments of \$1.2 million, claims of \$0.9 million, and bad debt write-off's of \$0.7 million.

2016 Compared to 2015

Total operating expenses increased \$11.6 million or 3.1% compared to 2015.

Pension expense increased \$10.0 million in 2016. This expense was allocated across the Power sections as follows: Admin & General \$2.9 million, Distribution \$2.9 million, Maintenance \$1.4 million, Generation \$1.0 million, Telecommunications \$0.8 million, Other \$0.7 million, and Transmission \$0.4 million.

Purchased power increased \$0.5 million (0.4%). The increase was primarily due to increased contract costs and renewable energy credits purchased offset by increased credits and decreased purchased power.

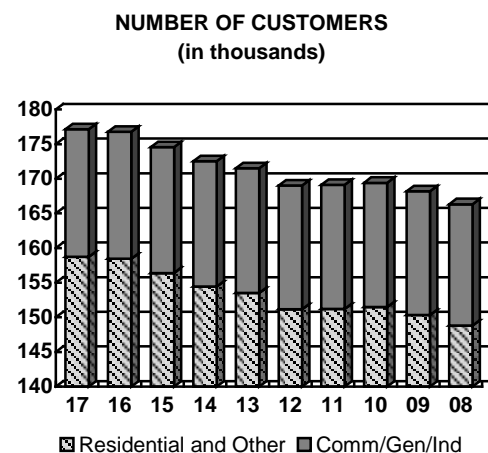
Transmission expenses increased \$6.1 million (28.0%) and distribution expenses increased \$10.3 million (101.5%). In 2015 Tacoma Power conducted a review of expenses and determined that a large amount of costs that were assigned to administration and general expense should be reclassified to non-administrative groups. The increases in transmission and distribution expenses are primarily due to reclassifying these expenses effective January 1, 2016.

Generation expenses increased \$5.1 million (35.7%), maintenance expenses increased \$4.6 million (16.7%) and other production expenses increased \$3.7 million (24.3%) primarily due to the reclassification of expenses previously mentioned.

Administration and general expenses decreased \$17.5 million (29.9%) primarily due to the reclassification of expenses previously mentioned.

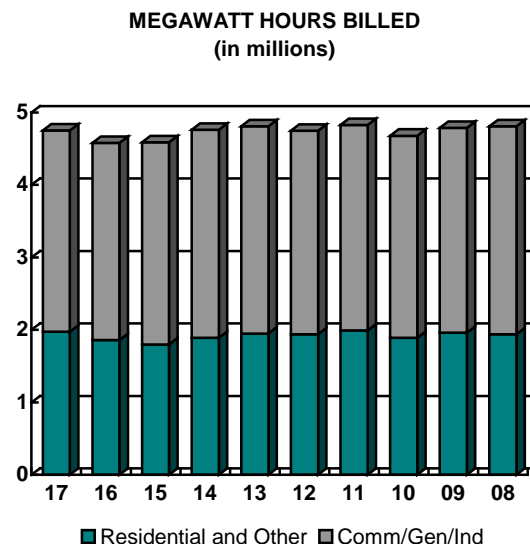
Customer Counts

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 2017 is 177,153 compared to 176,784 in 2016 and 174,562 in 2015.



Megawatt-hours Billed

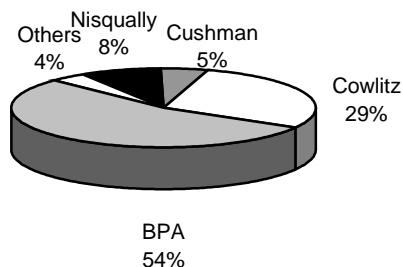
Megawatt-hours billed to residential and other customers increased 6.4% in 2017, while commercial / general / industrial billings increased 1.9%. Wholesale power billed in 2017 was 2,835,719 megawatt-hours compared to 2,731,076 in 2016, an increase of 104,643 megawatt-hours or 3.8%. During 2017 hydro generation decreased 6,711 megawatt-hours compared to the previous year. Streamflows into Tacoma Power's system were 115% of average in 2017 compared to 113% of average in 2016.



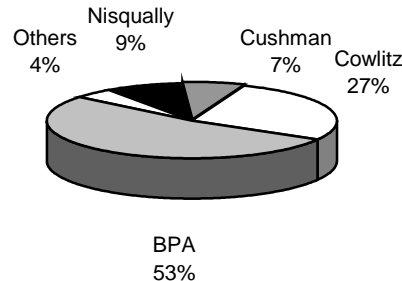
Sources of Power

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 - 2017**

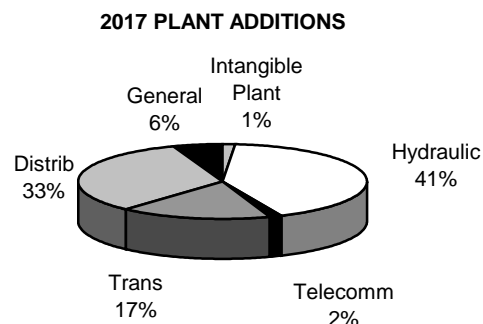
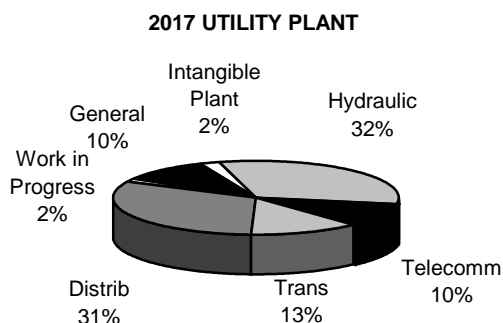


**Megawatt Hours Generated/
Purchased - 2016**



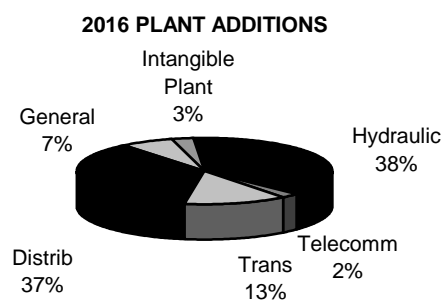
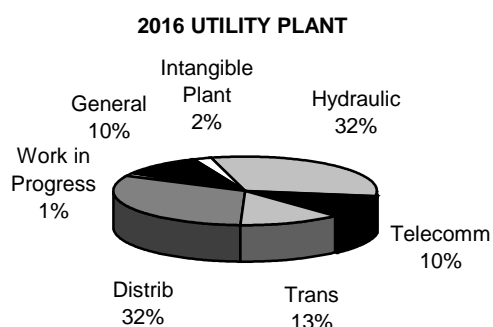
Utility Plant and Plant Additions

Tacoma Power has \$2.1 billion invested in its utility plant assets on a cost basis. The largest portion is for the generation (hydroelectric) business unit followed by the combined distribution and transmission business unit. The following graphs show the allocation of plant additions and total investment in plant.



Additions to Hydraulic plant in 2017 were \$22.8 million, which included the Cowlitz license implementation and the hydro governor and exciter replacement program. Distribution plant additions were \$17.9 million, which included addition and replacement programs for new services, pole and cable, road related additions and replacements, distribution transformers and meters and devices. Transmission plant additions were \$9.2 million, which included Potlatch system ring bus, substation additions and replacements, Henderson Bay tower replacement, Pearl Cushman upgrade and protection and controls additions and replacements. General plant additions were \$3.1 million, which included the auditorium upgrade, communication tower upgrades, and the wellness center.

Interest during construction for prior years was applied to Hydraulic plant for \$9.1 million and Transmission plant for \$1.1 million.



Additions to Hydraulic plant in 2016 were \$89.2 million, which included the Cowlitz Falls downstream fish passage and the Cushman license implementation. Distribution plant additions were \$27.2 million, which included addition and replacement programs for new services, pole replacements, and road related additions and replacements.

Transmission plant additions were \$16.5 million, which included system reliability improvements and substation additions and replacements.

The following table summarizes Tacoma Power's capital assets, net of accumulated depreciation, for the years ended December 31, 2017 through 2015.

Capital Assets, Net of Accumulated Depreciation
(in thousands)

<u>Net Utility Plant</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>17/16 Increase (Decrease)</u>	<u>16/15 Increase (Decrease)</u>
Intangible Plant	\$ 31,448	\$ 32,030	\$ 29,404	\$ (582)	\$ 2,626
Hydraulic Plant	454,498	441,163	359,992	13,335	81,171
Transmission Facilities	125,610	125,357	118,765	253	6,592
Distribution Facilities	286,735	290,766	284,826	(4,031)	5,940
General Plant	73,509	77,081	78,190	(3,572)	(1,109)
Telecommunications Plant	33,819	40,600	43,682	(6,781)	(3,082)
Construction Work in Progress	32,157	26,412	87,952	5,745	(61,540)
Total Net Utility Plant	<u>\$ 1,037,776</u>	<u>\$ 1,033,409</u>	<u>\$ 1,002,811</u>	<u>\$ 4,367</u>	<u>\$ 30,598</u>

Additional information on Tacoma Power's capital assets can be found in Note 4 of the financial statements and also in the supplementary Statistical Data.

Debt Administration

At December 31, 2017 Tacoma Power had outstanding revenue bonds of \$404.6 million, an increase of \$33.5 million compared to 2016. Tacoma Power issued \$70.6 million of Electric System Revenue Bonds, Series 2017 in September 2017. The proceeds of the issuance and operating funds were used to pay down \$80 million of the Wells Fargo line of credit. In October 2017 Tacoma Power defeased \$24.3 million of 2013 Series A Electric System Revenue and Refunding Bonds.

No draws were taken in 2017 on the line of credit agreement with Wells Fargo. No draws have been taken on the 3-year line of credit agreement with Key Bank.

At December 31, 2016 Tacoma Power had outstanding revenue bonds of \$371.1 million, a decrease of \$14.7 million compared to 2015. No new revenue bonds were issued in 2016. On March 10, 2016 and August 16, 2016 Tacoma Power took draws of \$15 million respectively on the line of credit agreement with Wells Fargo bringing the total drawn to \$80.3 million. No draws have been taken on the 3-year line of credit agreement with Key Bank.

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.

All bonds are rated AA by Standard and Poor's and AA- by Fitch, Inc. Bonds prior to 2017 are rated Aa3 by Moody's Investors Service.

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 2017, principal and interest were covered 3.43 times compared to 2.94 times in 2016 and 2.54 times in 2015.

Summary

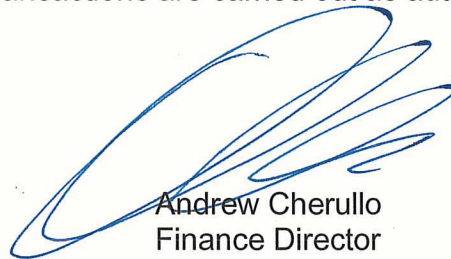
The management of the Finance Department of the City of Tacoma is responsible for preparing the accompanying financial statements and for their integrity. We prepared the financial statements according to GAAP in the United States of America, and they fairly portray Tacoma Power's financial position 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 independently 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.



Linda McCrea
Interim Director of Utilities/CEO



Andrew Cherullo
Finance Director

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER
STATEMENTS OF NET POSITION

ASSETS AND DEFERRED OUTFLOWS	DECEMBER 31,	
	2017	2016
UTILITY PLANT		
In Service, at Original Cost	\$2,055,844,322	\$2,004,204,782
Less - Accumulated Depreciation	(1,050,225,152)	(997,207,625)
Total	1,005,619,170	1,006,997,157
Construction Work in Progress	32,156,858	26,411,907
Net Utility Plant	1,037,776,028	1,033,409,064
NON-UTILITY PROPERTY	182,051	182,051
SPECIAL FUNDS		
Construction Funds	6,849	13,387,867
Debt Service Funds	21,208,267	22,180,111
Special Bond Reserve Funds	4,967,361	4,981,885
Wynoochee Reserve Funds	2,578,307	2,557,943
Total Special Funds	28,760,784	43,107,806
CURRENT ASSETS		
Operating Funds Cash and Equity in		
Pooled Investments	195,175,918	214,474,287
Accounts Receivable	34,993,074	30,021,427
(Net of Allowance for Doubtful Accounts of \$3,093,046 in 2017 and \$2,174,162 in 2016)		
Accrued Unbilled Revenue	30,701,425	28,587,295
Materials and Supplies	6,987,004	7,468,481
Interfund Receivables	1,820,401	2,226,220
Prepayments and Other	6,808,178	6,384,609
Total Current Assets	276,486,000	289,162,319
OTHER ASSETS		
Regulatory Asset - Conservation		
(Net of Amortization of \$32,641,091 in 2017 and \$25,121,809 in 2016)		
	49,689,386	50,071,005
Conservation Loans Receivable	2,625,268	2,542,470
Total Other Assets	52,314,654	52,613,475
Total Assets	1,395,519,517	1,418,474,715
DEFERRED OUTFLOWS OF RESOURCES		
Deferred Outflow for Pensions.....	38,426,742	39,469,454
Total Deferred Outflows	38,426,742	39,469,454
TOTAL ASSETS AND DEFERRED OUTFLOWS	<u>\$1,433,946,259</u>	<u>\$1,457,944,169</u>

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

NET POSITION, LIABILITIES AND DEFERRED INFLOWS	DECEMBER 31,	
	2017	2016
NET POSITION		
Net Investment in Capital Assets	\$613,307,151	\$581,629,142
Restricted for:		
Wynoochee Reserve Funds	2,578,307	2,557,943
Debt Service Funds	11,453,009	12,667,207
Unrestricted	202,832,206	225,141,401
Total Net Position	<u>830,170,673</u>	<u>821,995,693</u>
LONG-TERM DEBT		
Revenue Bonds	417,800,137	377,351,726
Revolving Line of Credit	-	80,250,000
Total Long-Term Debt	<u>417,800,137</u>	<u>457,601,726</u>
CURRENT LIABILITIES		
Current Portion of Long-Term Debt	11,825,000	12,730,000
Taxes and Other Payables	28,147,416	27,457,682
Purchased Power Payable	13,219,076	12,639,142
Salaries, Wages and Compensated Absences Payable ..	3,036,398	2,912,713
Interest Payable	9,755,258	9,512,905
Customers' Deposits	2,791,006	2,772,395
Interfund Payables	67,461	2,140,909
Total Current Liabilities	<u>68,841,615</u>	<u>70,165,746</u>
LONG-TERM LIABILITIES		
Long Term Accrued Compensated Absences	9,398,115	9,681,941
Net Pension Liability	36,687,245	34,177,293
Other Long Term Liabilities	15,143,610	14,033,787
Total Long Term Liabilities	<u>61,228,970</u>	<u>57,893,021</u>
Total Liabilities	<u>547,870,722</u>	<u>585,660,493</u>
DEFERRED INFLOWS OF RESOURCES		
Deferred Inflow for Pensions	7,904,864	2,287,983
Rate Stabilization	48,000,000	48,000,000
Total Deferred Inflows	<u>55,904,864</u>	<u>50,287,983</u>
TOTAL NET POSITION, LIABILITIES AND DEFERRED INFLOWS	<u><u>\$1,433,946,259</u></u>	<u><u>\$1,457,944,169</u></u>

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	YEAR ENDED DECEMBER 31,	
	2017	2016
OPERATING REVENUES		
Sales of Electric Energy	\$401,631,506	\$374,249,290
Other Operating Revenue	18,192,038	17,690,192
Click! Network Operating Revenue	26,519,861	26,674,906
Total Operating Revenue	446,343,405	418,614,388
OPERATING EXPENSES		
Operations		
Purchased and Interchanged Power	135,822,340	126,835,928
Generation	23,118,677	19,270,201
Transmission	27,562,757	28,075,318
Distribution	19,675,524	20,477,257
Other	20,077,132	18,677,827
Maintenance	30,074,370	32,342,896
Telecommunications Expense	25,309,470	26,059,166
Administrative and General	43,582,748	41,051,795
Depreciation	57,231,313	55,702,297
Taxes	20,755,847	19,727,313
Total Operating Expenses	403,210,178	388,219,998
Net Operating Income	43,133,227	30,394,390
NON-OPERATING REVENUES (EXPENSES)		
Interest Income	2,251,477	2,405,144
Contribution to Family Need	(100,000)	(480,000)
Other	(1,534,389)	1,555,659
Interest on Long-Term Debt (Net of AFUDC)	(18,209,650)	(15,893,207)
Gain/(Loss) on Defeasance or Refunding of Debt and Amortization of Debt Premium	4,132,856	(303,527)
Total Non-Operating Expenses	(13,459,706)	(12,715,931)
Net Income Before Capital Contributions and Transfers	29,673,521	17,678,459
Capital Contributions		
Cash	8,806,311	4,741,136
Donated Fixed Assets	149,323	421,334
BABs and CREBs Interest Subsidies	3,687,700	3,683,746
Transfers		
City of Tacoma Gross Earnings Tax	(34,141,875)	(30,460,098)
Transfers to/(from) Other Funds	-	(2,181)
CHANGE IN NET POSITION	8,174,980	(3,937,604)
TOTAL NET POSITION - BEGINNING OF YEAR	821,995,693	825,933,297
TOTAL NET POSITION - END OF YEAR	\$830,170,673	\$821,995,693

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

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

STATEMENTS OF CASH FLOWS

	YEAR TO DATE	
	December 31, 2017	December 31, 2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash from Customers	\$ 439,257,628	\$ 420,101,423
Cash Paid to Suppliers	(203,113,067)	(193,431,153)
Cash Paid to Employees	(113,801,766)	(111,575,956)
Taxes Paid	(19,994,454)	(19,155,309)
Conservation Loans	(82,798)	(1,119,433)
Net Cash from Operating Activities	102,265,543	94,819,572
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Transfer Out for Gross Earnings Tax	(34,141,875)	(30,460,098)
Transfer to/from Other Funds	-	(2,181)
Transfer to Family Need Fund	(100,000)	(480,000)
Net Cash from Non-Capital Financing Activities..	(34,241,875)	(30,942,279)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital Expenditures	(60,000,285)	(82,126,418)
Proceeds from Issuance of Long-Term Debt	70,575,000	30,000,000
Debt Issuance Costs	(250,578)	-
Principal Payments on Long-Term Debt	(92,730,000)	(14,735,000)
Payments for Early Extinguishment of Debt	(24,300,000)	-
Premium on Sale of Bonds	9,881,268	-
Interest Paid	(19,415,965)	(20,013,668)
BABs and CREBs Interest Subsidies	3,687,700	3,683,746
Contributions in Aid of Construction	8,806,311	4,741,136
Other Long-Term Liabilities	1,109,823	908,523
Net Cash from Capital and Related Financing Activities	(102,636,726)	(77,541,681)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest Received	2,251,477	2,405,144
Other Non-Op Revenues and Deductions	(1,283,810)	1,555,659
Net Cash from Investing Activities	967,667	3,960,803
Net Change in Cash and Equity in Pooled Investments	(33,645,391)	(9,703,585)
Cash and Equity in Pooled Investments at January 1..	257,582,093	267,285,678
Cash and Equity in Pooled Investments at December 31	\$223,936,702	\$257,582,093

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

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

STATEMENTS OF CASH FLOWS

	December 31, 2017	December 31, 2016
Reconciliation of Net Operating Income to Net Cash Provided by Operating Activities:		
Net Operating Income	\$43,133,227	\$30,394,390
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	57,231,313	55,702,297
Amortization of Regulatory Assets	7,519,282	6,492,341
Pension Expenses	9,169,545	5,860,495
Cash provided from changes in operating assets and liabilities:		
Accounts Receivable and Accrued Unbilled Revenue..	(7,085,780)	1,487,036
Conservation Loans Receivable	(82,798)	(1,119,433)
Interfund Receivables	405,819	(741,907)
Materials and Supplies, and Other	57,908	(1,777,443)
Taxes and Other Payables	689,734	7,100,914
Purchased Power Payable	579,934	625,664
Salaries, Wages and Compensated Absences Payable..	123,685	425,294
Long Term Accrued Compensated Absences	(283,826)	159,291
Customers' Deposits	18,611	(336,413)
Regulatory Asset - Conservation	(7,137,663)	(10,269,422)
Interfund Payables	(2,073,448)	816,468
Total Adjustments	59,132,316	64,425,182
Net Cash from Operating Activities	<u>\$102,265,543</u>	<u>\$94,819,572</u>
 Reconciliation of Cash and Equity in Pooled Investments to Balance Sheet:		
Cash and Equity in Pooled Investments in Special Funds	\$28,760,784	\$43,107,806
Cash and Equity in Pooled Investments in Operating Funds	195,175,918	214,474,287
Cash and Equity in Pooled Investments at December 31	<u>\$223,936,702</u>	<u>\$257,582,093</u>

**CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER**

**NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016**

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 177,153 retail customers and has 1,069 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 Tacoma Power'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.

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 certificates of deposit with East West Bank and Opus Bank.

The Division's equity in that portion of the City of Tacoma Investment Pool held in qualified public depositories at December 31, 2017 and 2016 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.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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 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.

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.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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 Generally Accepted Accounting Principles, land use rights such as easements and right-of-ways are recorded as intangible assets.

CAPITAL CONTRIBUTIONS - In accordance with Generally Accepted Accounting Principles, 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 PTO (personal time off) without distinction between vacation and sick leave. Employees who worked for the City prior to the change could choose to stay with the original policy or opt to convert to the new policy. The amount of PTO earned is based on years of service. The maximum accrual for PTO is 960 hours, and upon termination, employees are entitled to compensation for unused PTO at 100%. Vacation pay and PTO are recorded as a liability and expense in the year earned.

Employees in the original policy accumulate sick leave at the rate of one day per month with no maximum accumulation specified. 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. Sick leave pay is recorded as a liability and an expense in the year earned.

The accrued liability is computed at 100% vacation and PTO while sick leave is accrued at 10%, which is considered the amount vested or 25% if the employee meets retirement criteria. Based on historical information, 10% of compensated absences are considered short term.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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 7.5% 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 deferred outflows and liabilities and deferred inflows 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 INVESTMENTS MEASURED AT FAIR VALUE

The City measures and records its investments within the fair value hierarchy established by generally accepted accounting principles.

The Hierarchy is based on the valuation inputs used to measure the fair value of the asset, where fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. These guidelines recognize a three-tiered fair value hierarchy, as follows:

- Level 1 - Level 1 inputs are quoted (adjusted) prices in active markets for identical assets or liabilities that the government can access at the measurement date. Observable markets include exchange markets, dealer markets, brokered markets and principal-to-principal markets.
- Level 2 - Level 2 inputs are other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs are sourced from pricing vendors using models that are market-based and corroborated by observable market data including: quoted prices; nominal yield spreads; benchmark yield curves; and other corroborated inputs.
- Level 3 - Level 3 inputs are unobservable inputs for the asset or liability and should only be used when relevant Level 1 or Level 2 inputs are unavailable.

The fair value evaluations are provided by Interactive Data. Interactive Data utilizes evaluated pricing models that vary by asset class and incorporate available trade, bid and other market information and for structured securities, cash flow and, when available, loan performance data. Because many fixed income securities do not trade on a daily basis, Interactive Data's evaluated pricing applications apply available information as applicable through processes such as benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing, to prepare evaluations. In addition, Interactive Data uses model processes, such as the Option Adjusted Spread model to assess interest rate impact and development payment scenarios. Their models and processes take into account market convention. For each asset class, a team of evaluators gathers information from market sources and integrates relevant credit information, perceived market movements and sector news into the evaluated pricing applications and models.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

Cash and cash equivalents include highly liquid investments including short-term investment funds. Cash and cash equivalents are valued at cost and, therefore, excluded from the fair value schedule.

Data regarding the City's investments, valued and categorized according to the above outlined levels, is below:

	As of 12/31/2017	Level 1	Level 2	Level 3
Debt Securities				
U.S. Treasury Securities	\$ 218,142,864	\$ -	\$ 218,142,864	\$ -
U.S. Agency Securities	517,345,818	-	517,345,818	-
Supranational Securities	19,966,040	-	19,966,040	-
Municipal Bonds	40,760,727	-	40,760,727	-
Total	<u>\$ 796,215,449</u>	<u>\$ -</u>	<u>\$ 796,215,449</u>	<u>\$ -</u>

	As of 12/31/2016	Level 1	Level 2	Level 3
Debt Securities				
U.S. Treasury Securities	\$ 146,824,628	\$ -	\$ 146,824,628	\$ -
U.S. Agency Securities	544,579,831	-	544,579,831	-
Municipal Bonds	61,450,051	-	61,450,051	-
Total	<u>\$ 752,854,510</u>	<u>\$ -</u>	<u>\$ 752,854,510</u>	<u>\$ -</u>

Tacoma Power's share of the City investments shown in the table above is 24.19% and 33.84% as of December 31, 2017 and 2016.

NOTE 4 UTILITY PLANT

A summary of the balances and changes in utility plant for 2017 and 2016 follows:

	Balance December 31, 2016	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2017
Intangible Plant	\$ 45,432,098	\$ 690,906	\$ (47,342)	\$ -	\$ 46,075,662
Hydraulic Production					
Plant	643,897,651	22,816,989	-	-	666,714,640
Transmission Plant	229,380,382	8,922,577	(224,262)	-	238,078,697
Distribution Plant	642,437,552	17,886,641	(2,608,125)	-	657,716,068
Regional Transmission	24,923,858	283,267	-	-	25,207,125
General Plant	205,551,865	3,085,910	-	-	208,637,775
Telecommunications					
Plant	212,581,376	832,979	-	-	213,414,355
Total Utility Plant in					
Service	2,004,204,782	54,519,269	(2,879,729)	-	2,055,844,322
Less Accumulated					
Depreciation	(997,207,625)	(57,231,313)	2,832,387	1,381,399	(1,050,225,152)
	<u>1,006,997,157</u>	<u>(2,712,044)</u>	<u>(47,342)</u>	<u>1,381,399</u>	<u>1,005,619,170</u>
Construction Work In					
Progress	26,411,907	66,166,265	-	(60,421,314)	32,156,858
Net Utility Plant	<u>\$ 1,033,409,064</u>	<u>\$ 63,454,221</u>	<u>\$ (47,342)</u>	<u>\$ (59,039,915)</u>	<u>\$ 1,037,776,028</u>

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

	Balance December 31, 2015	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2016
Intangible Plant	\$ 41,682,352	\$ 3,797,958	\$ (48,212)	\$ -	\$ 45,432,098
Hydraulic Production Plant	554,637,653	89,259,998	-	-	643,897,651
Transmission Plant	219,918,041	9,721,911	(259,570)	-	229,380,382
Distribution Plant	618,397,975	27,229,473	(3,189,896)	-	642,437,552
Regional Transmission	18,147,561	6,776,297	-	-	24,923,858
General Plant	200,160,423	5,391,442	-	-	205,551,865
Telecommunications Plant	208,198,584	4,382,792	-	-	212,581,376
Total Utility Plant in Service	1,861,142,589	146,559,871	(3,497,678)	-	2,004,204,782
Less Accumulated Depreciation	(946,283,353)	(55,702,297)	3,449,466	1,328,559	(997,207,625)
	914,859,236	90,857,574	(48,212)	1,328,559	1,006,997,157
Construction Work In Progress	87,951,638	85,011,567	-	(146,551,298)	26,411,907
Net Utility Plant	<u>\$ 1,002,810,874</u>	<u>\$ 175,869,141</u>	<u>\$ (48,212)</u>	<u>\$ (145,222,739)</u>	<u>\$ 1,033,409,064</u>

Total Utility Plant in Service includes non-depreciable assets of \$76,906,141 for 2017 and \$75,780,466 for 2016.

The total amount of interest cost incurred and capitalized is \$1,448,668 for 2017 and \$3,752,735 for 2016.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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, 2017 and December 31, 2016 was as follows:

	Balance December 31, 2016	Additions	Reductions	Balance December 31, 2017	Due Within One Year
Revenue Bonds	\$ 371,065,000	70,575,000	\$ (37,030,000)	\$ 404,610,000	\$ 11,575,000
Plus: Unamortized					
Premium	19,016,726	9,881,268	(4,132,857)	24,765,137	-
Net Revenue Bonds	390,081,726	80,456,268	(41,162,857)	429,375,137	11,575,000
Line of Credit	80,250,000	-	(80,000,000)	250,000	250,000
Total Long-Term					
Debt	<u>\$ 470,331,726</u>	<u>\$ 80,456,268</u>	<u>\$ (121,162,857)</u>	<u>\$ 429,625,137</u>	<u>\$ 11,825,000</u>

	Balance December 31, 2015	Additions	Reductions	Balance December 31, 2016	Due Within One Year
Revenue Bonds	\$ 385,800,000	\$ -	\$ (14,735,000)	\$ 371,065,000	\$ 12,730,000
Plus: Unamortized					
Premium	20,613,130	-	(1,596,404)	19,016,726	-
Net Revenue Bonds	406,413,130	-	(16,331,404)	390,081,726	12,730,000
Line of Credit	50,250,000	30,000,000	-	80,250,000	-
Total Long-Term					
Debt	<u>\$ 456,663,130</u>	<u>\$ 30,000,000</u>	<u>\$ (16,331,404)</u>	<u>\$ 470,331,726</u>	<u>\$ 12,730,000</u>

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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

	<u>2017</u>	<u>2016</u>
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 \$7,470,000 to \$14,310,000 from 2018 to 2042. Original Issue: \$181,610,000 Current Portion: \$11,575,000	127,160,000	164,190,000
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 from 2022 to 2030. Original Issue: \$35,620,000 Current Portion: \$0	35,620,000	35,620,000
2017 Revenue Bonds, with interest rates ranging from 4.0% to 5.0%, due in yearly installments of \$2,150,000 to \$5,225,000 from 2022 to 2047. Original Issue: \$70,575,000 Current Portion: \$0	70,575,000	-
	404,610,000	371,065,000
Unamortized premium	24,765,137	19,016,726
Current Portion of Revenue Bond Debt	(11,575,000)	(12,730,000)
Long-term Portion of Revenue Bond Debt	417,800,137	377,351,726
Revolving Line of Credit	-	80,250,000
Total Long Term Debt	<u>\$ 417,800,137</u>	<u>\$ 457,601,726</u>

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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) of 1.96044% at December 31, 2017. Each advance is secured by Revenues as set forth in the Note Ordinance. The balance outstanding is \$250,000 as of December 31, 2017.

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

	Principal	Interest
2018	11,575,000	19,826,810
2019	10,095,000	19,915,735
2020	9,365,000	19,454,235
2021	7,470,000	19,035,860
2022	5,945,000	18,702,985
2023-2027	51,000,000	88,475,821
2028-2032	79,030,000	72,816,517
2033-2037	120,460,000	37,650,167
2038-2042	85,475,000	14,242,200
2043-2047	24,195,000	2,495,100
	\$ 404,610,000	\$ 312,615,430

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. The Division was in compliance with all loan covenants at December 31, 2017 and 2016.

In October 2017, Tacoma Power used cash to defease \$24,300,000 of the outstanding 2013 Series A Electric System Revenue and Refunding Bonds to levelize and reduce future debt service payments. This defeasance resulted in a loss of \$1,903,106. The Cash Flow impact of the defeasance was a reduction in principal and interest payments in the amount of \$22,025,000 in 2020 and \$5,130,000 in 2021.

As of December 31, 2017, the following outstanding bonds were considered defeased:

<u>Issue</u>	<u>Amount</u>
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
2013 Electric System Revenue Refunding Bonds - Series A	24,300,000
.	\$ 81,685,000

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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 459,284 and 433,427 kilowatts per hour for 2017 and 2016, respectively. Charges for the BPA purchased power were approximately \$120 million and \$114 million for 2017 and 2016, respectively, and are based on the total amount of energy delivered and the monthly peak power demand.

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 2017 and 2016, Tacoma Power recovered \$1,263,968 and \$7,076,890 respectively through the ECA which are recorded as reductions of power purchase expense. Receipt of these funds is cyclical, resulting in a greater amount recovered in the first year of the biennium.

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.

Information for the year ended December 31, 2017 pertaining to these contracts is summarized as follows:

<u>Tacoma Power's Current Share of</u>	<u>Grand Coulee Project Hydro Authority</u>	<u>Grant County PUD - Priest Rapids Project</u>
Energy Output	228,781 mWh	27,440 mWh
Megawatt Capacity	-	5 mW
Operating Costs	\$ 3,622,294	\$481,320
Incentive Payments	\$ 2,886,324	-
Contract Expiration Date	5/9/2024	4/1/2052

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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 2017 and 2016 were \$6,830,417 and \$6,412,705, respectively, for Grand Coulee Project Hydro Authority, however, proceeds under the contract exceeded expenses in 2016 and 2015 for Grant County PUD - Priest Rapids resulting in a gain of \$481,320 and \$80,802, 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, 2017 Tacoma Power had forward sales contracts totaling \$16.6 million dollars extending out to June 2019 with a fair market value of \$14.8 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:

<u>Interchange Summary</u>	<u>2017</u> (in kWh)	<u>2016</u> (in kWh)
Secondary Sales	(2,835,719,000)	(2,731,083,000)
Portfolio Purchases	369,775,000	263,105,000
Miscellaneous Exchanges	(1,193,000)	(1,533,000)
Other	(8,093,000)	26,228,000
Net Interchange	<u>(2,475,230,000)</u>	<u>(2,443,283,000)</u>

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 2017 and 2016 were \$4,241,637 and \$6,733,591 respectively.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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 2017 and 2016, Fleet Services returned 75% of the interest earned to Tacoma Power's replacement fund. The amount of the refund was \$108,119 and \$106,192 for 2017 and 2016, 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 \$700,000 and \$900,000 in 2017 and 2016 respectively. Assets in the Self-Insurance Fund total \$7.0 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.

Other 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 property insurance policy has a deductible of \$250,000 for buildings and property within buildings and \$10,000 per vehicle. General government obtains coverage on general government's buildings and property within buildings with a limit of \$500,000 and a retention of \$150,000 with exceptions. For the Department, 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 \$20 million of excess coverage with a \$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 or System), 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.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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 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, 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 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, 2016 (measurement date) is as follows:

Retirees and beneficiaries currently receiving benefits	2,303	
Terminated vested and other terminated participants	675	
Active members:		
City of Tacoma	2,687	
South Sound 911	2	
Pierce Transit	8	
Tacoma-Pierce County Health Department	267	
Total active members		2,964
Total membership		<u>5,942</u>

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 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.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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.

In fiscal year 2017, 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%. On November 28, 2017 the Tacoma City Council approved the TERS Board's recommendation to increase the contribution rate by 1% (split 0.54% for employers and 0.46% for employees) effective the first pay period in February 2018, 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, 2016
Valuation Date	January 1, 2017
Actuarial Cost Method	Entry Age Normal
Amortization Method	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: <ul style="list-style-type: none">• Level percent• Open periods• 30 year amortization period at 01/01/2015• 3.75% amortization growth rate
Asset Valuation Method	4 year smoothing period; Corridor - None
Inflation	2.75%
Salary Increases	Varies by service
Investment Rate of Return	7.00%
Cost of Living Adjustment	2.125%
Retirement Age	Varies by age, gender, and eligibility
Turnover	Varies by service, and gender
Mortality	RP-2014 Mortality for Employees, Healthy and Disabled Annuitants. Generational improvements with projection scale based on Social Security Administration Data.

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. The following changes in assumptions occurred since the January 1, 2016 Actuarial Valuation:

1. The amortization growth rate decreased from 4% to 3.75%
2. The inflation rate decreased from 3% to 2.75%
3. The investment rate of return decreased from 7.25% to 7%

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

Target Allocations - The long-term expected rate of return is determined by adding expected inflation to expected long-term real returns and reflecting expected volatility and correlation. The capital market assumptions are per Milliman's (the System's actuary) investment consulting practice as of December 31, 2016. The target asset allocation is based on the Tacoma Employees' Retirement System Investment Policy Statement dated March 2016.

Asset Class	Target Allocation	Long-term Expected Arithmetic Real Rate of Return
Investment Grade Fixed Income	15.0%	1.63%
US Inflation-Indexed Bonds	5.0%	1.21%
High Yield Bonds	9.0%	5.00%
Emerging Market Debt	5.0%	3.74%
Global Equity	41.5%	5.50%
Public Real Estate	2.0%	5.80%
Private Real Estate	2.5%	3.56%
Private Equity	10.0%	9.04%
Master Limited Partnerships	4.0%	4.12%
Timber	2.0%	3.79%
Infrastructure	2.0%	5.03%
Agriculture	2.0%	4.33%
Assumed Inflation - Mean		2.75%
Assumed Inflation - Standard Deviation		1.85%
Portfolio Arithmetic Real Mean Return		4.76%
Portfolio Median Nominal Geometric Return		6.72%
Portfolio Standard Deviation		11.77%
Long-Term Expected Rate of Return, net of investment expenses		7.00%

Sensitivity Analysis - The following presents the net pension liability (asset) of the System, calculated using the discount rate of 7%, 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%) or 1 percentage point higher (8%) than the current rate.

	1% Decrease 6.00%	Current Discount Rate 7.00%	1% Increase 8.00%
Net pension liability (asset)	\$ 117,478,293	\$ 36,687,245	\$ (28,877,776)

As of December 31, 2017, the deferred inflows and outflows of resources are as follows:

	Deferred Inflows of Resources	Deferred Outflows of Resources
Difference Between Expected and Actual Experience	\$ (7,896,446)	\$ -
Changes of assumptions	-	12,184,553
Net Difference Between Projected and Actual Earnings	-	16,695,395
Changes in Employer Proportion	(8,418)	17,895
Contributions Made Subsequent to the Measurement Date		9,528,899
Total	\$ (7,904,864)	\$ 38,426,742

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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.

Amounts will be recognized in pension expense as follows:

2018	\$	6,536,944
2019		6,536,943
2020		7,538,909
2021		(283,779)
2022		663,962
Thereafter		-
	\$	<u>20,992,979</u>

The proportionate share of the Power Division is 39.50% of total System's pension liability. 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. GASB 45 requires that the portion of age-adjusted expected retiree health claims costs that exceed the premium charged to retirees be recognized as a liability for accounting purposes. 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 (3.50%).

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 under GASB 45. 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 2017 is 20 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 statements of net position. The City has a Net OPEB Obligation as of December 31, 2017 as the City has not set aside funds for OPEB.

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

Excise Tax for High Cost or “Cadillac” Health Plans in 2020 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 Consolidated Appropriations Act (CAA), which was signed into law in December 2015, delays the tax for two years, until 2020.

GASB Statement No. 45, as well as GASB 74 and 75, indicate 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. 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.

There is significant uncertainty with respect to the excise tax at this time. President Trump recently signed an executive order which gives instruction to the leaders of the new administration to unwind certain aspects of the ACA, especially those components deemed “burdensome.” It remains unclear how this would be implemented, especially due to the interconnected nature of the ACA. The City has continued to value the excise tax as it currently appears in the tax code, but will monitor this situation carefully going forward.

Summary of Changes – As of the January 1, 2017 valuation the total AAL was \$240,449,771, for the City, 12.5% higher than expected primarily due to changes demographic experience, medical cost expectations and medical trend assumptions, and demographic and economic assumptions.

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

	<u>January 1, 2015</u>	<u>January 1, 2017</u>
Active employees	3,404	3,492
Terminated vested employees	442	476
Retired employees & dependents	<u>744</u>	<u>691</u>
Total	<u><u>4,590</u></u>	<u><u>4,659</u></u>
Annual Benefit Payments	\$ 8,963,089	\$ 9,010,942
Discount rate	3.75%	3.50%
Present Value of Benefits (PVB)	\$ 262,184,195	\$ 289,047,229
Actuarial Accrued Liability (AAL)	\$ 208,814,312	\$ 240,449,771
Assets	<u>\$ -</u>	<u>\$ -</u>
Unfunded Actuarial Accrued Liability (UAAL)	<u><u>\$ 208,814,312</u></u>	<u><u>\$ 240,449,771</u></u>
Normal Cost	\$ 3,832,131	\$ 3,261,947
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 19,529,549

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

The following table shows the total value of the benefits provided, the member paid premiums and the City paid benefits as of January 1, 2017.

Value of Subsidy at 3.50% Interest Rate	Total Value of Benefits	Member Paid Premiums	City Paid Benefits
Present Value of Benefits (PVB)	\$ 399,300,824	\$ 110,253,595	\$ 289,047,229
Actuarial Accrued Liability (AAL)	\$ 285,825,708	\$ 45,375,937	\$ 240,449,771
Normal Cost	\$ 7,595,595	\$ 4,443,955	\$ 3,151,640
Annual Benefit Payments	\$ 11,674,734	\$ 2,663,793	\$ 9,010,941

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, 2017.

	City	Division
Determination of Annual Required Contribution:		
Normal Cost at Year-end	\$ 3,261,947	\$ 657,735
Amortization of UAAL	16,267,602	278,261
Annual Required Contribution (ARC)	<u>\$ 19,529,549</u>	<u>\$ 935,996</u>
Determination of NET OPEB Obligation:		
Annual Required Contribution (ARC)	\$ 19,529,549	\$ 935,996
Interest on prior year Net OPEB Obligation	2,895,939	381,185
Adjustments to ARC	(4,743,612)	(532,159)
Annual OPEB Cost	17,681,876	785,022
Actual benefits paid	(9,010,941)	(393,983)
Increase in Net OPEB Obligation	8,670,935	391,039
Net OPEB Obligation - beginning of year	82,741,128	10,890,990
Net OPEB Obligation - end of year	<u>\$ 91,412,063</u>	<u>\$ 11,282,029</u>

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 3.50% interest rate.

	Annual OPEB Cost		Benefits Paid		Net OPEB Obligation	
Year Ended	City	Division	City	Division	City	Division
12/31/2015	\$ 15,954,387	\$ 1,194,337	\$ 8,963,089	\$ 324,146	\$ 73,129,502	\$ 10,068,491
12/31/2016	\$ 18,151,028	\$ 1,166,592	\$ 8,539,402	\$ 344,092	\$ 82,741,128	\$ 10,890,990
12/31/2017	\$ 17,681,876	\$ 785,022	\$ 9,010,941	\$ 393,983	\$ 91,412,063	\$ 11,282,029

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

TACOMA POWER NOTES TO FINANCIAL STATEMENTS (continued)

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 ARC, 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 20 years.

Actuarial Methods and Significant Actuarial Assumptions:

Valuation Date:	January 1, 2017
Census Date:	January 1, 2017
Actuarial Cost Method:	Entry Age
Amortization Method:	Combination of level percentage and level dollar amount, see note above.
Remaining Amortization Period:	20 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: 3.50% for pay-as-you-go funding

Medical Cost Trend:	2017	9.10%
	2018	6.40%
	2019	5.80%
	2020	5.30%
	2030	5.40%
	2040	5.50%
	2050	5.20%

The trend for year 2017 reflects the amount by which 2018 medical costs are expected to exceed 2017 medical costs. The medical cost rate is assumed to continue grading downward until achieving the ultimate rate of 4.40% in 2073 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): 3.50%

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 2017/2018 biennial Capital Improvement Program is approximately \$190.5 million. As of December 31, 2017, the remaining financial requirement for the 2017/2018 biennial Capital budget was approximately \$140.9 million.

Ted Coates, et al. v. Tacoma On June 22, 2017, plaintiffs filed their suit in Pierce County Superior Court, alleging Tacoma Power has been unlawfully subsidizing the capital expenses and the operational and maintenance (O&M) expenses of its commercial telecommunications business (Click!). The plaintiffs have requested an immediate cessation of all such subsidies and to refund to the Tacoma Power electric utility customers funds spent subsidizing these operations for the past three years (alleged to be in excess of \$21 million). The law firm of K&L Gates has been retained by the City to defend Tacoma Power, Click! and the City. On March 2, 2018 the Court granted plaintiffs' motion for partial summary judgment ordering that Tacoma Power electric utility revenues and funds may not lawfully be used to pay for Click! Network expenses or capital improvements that are attributable or properly allocable to commercial telecommunications service rather than electric utility service. The City is considering pursuing an interlocutory appeal of the Court's order on partial summary judgment, which, if granted, would stay the underlying proceedings. Trial is scheduled for June 21, 2018. The insurance carrier is currently defending under a reservation of rights letter.

General Legal Matters - Tacoma Power 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 Utility.

REQUIRED SUPPLEMENTARY INFORMATION

Proportionate Share of the Net Pension Liability Last 10 Years*

	Fiscal Year Ended December 31st,		
	2017	2016	2015
Employer's proportion of the net pension liability (asset) as a percentage	39.50%	39.47%	39.80%
Employer's proportion share of net pension liability (asset)	\$36,687,245	\$34,177,293	(\$3,823,476)
Employer's covered payroll (1)	\$91,704,363	\$93,063,240	\$86,312,354
Employer's proportionate share of net pension liability (asset) as a percentage of its covered employee payroll (1)	40.01%	36.72%	-4.11%
Plan fiduciary net position as a percentage the total pension liability	93.91%	93.94%	100.71%

Schedule of Contributions Last 10 Fiscal Years*

	Fiscal Year Ended December 31st,		
	2017	2016	2015
Contractually required employer contribution	\$9,528,899	\$9,322,005	\$9,053,341
Contributions in relation to the contractually required employer contribution	(9,528,899)	(9,322,005)	(9,053,341)
Employer contribution deficiency (excess)			
Employer's covered employee payroll	\$95,163,955	\$91,704,363	\$93,063,240
Employer contribution as a percentage of covered-employee payroll	10.01%	10.17%	9.73%

(1) The 2016 covered payroll has been updated to accurately reflect the covered payroll, which therefore also updated the calculation for the Employer's proportionate share of net pension liability (asset) as a percentage of its covered employee payroll.

* The above schedules are intended to show information for 10 years, the additional years' information will be displayed as it becomes available.

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STATISTICAL DATA (Unaudited)

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

TEN-YEAR FINANCIAL REVIEW

STATEMENTS OF NET POSITION	2017	2016	2015	2014
ASSETS				
Utility Plant - Net	\$1,037,776,028	\$1,033,409,064	\$1,002,810,874	\$978,885,275
Special and Other Assets	81,257,489	95,903,332	125,203,792	160,778,160
Current Assets	276,486,000	289,162,319	267,460,091	365,173,352
Deferred Charges	-	-	-	-
Total Assets	1,395,519,517	1,418,474,715	1,395,474,757	1,504,836,787
Deferred Outflows	38,426,742	39,469,454	10,977,517	8,026,229
TOTAL ASSETS AND DEFERRED OUTFLOWS	1,433,946,259	1,457,944,169	1,406,452,274	1,512,863,016
NET POSITION	830,170,673	821,995,693	825,933,297	822,803,061
LIABILITIES				
Long-Term Debt	417,800,137	457,601,726	441,928,130	530,580,510
Current Liabilities	68,841,615	70,165,746	63,906,544	86,776,174
Long-Term Liabilities	61,228,970	57,893,021	22,647,914	24,703,271
Total Liabilities	547,870,722	585,660,493	528,482,588	642,059,955
Deferred Inflows	55,904,864	50,287,983	52,036,389	48,000,000
TOTAL NET POSITION, LIABILITIES, AND DEFERRED INFLOWS	\$1,433,946,259	\$1,457,944,169	\$1,406,452,274	\$1,512,863,016
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION				
OPERATING REVENUES				
Residential	\$169,583,337	\$154,091,270	\$149,195,092	\$150,972,050
Commercial	29,133,553	27,703,400	26,956,059	26,594,512
General	119,704,634	115,600,650	116,053,999	114,718,365
Contract Industrial	22,278,802	21,462,712	21,356,911	21,150,771
Bulk Power	57,062,247	54,506,535	50,380,147	82,796,740
Unbilled	2,114,131	(840,477)	677,091	(666,187)
Other	1,754,802	1,725,200	1,643,756	1,609,143
Total Electric Revenues	401,631,506	374,249,290	366,263,055	397,175,394
Other Operating Revenue	44,711,899	44,365,098	44,363,160	44,070,713
Total Operating Revenues	446,343,405	418,614,388	410,626,215	441,246,107
OPERATING EXPENSES				
Operation and Maintenance	325,223,018	312,790,388	299,200,704	294,741,044
Taxes	20,755,847	19,727,313	19,993,833	19,276,216
Depreciation	57,231,313	55,702,297	57,381,578	59,156,228
Loss on Asset Impairment	-	-	-	-
Total Operating Expenses	403,210,178	388,219,998	376,576,115	373,173,488
NET OPERATING INCOME	43,133,227	30,394,390	34,050,100	68,072,619
NON-OPERATING REVENUES (EXPENSES)				
Other Income and Expense (Net)	(1,534,389)	1,555,659	(1,923,329)	(728,908)
Interest Earned on Investments	2,251,477	2,405,144	1,796,071	3,780,834
Interest Charges (Net)	(14,076,794)	(16,196,734)	(19,428,673)	(27,290,021)
Contributions to Family Need ..	(100,000)	(480,000)	(480,000)	(900,000)
Gain on Sale of Utility Plant .	-	-	-	-
Net Income Before Contributions, Transfers & Extraordinary Items	29,673,521	17,678,459	14,014,169	42,934,524
Total Capital Contributions	12,643,334	8,846,216	9,383,844	7,788,292
Transfers Out	(34,141,875)	(30,462,279)	(24,969,422)	(26,998,415)
CHANGE IN NET POSITION	\$8,174,980	(\$3,937,604)	(\$1,571,409)	\$23,724,401

In accordance with Governmental Accounting Standards Board Statement No.65 both 2012 and 2011 were restated for comparative purposes. Years prior to 2011 are shown as originally reported.

2013	2012	2011	2010	2009	2008
\$959,885,269	\$954,141,423	\$944,969,878	\$933,796,881	\$900,879,652	\$855,373,200
213,192,582	154,745,677	196,860,001	223,057,734	104,606,844	122,629,299
328,974,357	333,694,736	313,457,995	279,967,672	288,083,393	312,006,708
-	-	-	17,651,421	7,304,736	1,990,596
1,502,052,208	1,442,581,836	1,455,287,874	1,454,473,708	1,300,874,625	1,291,999,803
15,941,231	7,848,910	8,213,239	-	-	-
1,517,993,439	1,450,430,746	1,463,501,113	1,454,473,708	1,300,874,625	1,291,999,803
799,078,660	779,206,485	762,944,507	744,735,781	735,593,799	695,305,259
564,960,765	518,251,959	563,718,608	582,930,840	459,202,498	490,528,958
82,905,132	84,070,814	82,861,816	95,884,868	83,385,715	100,219,839
23,048,882	20,901,488	17,976,182	30,922,219	22,692,613	5,945,747
670,914,779	623,224,261	664,556,606	709,737,927	565,280,826	596,694,544
48,000,000	48,000,000	36,000,000	-	-	-
\$1,517,993,439	\$1,450,430,746	\$1,463,501,113	\$1,454,473,708	\$1,300,874,625	\$1,291,999,803
\$149,662,791	\$141,236,063	\$136,944,688	\$127,908,143	\$125,807,518	\$131,188,854
25,110,481	23,499,735	22,324,063	21,147,156	21,005,151	22,138,244
109,046,936	103,586,233	99,958,156	96,579,940	90,782,730	100,142,959
19,804,613	18,870,807	18,341,067	16,898,845	14,101,372	15,430,080
64,210,259	53,532,081	48,118,090	69,518,730	67,338,457	98,545,139
1,651,808	4,615,802	369,424	(3,564,337)	(411,080)	1,576,914
1,562,082	1,558,268	1,373,168	1,472,125	1,190,013	1,387,629
371,048,970	346,898,989	327,428,656	329,960,602	319,814,161	370,409,819
43,413,115	40,983,752	36,895,939	36,892,658	35,691,490	33,998,632
414,462,085	387,882,741	364,324,595	366,853,260	355,505,651	404,408,451
276,558,723	267,457,626	247,409,057	259,366,287	220,849,709	246,856,188
19,562,858	17,494,729	16,970,015	15,553,041	15,187,859	16,075,356
56,397,306	57,842,109	56,555,538	55,717,463	53,049,558	48,377,708
-	-	-	-	-	-
352,518,887	342,794,464	320,934,610	330,636,791	289,087,126	311,309,252
61,943,198	45,088,277	43,389,985	36,216,469	66,418,525	93,099,199
(252,363)	3,055,848	1,226,132	2,202,089	1,322,007	3,255,797
1,899,829	5,835,775	8,444,683	7,786,710	8,721,608	12,539,619
(25,688,219)	(22,859,967)	(21,917,623)	(22,773,604)	(22,804,261)	(22,420,879)
(900,000)	(450,000)	(450,000)	(900,000)	(1,229,676)	(450,000)
-	-	-	-	-	2,923,465
37,002,445	30,669,933	30,693,177	22,531,664	52,428,203	88,947,201
8,839,960	9,480,111	14,222,934	10,224,518	9,844,736	10,219,425
(25,970,230)	(23,888,066)	(23,913,077)	(23,614,200)	(21,984,399)	(25,679,317)
\$19,872,175	\$16,261,978	\$21,003,034	\$9,141,982	\$40,288,540	\$73,487,309

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

TEN-YEAR POWER SUMMARY

	2017	2016	2015	2014
MWh Available				
Generated				
Nisqually	631,627	630,483	511,592	635,121
Cushman	377,366	507,618	272,457	358,509
Cowlitz	2,138,980	1,989,438	1,630,130	2,111,686
Wynoochee	34,103	37,209	12,680	14,272
Hood Street	3,282	2,942	1,889	2,281
Grant Net Actual	-	-	-	(2,018)
Tacoma's Share of Priest Rapids	27,440	26,975	25,360	22,733
Tacoma's Share of GCPHA	228,781	253,625	258,679	272,846
Total Generated	3,441,579	3,448,290	2,712,787	3,415,430
Purchased	4,023,330	3,807,370	3,674,140	3,845,666
Interchange - Net	(2,458,785)	(2,438,369)	(1,569,981)	(2,339,277)
Losses - Net	27,919	(8,870)	10,340	14,057
Total System Load	5,034,043	4,808,421	4,827,286	4,935,876
MWh Billed				
Residential and Other.....	1,975,096	1,855,706	1,801,114	1,890,970
Commercial/General/Industrial....	2,777,190	2,771,822	2,786,233	2,838,966
Total Firm MWh Billed	4,752,286	4,627,528	4,587,347	4,729,936
MWh Available Over MWh Billed				
(Causes: Timing differences, internal use, and losses other than those reflected above.)	281,757	180,893	239,939	205,940
Percent of Power Generated	68.37%	71.71%	56.20%	69.20%
Average Load Factor	57.27%	60.02%	62.71%	55.31%
Average Number of Billings	177,153	176,784	174,562	172,531
Maximum Hourly Energy Load				
MWh	997	913	877	1,016
Date	1/5/17	12/17/16	12/31/15	2/6/14
Time	0800 hr	0900 hr	0900 hr	800 hr
Maximum Daily Energy Load				
MWh	20,525	19,641	18,675	21,686
Date	1/5/17	12/17/16	12/31/15	2/6/14
Minimum Hourly Energy Load				
MWh	350	351	354	348
Date	7/2/17	7/5/16	6/21/15	7/6/14
Time	0600 hr	0400 hr	0600 hr	0600 hr
Minimum Daily Energy Load				
MWh	10,315	10,110	10,262	10,221
Date	6/4/17	9/4/16	5/24/15	7/5/14
Average Hourly Energy Load	571	548	550	562

2013	2012	2011	2010	2009	2008
572,932	699,104	663,345	586,433	553,062	530,839
239,528	261,735	410,723	393,563	246,898	208,604
1,792,975	2,322,875	2,157,106	1,725,424	1,677,554	1,736,328
24,404	38,149	35,692	36,320	25,298	25,368
3,503	4,029	3,313	4,133	3,243	4,217
(3,279)	(3,285)	-	-	-	-
34,846	37,355	34,417	30,705	-	-
254,570	255,564	237,794	240,845	-	-
2,919,479	3,615,526	3,542,390	3,017,423	2,506,055	2,505,356
3,756,763	4,167,263	3,799,037	4,132,049	4,235,019	4,252,681
(1,665,811)	(2,814,479)	(2,266,720)	(1,993,911)	(1,729,701)	(1,677,704)
7,398	20,718	(8,112)	10,599	4,210	10,132
5,017,829	4,989,028	5,066,595	5,166,160	5,015,583	5,090,465
1,950,829	1,935,518	1,997,714	1,925,549	1,994,692	1,979,930
2,855,932	2,812,769	2,838,424	2,794,406	2,829,425	2,866,480
4,806,761	4,748,287	4,836,138	4,719,955	4,824,117	4,846,410
211,068	240,741	230,457	446,205	191,466	244,055
58.18%	72.47%	69.92%	58.41%	49.97%	49.22%
54.18%	61.47%	58.86%	52.82%	51.69%	56.68%
171,506	169,012	169,123	169,413	168,207	166,307
980	924	931	992	1,062	1,018
12/9/13	1/16/12	1/3/11	11/23/10	12/10/09	12/15/08
800 hr	1800 hr	0800 hr	1800 hr	800 hr	1900 hr
21,172	19,100	18,788	20,591	21,103	21,237
12/09/13	1/16/12	1/11/11	11/23/10	12/9/09	12/15/08
349	340	310	303	295	349
9/8/13	9/19/12	7/5/11	9/3/10	7/5/09	7/6/08
0500 hr	0400 hr	0400 hr	0300 hr	0700 hr	0700 hr
10,379	10,160	9,171	9,041	9,036	10,235
7/4/13	9/2/12	7/3/11	9/5/10	8/15/09	8/31/08
572	566	548	524	549	577

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

GROSS GENERATION REPORT - December 31, 2017 AND December 31, 2016

	YEAR ENDED		2017 OVER (UNDER) 2016	PERCENT CHANGE
	Dec 31 2017	Dec 31 2016		
KWH GENERATED, PURCHASED AND INTERCHANGED - Gross				
Generated - LaGrande	399,198,000	378,898,000	20,300,000	5.4%
Generated - Alder	232,429,000	251,585,000	(19,156,000)	-7.6%
TOTAL NISQUALLY	631,627,000	630,483,000	1,144,000	0.2%
Generated - Cushman No. 1	145,908,000	185,318,000	(39,410,000)	-21.3%
Generated - Cushman No. 2	231,458,000	322,300,000	(90,842,000)	-28.2%
TOTAL CUSHMAN	377,366,000	507,618,000	(130,252,000)	-25.7%
Generated - Mossyrock	1,267,003,000	1,203,631,000	63,372,000	5.3%
Generated - Mayfield	871,977,000	785,807,000	86,170,000	11.0%
TOTAL COWLITZ	2,138,980,000	1,989,438,000	149,542,000	7.5%
Generated - Wynoochee	34,103,000	37,209,000	(3,106,000)	-8.3%
Generated - Hood Street	3,282,487	2,942,400	340,087	11.6%
Tacoma's Share of Priest Rapids	27,440,000	26,975,000	465,000	1.7%
Tacoma's Share of GCPHA	228,781,000	253,625,000	(24,844,000)	-9.8%
TOTAL KWH GENERATED - TACOMA SYSTEM	3,441,579,487	3,448,290,400	(6,710,913)	-0.2%
Purchased Power				
BPA Slice Contract	2,475,180,000	2,265,823,000	209,357,000	9.2%
BPA Block Contract	1,548,150,000	1,541,547,000	6,603,000	0.4%
Interchange Net	(2,458,785,000)	(2,438,369,000)	(20,416,000)	0.8%
TOTAL KWH GENERATED, PURCHASED AND INTERCHANGED ..	5,006,124,487	4,817,291,400	188,833,087	3.9%
Losses	37,621,097	41,976,966	(4,355,869)	-10.4%
Baldi Replacement	1,172,164	1,864,094	(691,930)	-37.1%
Ketron	297,065	262,023	35,042	13.4%
NT PC Mutuals Schedules.....	(31,634,000)	(28,498,000)	(3,136,000)	11.0%
PC Mutual Inadvertent	20,462,383	(24,475,004)	44,937,387	-183.6%
TACOMA SYSTEM FIRM LOAD	5,034,043,196	4,808,421,479	225,621,717	4.7%
PIERCE COUNTY MUTUAL LOAD	1,530,309,000	1,435,535,000	94,774,000	6.6%
KWH BILLED				
Residential Sales	1,938,642,781	1,817,931,140	120,711,641	6.6%
Commercial Sales	327,155,195	316,085,742	11,069,453	3.5%
General	1,940,256,895	1,947,062,423	(6,805,528)	-0.3%
Contract Industrial	509,777,460	508,673,780	1,103,680	0.2%
Public Street and Highway Lighting	28,948,502	31,555,485	(2,606,983)	-8.3%
Sales to Other Electric Utilities	7,505,100	6,219,000	1,286,100	20.7%
TOTAL FIRM	4,752,285,933	4,627,527,570	124,758,363	2.7%
Bulk Power Sales	2,835,719,000	2,731,076,000	104,643,000	3.8%
TOTAL KWH BILLED	7,588,004,933	7,358,603,570	229,401,363	3.1%

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

DEBT SERVICE REQUIREMENTS
DECEMBER 31, 2017

<u>YEAR</u>	<u>PRINCIPAL</u>	<u>INTEREST</u>	<u>TOTAL</u>
2018	11,575,000	19,826,810	31,401,810
2019	10,095,000	19,915,735	30,010,735
2020	9,365,000	19,454,235	28,819,235
2021	7,470,000	19,035,860	26,505,860
2022	5,945,000	18,702,985	24,647,985
2023	6,240,000	18,398,359	24,638,359
2024	6,555,000	18,078,484	24,633,484
2025	6,885,000	17,785,335	24,670,335
2026	7,135,000	17,517,281	24,652,281
2027	24,185,000	16,696,362	40,881,362
2028	7,420,000	15,828,723	23,248,723
2029	7,785,000	15,448,598	23,233,598
2030	8,180,000	15,049,474	23,229,474
2031	27,310,000	14,054,213	41,364,213
2032	28,335,000	12,435,509	40,770,509
2033	29,335,000	10,732,501	40,067,501
2034	30,460,000	8,948,818	39,408,818
2035	31,630,000	7,096,673	38,726,673
2036	14,165,000	5,799,025	19,964,025
2037	14,870,000	5,073,150	19,943,150
2038	15,615,000	4,311,025	19,926,025
2039	16,395,000	3,574,375	19,969,375
2040	17,090,000	2,867,000	19,957,000
2041	17,810,000	2,129,425	19,939,425
2042	18,565,000	1,360,375	19,925,375
2043	4,470,000	878,400	5,348,400
2044	4,645,000	696,100	5,341,100
2045	4,830,000	506,600	5,336,600
2046	5,025,000	309,500	5,334,500
2047	5,225,000	104,500	5,329,500
	<u>\$404,610,000</u>	<u>\$312,615,430</u>	<u>\$717,225,430</u>

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

FUNDS AVAILABLE FOR DEBT SERVICE

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>
Total Income	\$450,724,229	\$425,755,909	\$413,680,801	\$447,043,485	\$418,841,237
Less: Operating Exp	<u>345,978,867</u>	<u>332,517,701</u>	<u>319,194,537</u>	<u>314,017,260</u>	<u>296,121,581</u>
Income Available for Debt Service	<u>\$104,745,362</u>	<u>\$93,238,208</u>	<u>\$94,486,264</u>	<u>\$133,026,225</u>	<u>\$122,719,656</u>
Bond Redemption	\$11,575,000	\$12,730,000	\$14,735,000	\$32,115,000	\$28,295,000
Bond Interest	<u>18,949,910</u>	<u>19,025,810</u>	<u>22,420,035</u>	<u>26,626,411</u>	<u>24,112,971</u>
Debt Service Payable on All Debt	\$30,524,910	\$31,755,810	\$37,155,035	\$58,741,411	\$52,407,971
Times Debt Service Covered	3.43	2.94	2.54	2.26	2.34

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

RESOURCES
AS OF DECEMBER 31, 2017

GENERATING FACILITIES	GENERATING UNITS	AGGREGATE NAME PLATE RATING (kW)	APPROX. RATED 4-YR. AVERAGE ANNUAL OUTPUT (1,000 kWh)
Hydro:			
Alder	2	50,000	230,853
LaGrande	5	64,000	370,909
Cushman No. 1	2	43,200	142,697
Cushman No. 2	3	81,000	236,279
Mayfield	4	162,000	775,750
Mossyrock	2	300,000	1,191,716
Wynoochee	1	12,800	24,566
Total Hydro		713,000	2,972,770

Tacoma Power and the City of Seattle Light Department have entered into a 40-year purchase power contract with three Eastern Washington irrigation districts that have combined to develop the Grand Coulee Project Hydroelectric Authority. Tacoma Power and the City of Seattle Light Department share equally the output of the project which has a combined capacity of 128,700 kW and an annual energy capability of about 476,000,000 kWh.

CUSTOMERS BY CLASS	AVERAGE NUMBER BILLINGS	AVERAGE HOURLY ENERGY (kW)
Residential	157,813	1.397
Incidental	15,859	2.355
General	2,558	109.672
Public Streets and Highways	923	3.580
Total System	177,153	3.062

Circuit Miles of Transmission Lines

115 kV	308
230 kV	44

Circuit Miles of Distribution Lines

Overhead	1,174
Underground	848

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

TAXES AND EMPLOYEE WELFARE CONTRIBUTIONS
FOR THE YEAR 2017

FEDERAL

Power Social Security (FICA)	\$7,007,988	
Total		\$7,007,988

STATE OF WASHINGTON

Retail Sales and Use Taxes	2,164,183	
Power Utilities and Business Operations Tax	14,057,018	
Power State Employment Security	151,586	
Total		16,372,787

COUNTY

Lewis County - In Lieu of Taxes	1,562,667	
Mason County - In Lieu of Taxes	170,780	
Pierce County School Support - Eatonville	7,000	
White Pass School Support	113,334	
Mossyrock School Support	98,432	
Morton School Support	2,766	
Lewis County Fire Protection District	11,032	
Pierce County Fire Protection District	21,216	
Pierce County Drainage District	18,748	
Thurston County	2,396	
Total		2,008,371

MUNICIPALITIES

City of Tacoma Power Gross Earnings Tax	32,083,430	
Click!Network Gross Earnings Tax/Franchise Fees	3,285,846	
City of Fife Power Franchise Fee	1,228,892	
City of University Place Power Franchise Fee	1,090,041	
City of Lakewood Power Franchise Fee	888,463	
City of Fircrest Power Franchise Fee	250,361	
City of Steilacoom Power Franchise Fee	5,300	
Total		38,832,333
TOTAL TAXES		<u>\$64,221,479</u>

Taxes as a % of Operating Revenues of \$ 446,343,405 ..	14.39%
---------------------------------------------------------	--------

EMPLOYEE WELFARE CONTRIBUTIONS

Power Industrial Insurance and Medical Aid.....	\$1,379,690	
Power City of Tacoma Pension Fund	9,503,790	
Power Medical/Life Insurance	17,578,632	
TOTAL EMPLOYEE WELFARE CONTRIBUTIONS		<u><u>\$28,462,112</u></u>

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA POWER

2017 ELECTRIC RATES
(Based on 2017 rate schedules)

RATE PER MONTH

Schedule A-1 - Residential Service

Customer Charge	\$13.50 per month
Customer Charge (for collectively metered apartments)	\$11.00 per month
Energy (all energy measured in kilowatt-hours)	\$0.042437 per kWh
Delivery (all energy delivered in kilowatt-hours) .	\$0.034435 per kWh

Schedule A-2 - Low-Income/Elderly/Handicapped Residential Service

Seventy percent (70%) of the monthly bill as
calculated under Section 12.06.160 of the official
Code of the City of Tacoma, known as RESIDENTIAL SERVICE -
SCHEDULE A-1.

Schedule B - Small General Service

Customer Charge	\$20.75 per month
Customer Charge (for unmetered services)	\$16.10 per month
Energy (all energy measured in kilowatt-hours)	\$0.043549 per kWh
Delivery (all energy delivered in kilowatt-hours) ..	\$0.034587 per kWh

Schedule G - General Service

Customer Charge	\$63.00 per month
Energy (all energy measured in kilowatt-hours)	\$0.042964 per kWh
Delivery (all kilowatts of Billing Demand delivered)	\$7.91 per kW

Schedule HVG - High Voltage General Service

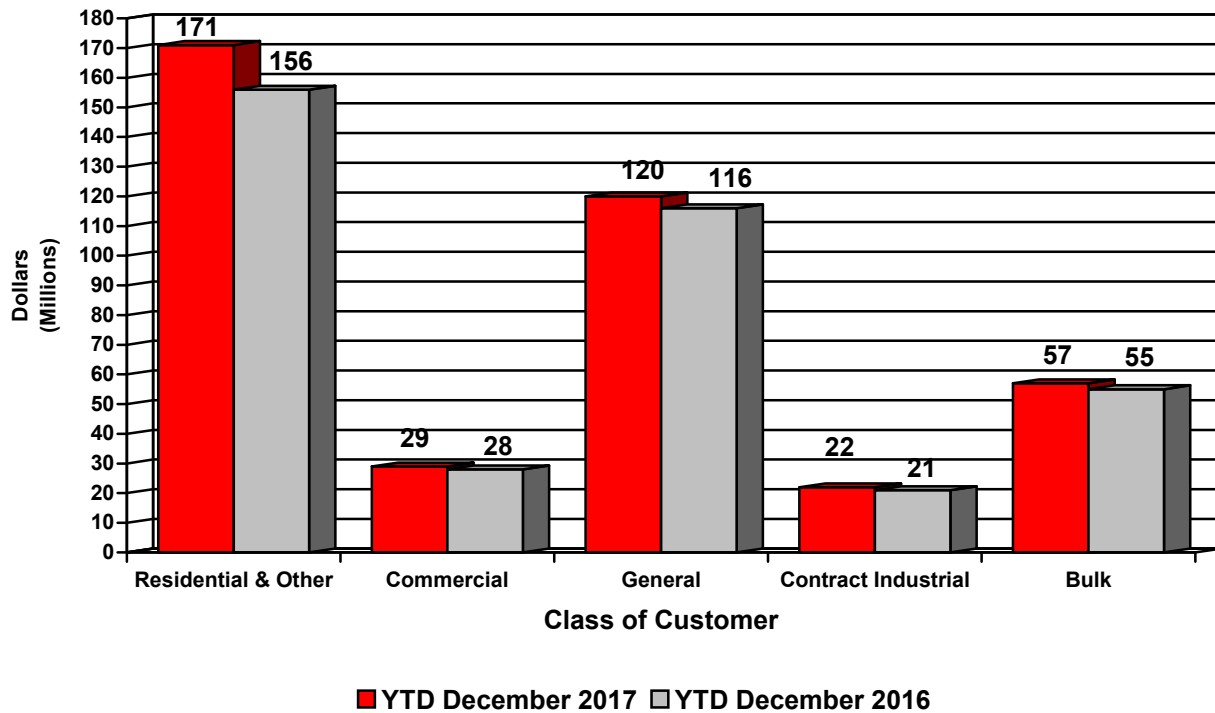
Customer Charge	\$850.00 per month
Energy (all energy measured in kilowatt-hours)	\$0.038295 per kWh
Delivery (all kilowatts of Billing Demand delivered)	\$4.51 per kW

Other schedules also now in effect are:

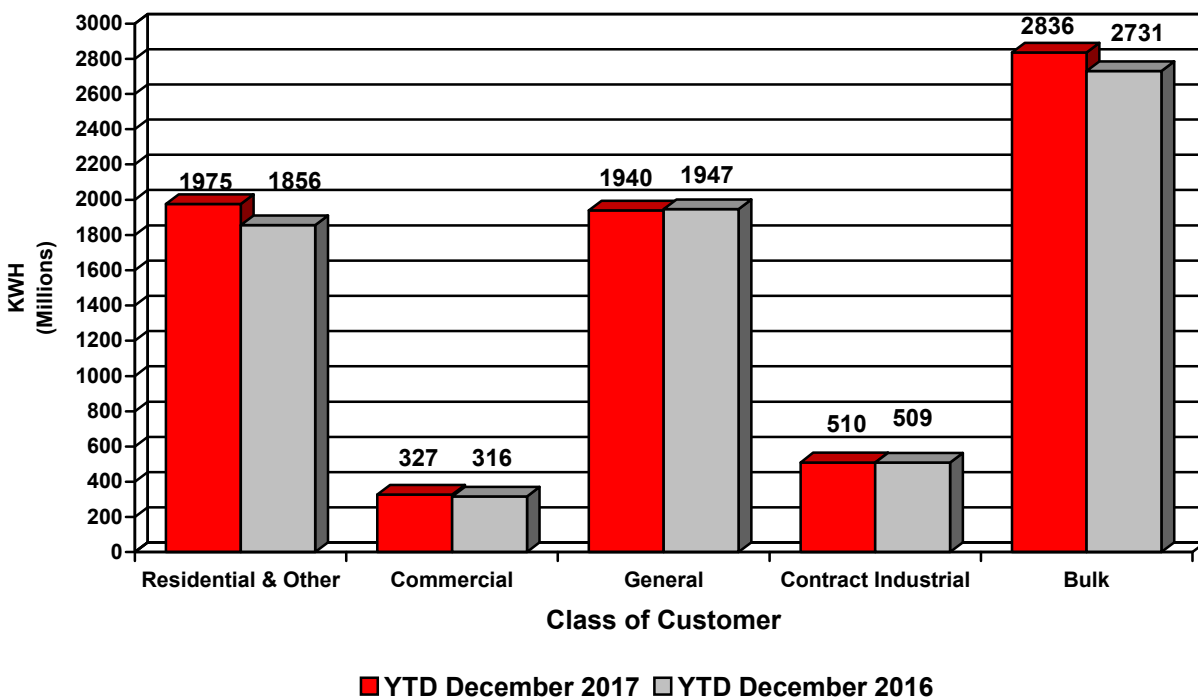
- CP - Contract Industrial Service (major industrial power use -
written contract required)
- H-1 - Street Lighting and Traffic Signal Service
- H-2 - Private Off-Street Lighting Service
- H-3 - Street Lighting Service

Electric rates were established by Ordinance No. 28422 passed April 4, 2017
and became effective April 16, 2017.

SALES OF ELECTRIC ENERGY
Year to Date - December 2017 & 2016

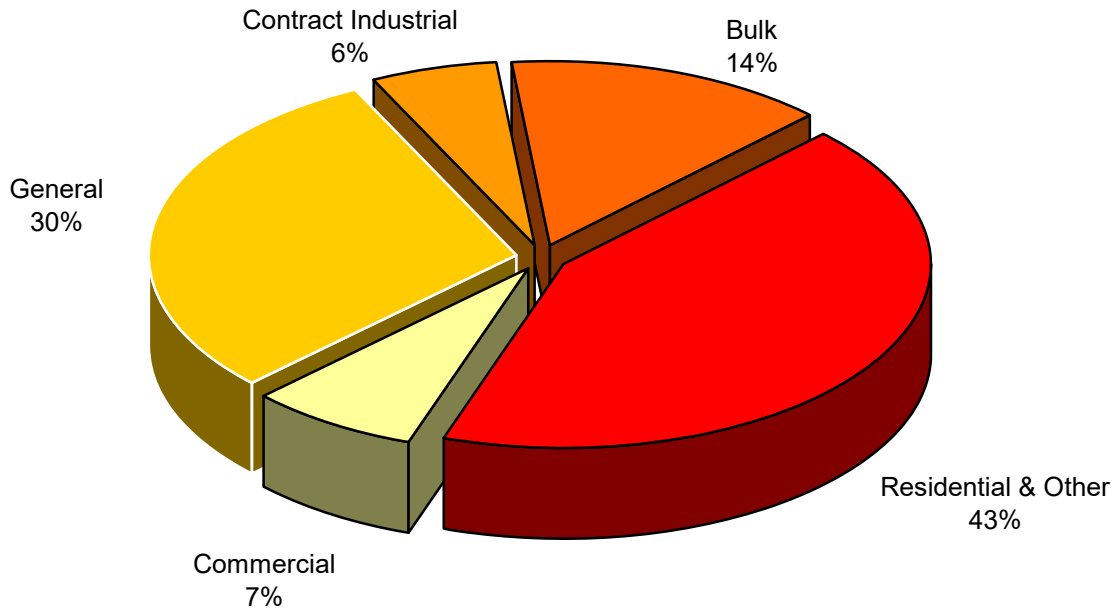


TOTAL POWER BILLED
Year to Date - December 2017 & 2016*

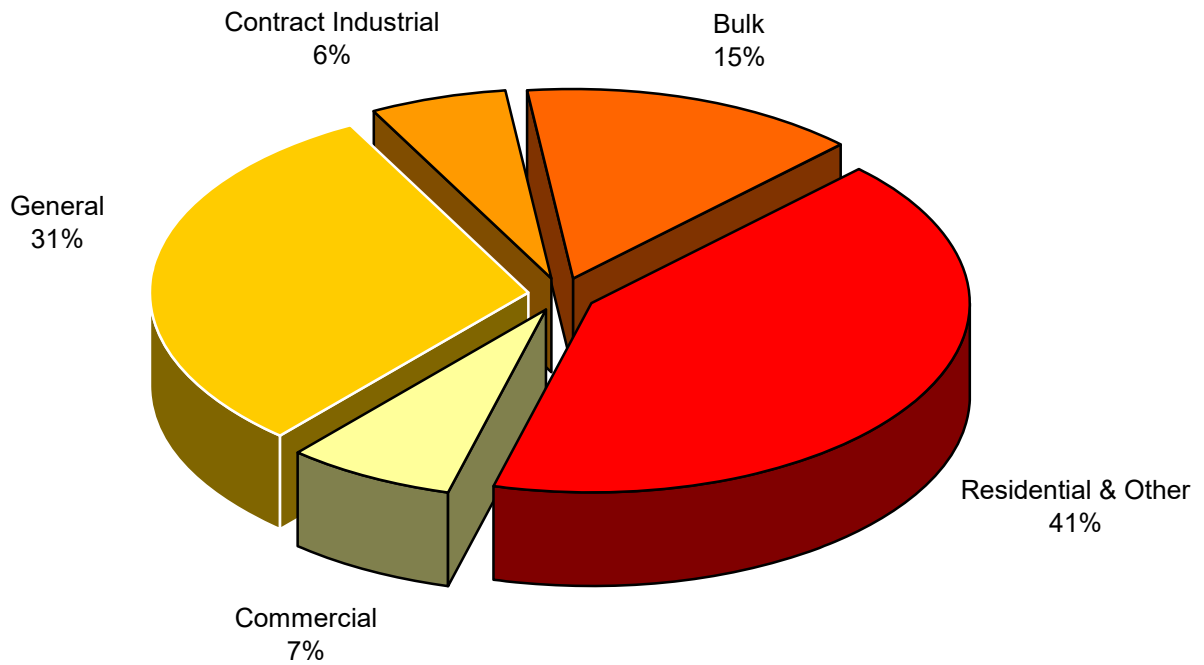


*The 2016 class of customer has been updated to reflect the information in the Gross Generation report.

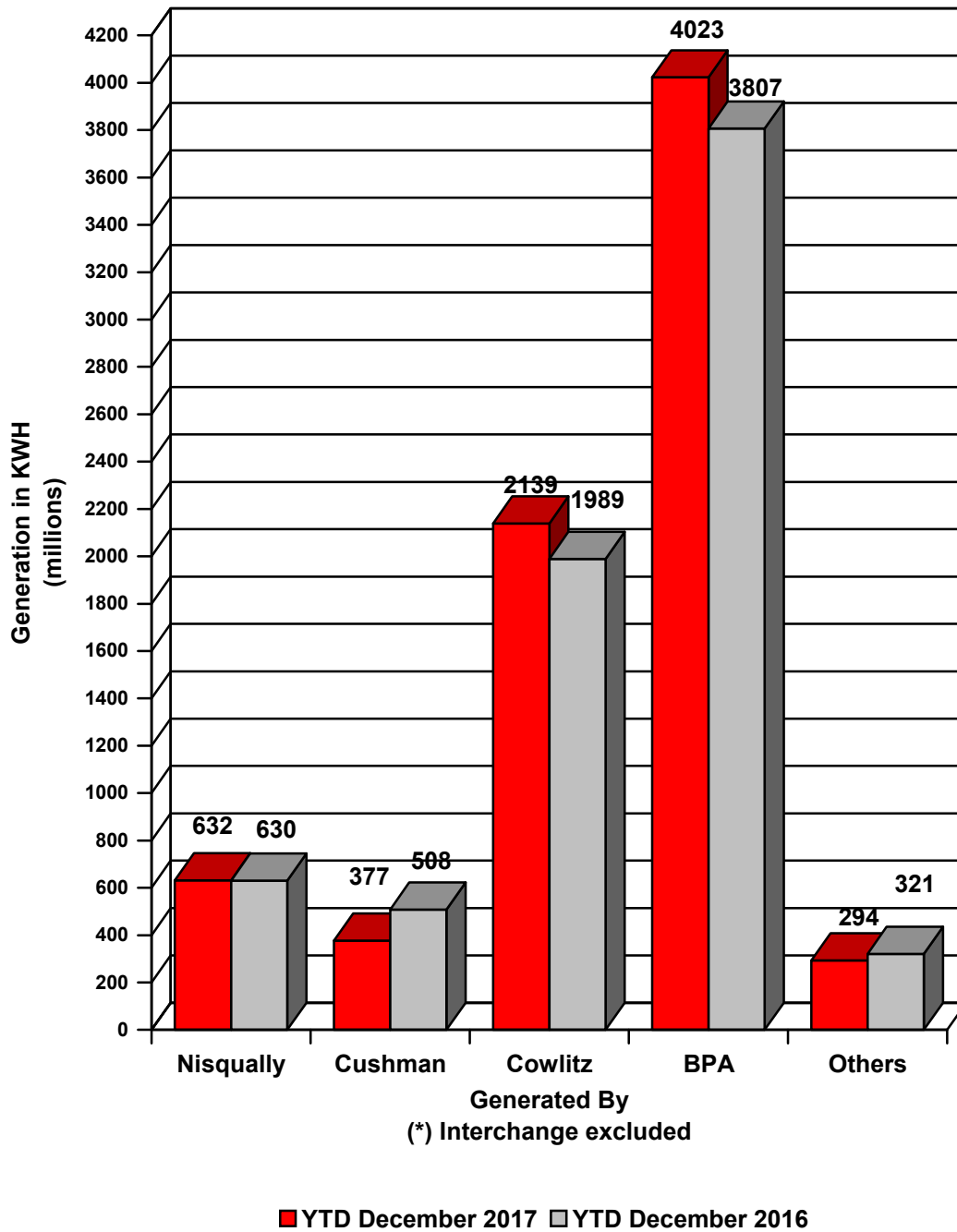
SALES OF ELECTRIC ENERGY
Year to Date - December 2017 (\$401,631,506)



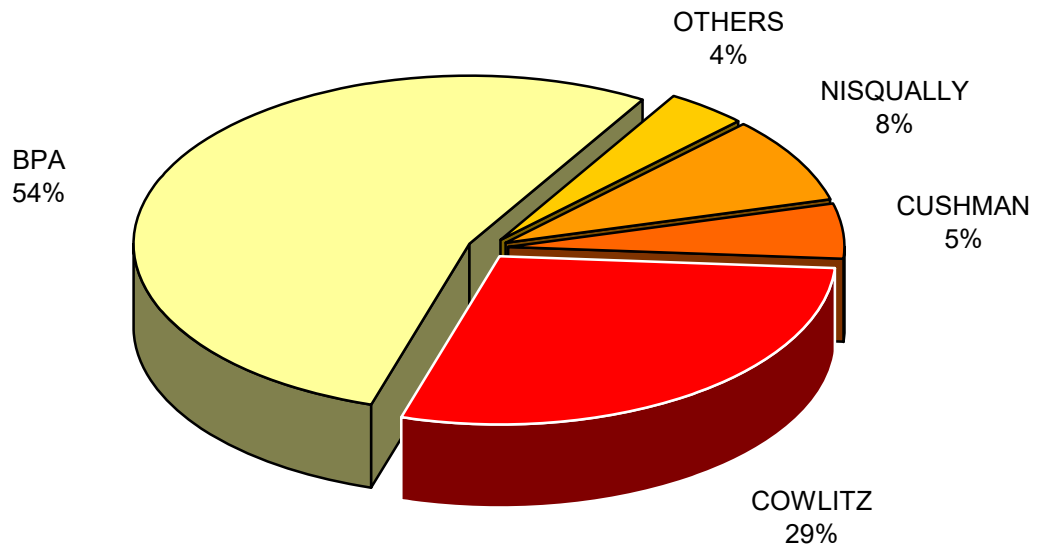
SALES OF ELECTRIC ENERGY
Year to Date - December 2016 (\$374,249,290)



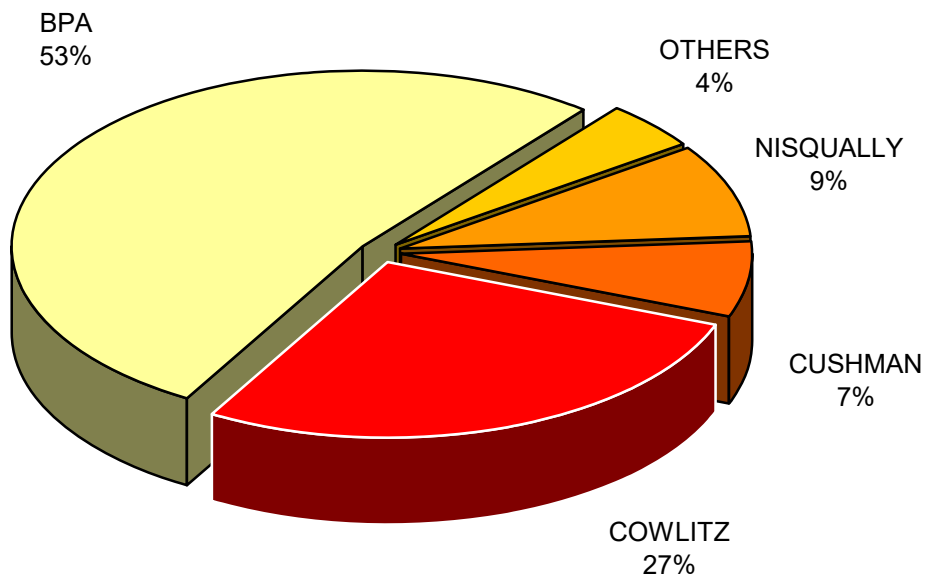
POWER SOURCES (*)
Year to Date December 2017 & 2016



POWER SOURCES (*)
Year to Date - December 2017

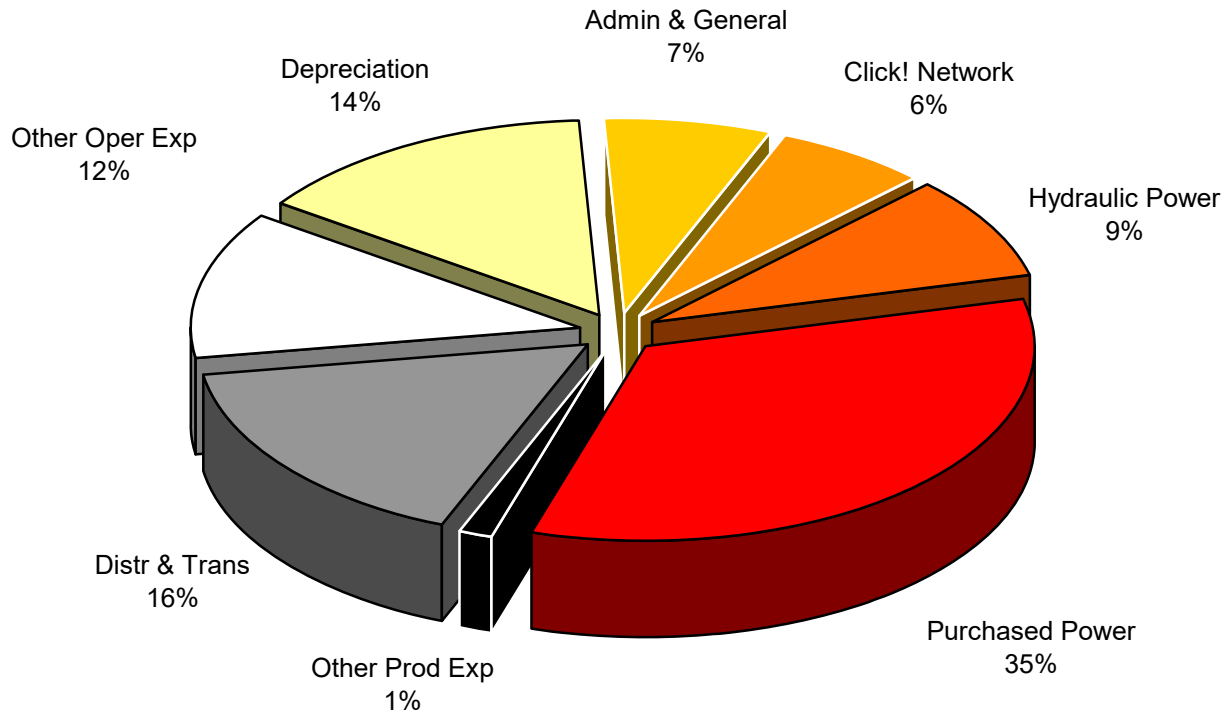


POWER SOURCES (*)
Year to Date - December 2016

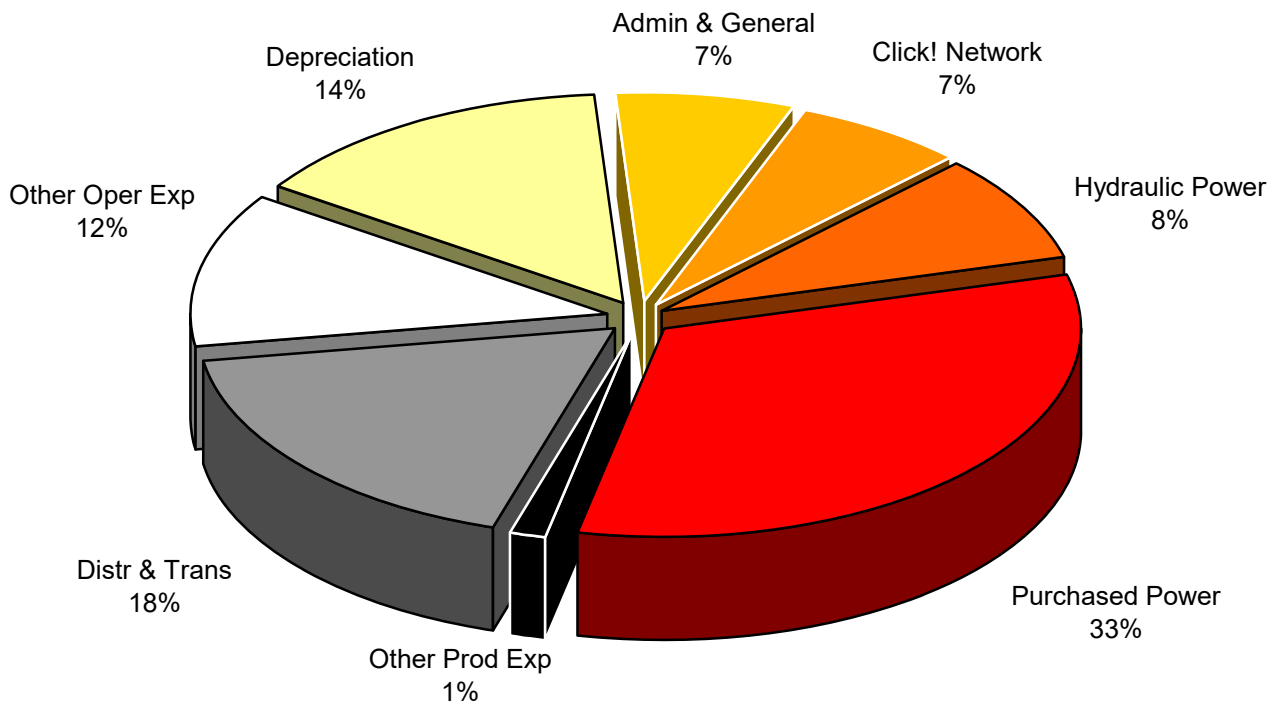


(*) Interchange excluded

TOTAL OPERATING EXPENSES *
Year to Date - December 2017 (\$403,210,178)

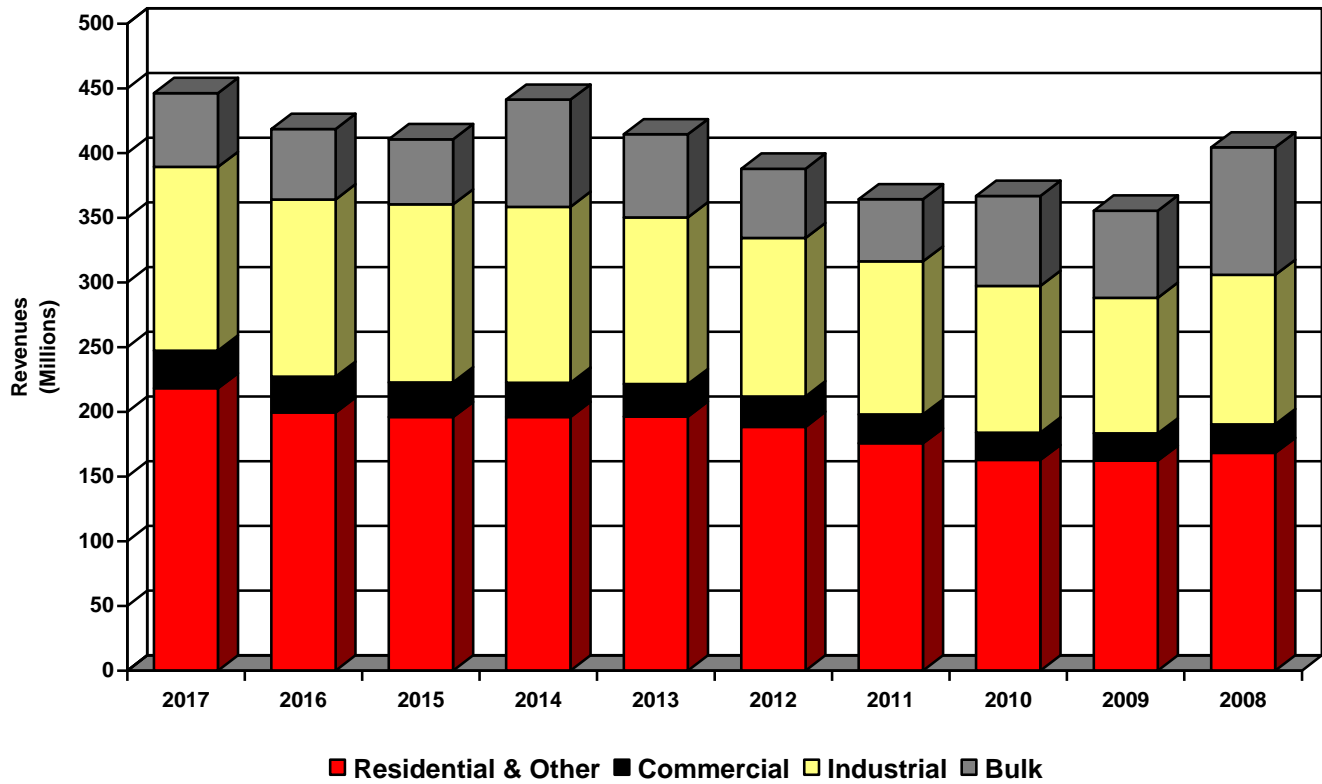


TOTAL OPERATING EXPENSES *
Year to Date - December 2016 (\$388,219,998)

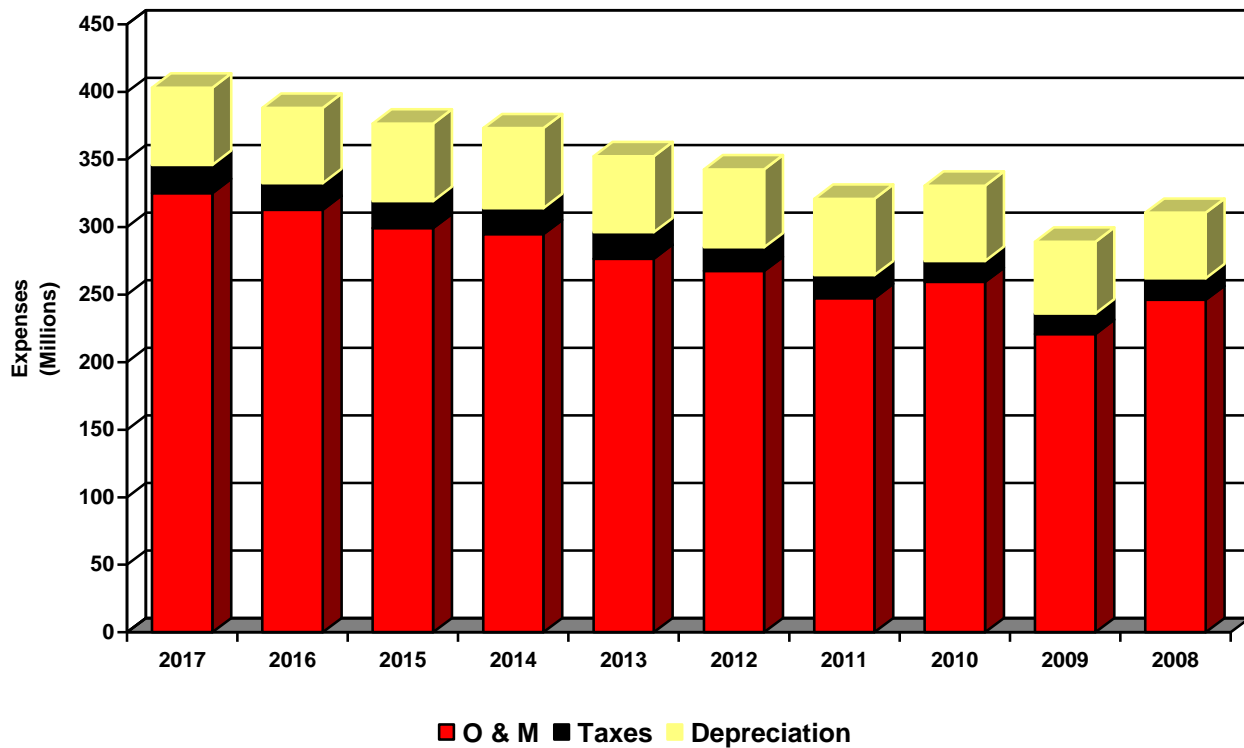


* City Gross Earnings Taxes are not included in Total Operating Expenses.

TEN-YEAR SUMMARY OF OPERATING REVENUES



TEN-YEAR SUMMARY OF OPERATING EXPENSES



2017 SUPERINTENDENT'S REPORT

CLICK!

Financial Status

Click! Network commercial revenues remained level at \$26.5 million in 2017 (\$26.7 million in 2016). The retail cable TV customer base dropped 8.4 percent ending the year with 16,010 active customers, and the Internet cable modem customers served by the two wholesale Internet Service Providers (ISPs) - Advanced Stream, and Rainier Connect, declined by 3.2 percent ending the year with 22,613 active customers. Click! provided 126 broadband transport circuits to Click!'s wholesale service providers allowing them to provide an array of telecommunication services to many businesses in the service area. Additionally, Click! continued to provide the City of Tacoma I-Net services to approximately 134 sites, keeping the cost of telecommunications low for many government entities, and also provided support for just over 14,000 gateway power meter connections.

Franchises

The Cable Television Franchise granted by the City of University Place was renewed in 2017. The Franchise governs use and occupancy of the rights-of-way and sets out obligations which must be fulfilled in order to maintain the right to occupy the rights-of-way and conduct the business of providing cable television services. The Franchise term is ten (10) years with two (2) 7-year automatic extensions available for a total potential term of 24 years. A new Telecommunications Franchise was granted to Click! Network by the City of Puyallup, providing the right to occupy the rights-of-way of the municipality for the provision of telecommunications services only. This Franchise was necessary to accommodate construction of a high-capacity fiber optic connection to the Centeris Data Center.

Cable TV Rate Adjustments

Cable television rate increases were anticipated in 2017 and 2018 and the incremental revenues to be generated by those increases was included in the biennial budget. A rate increase averaging 12.9% was implemented effective March 1, 2017. In October 2017, a rate increase was proposed to become effective January 1, 2018; however, the Public Utility Board postponed consideration of that rate increase indefinitely. Although comparisons of standalone cable television rates have become increasingly difficult in an environment of bundled telecommunications services, all information available indicates that Click! Cable TV rates continue to be lower than national averages for similarly situated cable television systems and are competitive with the rates available for comparable services in the Tacoma market.

Channel Additions

Additions to the channel lineup during 2017 included several networks being broadcast by local stations in the Seattle-Tacoma area. TBD TV, Charge! TV, and Stadium were launched, and Grit TV was discontinued by the broadcasters. UNIVERSO HD, Nat Geo WILD and Sundance were added to the lineup during the year.

Northwest Cable News, Esquire, Universal HD and Chiller discontinued operations in 2017, bringing the total channels carried to 443, consisting of 235 standard definition screens, 144 high definition screens and 64 audio channels. The maximum capacity of 24,000 hours of Video on Demand content was maintained through the year, giving customers the option to view popular programs and movies on a time-shifted basis. Programming from 100 networks was available on mobile devices through Watch TV Everywhere.

New Product Launch

A whole-home set-top box solution from TiVo was commercially launched in late 2016, and an Internet Protocol Video on Demand application was incorporated into the platform in January of 2017. This innovative application delivers programs to the main set-top box in a digital format, allowing the programs to be distributed throughout the home to televisions and mobile devices through Wi-Fi technology. The TiVo whole-home solution has been a popular addition to Click! services, allowing customers the ability to record up to six programs at once and to store one terabyte of programming.

Customer Satisfaction Survey

Customer Satisfaction survey cards were mailed to all new cable TV customers and to all customers who had a service related issue. Click! customer service representatives and technicians received ratings averaging 3.8 and 3.9, respectively, on a scale of 1-4.

In addition, a Brand Awareness Survey conducted on Click! Network's behalf by Washington State University's Social & Economic Sciences Research Center (SESRC) revealed that 44% of the nonsubscribers who responded were not very or not at all familiar with Click! and 51% were not aware that Click! offers internet service through two ISPs, validating Click!'s ongoing efforts to increase awareness of its brand and network services.

New Tools

Click! purchased the EXFO OTDR and Multicom Optical Fusion Splicer to use to expand our network and increase accessibility.

Spectrum Reclamation

In 2017, we moved 4 muxes from 77-80 to remux EIAs 17, 16, 15 and 14, we also moved all SD's out of remux 110 (the QAM ADU channel) and sprinkled them into various other muxes. Channels were moved out of remux 69. There are a few HD muxes that have 2 HDs that we could move a few SDs to and other SD muxes that we could squeeze more SD's in to. We also have some muxes available that are empty but are under the new or affected by the new Standard trap, on these we can move Premium channels to since you have to have standard to buy through to premium.

CLI Program

The Click! technicians found and repaired 3,048 leaks through the Effigis CPAT CLI program.

A vast majority of these were ingress signal leaks that were getting back into our system and causing network interference. The Effigis CPAT system also allows us to find and fix wireless LTE spectrum issues, as they occasionally interfere with the HFC network.

Asset Management Program

During 2017, Click! continued to build its asset list and is prepared to participate in the Tacoma Power's Strategic Asset Management program. Click! also developed a Network Maturity Model, to more effectively manage its asset lifecycles and plan future capital expenditures.

Safety and Work Practices

Safety posters and bulletin board messages were utilized to promote safety awareness. Each business unit held monthly safety meetings and the Click! Safety Committee met quarterly to improve safety related communications. Click! also sends out a monthly security newsletters with current and relevant topics on remaining safe in the digital world.

GENERATION

Hydroelectric Projects

Tacoma Power's hydro plants were available 99.78 percent of the time in 2017 except for scheduled maintenance outages. Annual maintenance was completed on all hydro units. Half of the many kiosks at the hydro projects were rebuilt and modernized with standardized messaging coordinated by Community Media Services.

Cowlitz

Construction of the Cowlitz Falls North Shore Fish Collector was completed on schedule and in time for the fish migration season and the facility successfully operated for the first season. Fish collection results show a significant increase in Spring Chinook collection efficiency. The excitation systems for three units at Mayfield were upgraded to maintain reliability.

Cushman

The first 250,000 sockeye salmon grown at Tacoma's new Saltwater Park Hatchery were released into Lake Cushman. Tacoma obtained 500,000 sockeye eggs from the Baker River Project for hatching and rearing at the Cushman hatcheries and release in 2018. All digital governing systems at Cushman 2 were upgraded to maintain reliability and improve grid response and compliance.

Nisqually

All digital governing systems at Alder were upgraded to maintain reliability and improve grid response and compliance. New safety booms were installed on Alder and LaGrande reservoir for public safety.

Regulatory Compliance and Dam Safety

All dam safety and license compliance requirements were met and submitted to the Federal Energy Regulatory Commission (FERC) on time. All North American electric Reliability Corporation (NERC) compliance obligations were met. Independent Consultant Part 12D Reports and the corresponding Potential Failure Mode Analyses (PFMA) were completed for the Cushman and Wynoochee Projects. Following the Orville Dam incident, the FERC required Tacoma to perform additional PFMAs for both the Cushman No. 1 and Alder Dam Spillways. No significant issues were highlighted with any of our structures. In October we convened the first meeting of the Mossyrock Board of Consultants (BOC) specifically looking at the regional seismicity and the effects that it was having on the spillway piers. The BOC agreed with our current risk mitigation of lowering the reservoir and recommended that we proceed with a more in-depth probabilistic seismic hazard analysis (PSHA) for both Mossyrock and Mayfield Dams. It is the BOC's opinion that having a PSHA performed for the Cowlitz basin is the best way to resolve the seismicity issue well into the next decade. Once the seismicity analysis is complete, we will reanalyze the structural stability of both Mayfield and Mossyrock Dams.

Parks

Tacoma Power's parks served over 264,000 customers in 2017. Even with the challenges of the Riffe Lake drawdown this year Tacoma Power's park customers continue to compliment the beauty of the parks and praise the friendly and helpful staff. Nearly 99 percent of the park customers rated the park staff as helpful in the 2700 surveys that were completed. A few of the many positive customer comments received include: "It's beautiful there" "We LOVE this park! The staff was exceptionally terrific this year" "We have recommended it PLENTY of times!"

Facilities

The TPU campus auditorium remodel was completed in time for the first Public Utility Board meeting of 2018. Security upgrades at many of Tacoma's substations and hydro facilities were completed in preparation for NERC CIP security deadlines. Parking improvements were made to address employee feedback, security and efficiency.

POWER MANAGEMENT

Power Management is responsible for planning for, acquiring, and operating power resources to meet current and future customer power needs in ways that minimize risks and retail costs. 2017 was a great year for Power Management. Highlights include:

1. Power Management, working with Public Works, launched a street light replacement program which will replace about 75% of the City's street lights with highly efficient and highly effective LED technology. This is the culmination of an innovative approach to fund the conversion through a rate process instead of the typical rebate process.
2. Power Management provided net wholesale revenue of nearly \$50 million, with more than \$4 million coming from non-traditional wholesale sales efforts. This was greater than budget and provides significant financial benefit to Tacoma Power customers.
3. Power Management revamped Tacoma Power's Evergreen Options programs by providing grants to non-profit organizations we serve. The first \$50,000 grant was awarded to the Metro Parks Point Defiance Zoo & Aquarium.
4. In response to a resolution by the City Council, Power Management developed a plan to increase adoption of residential solar usage while addressing equity issues for lower income customers.
5. Our section helped secure a grant for fast electric vehicle (EV) charging to be installed at the Lemay Car Museum. We also hosted Tacoma's first "ride and drive" EV event in partnership with the City of Tacoma.
6. Demand response (DR), or voluntary short-term usage reduction by customers, is a power resource tool that is likely to be an important option in the future. In 2017, Power Management participated in a residential water heater DR pilot and conceived an approach to pilot with industrial customer(s) in 2018.
7. Conservation efforts remain the primary power resource that Power Management actively acquires. We recognize conservation as a beneficial service to our customers. In 2017, we significantly surpassed conservation targets and achieved energy savings of over 13 aMW. With an increased focus on reducing costs for non-participants, the resource was acquired at a cost of about \$27/MWh - well below the long-term costs of power resource alternatives.
8. Power Management developed a framework for considering alternatives to contract extensions with Bonneville Power Administration (BPA) when the current contract expires in 2028. This will be one of the most important decisions Tacoma Power will make in the next several years, and this effort moves us toward being well-prepared to make the right choices.

9. To recognize the fact that Conservation Resources Management does more than just acquire conservation resources, the group changed its name to “Customer Energy Programs.” Some additional highlights from that group include:
- a. reducing first-year retail bills for low-income customers by about \$90,000
 - b. creating a pilot program for installing Ductless Heat Pumps (DHP) in manufactured housing, accommodating 1379 lobby visitors with energy questions
 - c. paying over \$385,000 in solar incentive payments
 - d. creating an innovative approach to increase participation in programs designed for low income customers
 - e. presenting to 24 community groups

Customer Energy Programs (CEP)

Tacoma Power meets all of its future load growth needs with conservation. This biennium, we continue to exceed energy conservation targets under Washington’s Energy Independence Act. We acquired energy conservation at an estimated cost of ~ \$29/MWh, which is lower than supply-side resources.

Biennial 2016-17 energy conservation acquisitions are estimated at over 11 aMW, exceeding the 9.4 aMW EIA target. Savings in excess of the target are eligible for use against our targets in the following two biennia subject to stipulations in RCW 19.285.040(c)(i), a Tacoma Power-led amendment to the Energy Independence Act.

CEP completed over 1,750 conservation projects and made over 1,360 solar payments. Our programs were also active in our community, engaging customers at 20 retail and 29 community outreach events.

2017 brought many changes to our programs, including new HVAC measures for the C/I Equipment Rebates and Residential Heating and Weatherization programs and ending our Energy Smart Grocer program by rolling the effort into the C/I Equipment Rebates program. The C/I group completed the contracting phase of the City of Tacoma street lighting projects, with installations starting in late 2017 and expected to complete by end of 2018.

We completed our biennial planning process and published the 2018-19 Conservation Plan. The plan includes several new efforts to help low-income and hard-to-reach customers despite reducing overall low-income spending (reduction in spending was due to several key measures no longer being cost effective).

Energy Resource Planning

Tacoma Power purchases a significant amount of power and transmission from BPA at an annual cost of approximately \$127 million and \$18 million respectively. According to requirements under the BPA Power Sales Agreement and the Tiered Rates Methodology, BPA is required to establish new power and transmission rates every two years. Power Management was an active participant in BPA's BP-18 Wholesale Power and Transmission rate cases this year.

Pursuant to the BPA Administrator's final decision issued in July 2017 Tacoma Power's BPA power and transmission costs increased by 4.1% and 0.2% effective October 1, 2017 for the two-year rate period.

The Planning Unit completed the 2017 Integrated Resource Plan (IRP) – a comprehensive update to the 2015 IRP. The 2017 IRP includes a new resource adequacy assessment, an update on 2015 IRP Action Items, and a compliance status for the Energy Independence Act (2007). This report was a result of careful research, an energetic stakeholder process, a much internal dialogue.

The Planning Unit participated with other Northwest utilities to study two important topics: the impacts of various forms of carbon policy on the environment and utilities, and the value of transportation electrification from ratepayer and societal perspectives. The Planning Unit also worked collaboratively with other utility partners to author a Transportation Electrification Authority bill that would clarify that customer owned utilities have the same authority as investor owned utilities to pursue transportation electrification with direct incentive pilot programs.

The Planning Unit worked with other parts of Tacoma Power to complete a report on potential near term strategies to interact with organized wholesale markets. The study considered functional staffing requirements, computer software and equipment costs for three level of CAISO interaction: participate as a Market Entity, pseudo-tie a unit, and bidding in an external resource.

Tacoma Power was the first Washington utility to join Forth – an electric vehicle advocacy organization which helped Tacoma Power successfully bid for grant funding for the installation of fast-charging infrastructure at the LeMay Car Museum In partnership with many local dealerships and community partners. Tacoma Power held its first ever electric vehicle "Ride and Drive Event" at Point Defiance Zoo & Aquarium.

The Planning Unit completed year-long case study of ductless heat pumps (DHP) in six existing homes. The case-study compares energy use of homes heated with DHPs against the same home heated with electric baseboard heat. Analysis is still under way, but preliminary results suggest heating energy savings of approximately 13% (or 6,400 kWh over a heating season).

This year the Planning Unit completed the biennial service area energy conservation potential assessment. The study indicates 31.7 aMW of achievable economic conservation potential over a 10-year period. For the 2018-2019 compliance biennium, a Tacoma Power target of 6.4 aMW was approved by the TPU PUB in accordance with regulations implementing the Energy Independence Act.

Resource Operations and Trading

*Note: Actual revenue and MWh values may be preliminary. After our official reports have been produced we may need to change them slightly.

Wholesale transactions in 2017 were characterized by similar sales volumes and slightly higher wholesale prices compared to the prior year. Net wholesale power sales were 2.4 million MWh, exceeding the budget estimates of 1.4 million MWh. Annual revenue was \$49.5 million compared to budget estimates of \$33.5 million.

Though the winter was wet overall, January was quite dry. Combined with the region's cold weather in December and January, Tacoma Power drafted our storage reservoirs well below normal levels in January to meet load. The reservoirs were well-positioned to handle the large storms and continual wet weather that hit the region in February.

Snowpack continued to build throughout the season, while inflows continued to be well above normal due to the record-setting wet winter. As a result, we were able to keep all or most of its generating resources near maximum throughout the spring runoff and still refill all of our storage reservoirs. By the end of the snow-build season the snowpack was well above normal, but melted in a relatively smooth pattern, allowing us to capture most of the inflows.

Inflows on the Federal System followed a similar pattern, with high inflows and high snowpack. As a result, flexibility on the system was limited and BPA was purchasing capacity throughout the spring. We were able to provide some of the needed capacity by using the flexibility of our own resources.

With full reservoirs, Tacoma was also able to use the flexibility of its resources to respond to several regional heat waves over the course of the hot, dry summer.

In 2017, the Trading group continued to find innovative ways to monetize the flexibility of its power resource portfolio by participating in emerging markets for various ancillary energy products.

We continued selling energy as a designated Asset Controlling Supplier (ACS), one of only three in the Pacific Northwest. With this designation, any sales made from our resource portfolio are deemed "low carbon" and can be sold at a premium. In 2017, ACS sales resulted in additional revenue of almost \$2.2 million.

We continued to monetize the flexibility of our resource portfolio by selling Capacity products in both the term and day-ahead markets. Sale of these products provided additional revenue of approximately \$1.8 million in 2017.

Tacoma Power also developed a new product that allows a local PUD to procure their reserve requirements from Tacoma Power rather than BPA. Tacoma Power is currently the only third party supplying these products to BPA customers. Sale of this product began in October 2017 and is expected to provide additional revenue of about \$450,000 per year. This program may be expanded to additional customers in 2019.

RATES, PLANNING, AND ANALYSIS

Retail Rates

Tacoma Power completed the public process for rate adjustments. The first adjustment was effective April 16, 2017; the second adjustment will become effective April 1, 2018. Preparation is underway for an expedited rate process and increased public outreach during the 2019/2020 rate adjustment.

Energy Risk Management

Our staff collaborated with Power Management Resource Operations and Planning staff to refine the system model module of the cash-flow-at-risk model. New Key Risk Indicators were developed based on the risk model and presented to the Risk Management Committee (RMC). Staff also implemented an interactive user interface of the risk model (HedgeHog) and developed an initial retail revenue simulation model.

Staff completed draft revisions of the Energy Risk Management Policy and Procedures. New business processes were developed and implemented to align Tacoma Power's energy risk management practices to industry standards for credit risk management and risk controls.

Finance

Tacoma Power took new actions to maintain its financial strength. In September, the utility successfully completed the issuance of \$80 million in new Bonds. The proceeds of the issuance were used to reimburse the short-term note purchase agreement which funded the 2015/2016 construction projects. This allowed the note purchase agreement to be paid down to the minimum draw amount and to start being used to finance construction projects occurring in the 2017/2018 biennium. This is a continuation of the financial planning strategy put in place during the 2015/2016 biennium. In October, Tacoma Power used \$27 million of cash reserves to retire additional Bonds. This allowed for the restructuring of the 2013A Bonds, leveling future debt service and reducing interest payments.

Tacoma Power's credit ratings of AA and AA- were confirmed by both Standard & Poor's and Fitch in 2017 as part of the process to issue new bonds.

Moody's also confirmed their Aa3 rating of Tacoma Power's bonds issued prior to 2017. These ratings will continue to allow Tacoma Power to access low interest rates for future borrowing needs.

Strategy

In 2017, Tacoma Power continued the implementation of the newly developed strategic plan. The Senior Leadership Team met monthly to review the status of initiatives, discuss challenges or roadblocks impacting initiatives, and discuss potential changes. Quarterly, all Section and Assistant Section Managers met to discuss the current status of the strategic plan and how to communicate the plan to the organization.

Tacoma Power has completed several initiatives throughout the year such as, developing an asset management roadmap, developing a TPU-wide leadership program, and finalizing a long-range financial plan. In October, the Senior Leadership Team met to refresh elements of the plan to ensure it remains focused on what is most important for the utility.

Transmission & Distribution

System Reliability

The reliability performance measures of the transmission and distribution system are based on a six-year average, from January 1, 2012 through December 31, 2017. On average, there were 84 customers without service per outage (ACO). The average outage duration for each customer served (SAIDI) was 55 outage minutes per customer. The average frequency of sustained interruption per customer (SAIFI) was 0.56 interruption averages per customer.

Rolling Average	6-Year	SAIDI	SAIFI	ACO
01/1/12-12/31/17		55.4	0.56	84.1
2016 Performance Target		≤ 75	≤ 0.95	≤ 150

The Tacoma native peak load was 993 MW on Thursday, January 5, 2017. The transmission peak was 1,362 MW and occurred on the same day as the native peak.

System Planning and Operations

On December 1, 2017, Tacoma Power began its second year of membership in the Western Frequency Response Sharing Group (WFRSG). As was the case last year, Tacoma's WFRSG membership provided additional support to Tacoma Power's decision to sell 2 MW of frequency response. The group has proven beneficial in helping us to monitor and enhance its frequency response performance. System Operations has been working closely with Generation Production Engineering, Power Management's Resource Operations & Trading, and Energy Management System support staff to discover ways to enhance response and monitoring. This will allow Tacoma Power to be confident in transacting greater amounts of frequency response in the future.

Transmission Service

Tacoma Power continues to provide transmission to three entities, as shown in the table below. Estimated annual revenue from the three entities is about \$7.9 million.

Customer	Reason for Service	MW	Term of Service
Bonneville Power Administration (BPA),	Delivery of BPA power to the Pierce County Mutuels (PCMs)	396	2028
Avangrid Renewables	Delivery of WestRock biomass generation to California	45	2021
Lewis County PUD	Delivery of Cowlitz Falls generation to BPA	70	Concurrent with FERC hydro license

Asset Management

The T&D Asset Management program recognized the need for alignment with Tacoma Power's strategic objectives. As a result, an asset management team, centrally located in Rates, Planning, and Analysis (RPA), formed to assist the business sections in aligning and standardizing Asset Management principles to Tacoma Power's strategic business objectives. A maturity assessment, performed by consulting firm AMCL, identified focus areas of improvement across sections of Tacoma Power. The T&D Asset Management team is working with RPA's Asset Management team to standardize asset management philosophies across committed sections of Tacoma Power while continuing to meet the specific needs of the Transmission and Distribution business units.

The T&D Asset Management (AM) team coordinates the capital budget process for all of T&D, while recommending intervention strategies based on economic modeling for programs such as Pole Replacement. For example, the pole replacement program tests and treats poles, identifying replacements from poles that have failed testing parameters. The pole test and treat program tested 4,642 poles with 3,732 of those poles eligible for treatment. Poles replaced under the Pole Replacement program totaled 680 for 2017.

System Improvements

We constructed and energized Potlatch Switching Station, a four-breaker ring bus, near Union, WA. This switching station segmented the Potlatch lines, which interconnect Cushman Project generation and serve Peninsula Light Company, into the Pearl-Potlatch and Cushman1-Cushman 2-Potlatch lines. Protective relay modifications were additionally completed at Pearl Substation, Cushman 1 Switchyard, and the Cushman 2 plant. Potlatch Switching Station will help to meet NERC TPL standard requirements and to improve availability and flexibility of Cushman Project generation, in addition to other benefits. The project has already realized its anticipated load and generation reliability improvements during a line fault in November.

We also made significant progress toward replacing the lattice structures along North 21st Street and bypassing Cushman Substation. The City Council voted on which properties and existing structures would be placed on the historical registry. We completed steel pole line design and ordered both steel poles and conductor. Conductor and the first batch of steel poles were delivered in 2017. The work order permit was submitted to the City of Tacoma. Replacement of the lattice towers is expected in summer of 2018, with a compact construction window to maintain transmission reliability.

We also completed a customer-funded capacity project to serve James Hardie with a new line extension and substation design. This new substation, dedicated to support James Hardie's facility expansion, will be located near Frederickson, WA. Electrical pre-construction began in late 2017. Energization is expected in the first quarter of 2018.

The customer-funded Taylor Substation civil and electrical design was completed. Civil construction and electrical pre-construction began in late 2017. An easement with the Port of Tacoma for the substation was obtained. This substation will serve PSE's LNG facility. Energization of the substation is expected in mid-2018 in accordance with the customer's request for service.

This past season T&D has seen a large increase in the amount of customer-driven construction over previous years. This resulted in the dedication of approximately 30,000 labor hours in 2017 from line construction crew on customer driven construction.

Electrical Services

New Services and Utility Staff Support groups completed design, agreements, and work orders for \$1,865,000 in residential projects and \$1,939,000 in commercial projects. Projects include New Cold, Cedar Springs, and Point Ruston.

Electrical Inspection and Utility Staff Support groups issued 12,292 electrical permits and performed 19,088 electrical inspections for total permit revenue of \$1,926,631. Utility Staff Support assisted 3,785 walk-in customers and supported 20,642 customer phone calls in the Electrical Permitting group.

Safety and Work Practices

T&D continues to work towards a zero incident workplace with a reduction in the number of serious workplace injuries. Training was provided to employees to focus on injury reduction strategies for specific body parts. Loss time accidents in T&D were reduced by over 65%.

The 360° Vehicle Walk-Around Program was developed and implemented. This program was put in place to mitigate motor vehicle collisions when vehicles are moved after being parked. This program has subsequently been adopted by Power and Water.

Employee Resources/Development

T&D Training and Development managed three apprenticeship programs, and provided training and work experiences to 33 apprentices and trainees in four areas: line (16); substation (12); advanced meter/relay technician (1); and system dispatcher (4). In addition to managing programs, T&D also conducted a recognition event to honor five Transmission & Distribution employees who graduated from their respective apprenticeships/advanced training programs.

Emergency Management

The Tacoma Power Emergency Response Plan (ERP) now includes a standardized Incident Command Structure (ICS) template. The template includes ICS Organizational Charts, an Emergency Contact List and FEMA forms all in one spreadsheet. This template can be used to report to FEMA when we apply for emergency compensation.

Collective Bargaining

During 2017 Tacoma Power Management and IBEW Local 483 with several Labor Representatives put great effort into finding agreement on the 483 Power Collective Bargaining Agreement that affects all of the field crews in T&D as well as dispatch and Generation. Negotiations started off with great hope of a short bargaining session but agreement on some key issues required many long sessions of negotiation. With the help of a PERC Mediator agreement was achieved on a fair contract including agreement to a four year term.

UTILITY TECHNOLOGY SERVICES

Utility Technology Strategy & Planning

In 2017, Utility Technology Services (UTS) received PUB approval for a special project of limited duration for a TPU-wide program to deploy Advanced Metering Infrastructure (AMI) across its entire water and electric service territories. The Advanced Metering Infrastructure Program's objective is to plan, design, build, implement, and stabilize a comprehensive advanced metering solution for TPU that will be critical for delivering a range of benefits to the utilities and their customers. The AMI Program is now focused on technology vendor procurement activities which are expected to be completed in 2018.

In 2017, UTS also prepared strategies for digital engagement and operational analytics which are helping to shape strategic initiatives around these emerging capabilities for TPU and the Utilities industry at large.

Employee Engagement

UTS' Employee Engagement Team focused on the establishment of four new initiatives in 2017: Employee Recognition, Information Sharing, Knowledge Transfer, and Having Fun! A UTS News Team has been established to improve communication across UTS and will enable more effective communication via channels which employees prefer.

Operational Efficiency

Tacoma Power's Outage Management System added the functionality to automate the initial Estimated Time of Restoration (ETR) to the public facing Tacoma Power Outage Map. This automation replaces a previous manual process, and provides an initial ETR much quicker for the customer.

The Interactive Voice Response (IVR) platform was enhanced to provide reporting capabilities in order to generate Key Performance Indicators (KPI) to measure the effectiveness of the voice-processing contact channel that includes Customer Services, Power's Outage Management System (OMS) and Electrical Inspection.

Customer Services replaced their legacy database for the intake, review, tracking and reporting for Low-Income Discount Rate applications and other low-income programs with a robust, reliable, and scalable cloud solution offering more features and functionality.

Customer Services' payment channels (cashiering, IVR, and Payboxes) were upgraded to accept the new MasterCard BIN number and Discover Cards. This upgrade was implemented prior to July 1, 2017, thus meeting MasterCard's compliance deadline in accepting the new card number.

To further improve project delivery and consistency, the Project and Portfolio Management Office enhanced and matured a number of key project/portfolio tools and processes, including financial management techniques and processes, implementing a resource capacity and demand tool and supporting processes, establishing a benefits framework and project approval gates, and enhanced portfolio and project reporting.

In 2017, UTS placed a greater emphasis on establishing and maintaining a Service Management Center of Excellence for Tacoma Public Utilities through the development of a Service Management Office (SMO). The SMO was tasked with providing leadership and oversight of the Tacoma Public Utilities IT Asset Management (ITAM), IT Service Management (ITSM), and UTS Contract/Vendor Management programs. The SMO leads the organization to develop the strategy, plans and operational capability necessary to assure the effective and efficient delivery of IT services to the business.

Technology Advancements

A Wide Area Network (WAN) project kicked off in 2017 with the aim of increasing bandwidth and realizing cost savings through collaboration with neighboring utilities.

These benefits are being realized in two phases. First, with the execution of an agreement with Lewis County PUD for dark fiber, TPU is positioned to replace legacy network transport equipment, and allows UTS to deliver a fully protected fiber ring with true physical redundancy. By upgrading our technology and creating a fiber optic redundant route, TPU will increase its network reliability significantly at each substation, natural resource facility, and hydro facility included in this first phase.

For phase two, TPU executed an interlocal agreement with Mason County PUD No.3. Through this agreement, UTS is able to provide enterprise level connectivity and significantly increase bandwidth for the entire Cushman project. Additionally, the equipment currently deployed at the remote locations can be consolidated back at the TPU main campus enabling UTS to streamline a variety of routine maintenance tasks. By completing this phase, there is potential for TPU to enter into agreements and begin collecting non-rate revenue by leveraging these new communications resources.

A contract was awarded to Utilicast to provide system integration services for the Energy Management System (EMS) replacement project. The EMS replacement team began work on the aggressive 18-month schedule and completed several important milestones including the installation of the new program development system, two of three contracted data conversions, and initial point-to-point testing of communications to the SCADA endpoint devices. In October, a team of individuals from Utilicast, UTS, and T&D traveled to Minnesota for two weeks to perform Factory Acceptance Testing of the new EMS.

The main campus data center project was approved and work began to convert the Energy Control Center computer room into a data center that included installing a second uninterruptable power supply and upgrading the current HVAC cooling system. The project will allow the utility to consolidate most of its computing assets into

a single space with better system resiliency and energy saving designs.

The private cloud infrastructure operated by UTS was further partitioned into separate resource pools for the separate deployment of operational and business systems to enable higher resource utilization and efficiency. The staffs supporting both business and operational systems infrastructure were merged into a single group for better collaboration while maintaining workforce boundaries.

In 2017, UTS successfully developed and implemented a new and robust IT Service Management toolset called “HelpHub” to assist in improving UTS’ IT service delivery. A new web-based customer portal was designed with input from customers that made it easier for Tacoma Public Utilities employees to request technology services, report technological incidents or problems to UTS staff. The back end of this tool has allowed UTS staff to better manage and track the different types of service requests and ensure customer technological needs are met. Plans for integrating and configuring the IT asset management toolset, work order module, event management, service level management and change management are underway and scheduled for implementation in 2018. This system is scalable and can be configured to include other service delivery organizations such as facilities.

To ensure ongoing sustainability of the Utility Bill technology, the PMO successfully delivered the Utility Bill Migration project. In addition to ensuring vendor supportability of backend technologies, the project benefits additionally included the migration of all TPU forms (invoices, warning notices, meter reading schedules, etc.). The customer invoice received a makeover that incorporated consumption data, cost per day averages and a visual meter graph.

Cybersecurity

In 2017, UTS established a new Cybersecurity group to lead TPU’s Cybersecurity Program. This group is working across TPU to improve cybersecurity controls, policies, procedures, and cybersecurity awareness.

UTS completed a project to connect the generation plant control system development lab to the operational network to allow for security updates to be tested prior to the deployment to protect the systems located at the hydroelectric projects. In addition, a remote access and password vaulting solution was deployed to provide secure, monitored outside access to employees or contractors working within the utility operational systems.

In support of the new Energy Management System upgrade, UTS procured a new Security Event and Information Management (SEIM) system. The new best-in-breed SEIM will increase the security awareness while reducing the amount of effort required to administer and configure the system compared to the current system used by UTS.

Regulatory

Tacoma Power subject matter experts vetted 22 Operations & Planning (O&P) Standards through the Standard Change Organizational Review and Evaluation (SCORE) process to ensure compliance prior to their 2017 effective dates. Personnel also completed a significant amount of work to meet new Critical Infrastructure Protection (CIP) Low-Impact requirements that became enforceable on April 1, 2017.

Reliability & Compliance (R&C) facilitated the review and approval of approximately 150 compliance documents and performed approximately 50 Internal Audits. Additionally, R&C gathered information and created a plan to update all compliance documentation and evidence related to the new EMS installation.



The City of Tacoma does not discriminate on the basis of disability in any of its programs, activities, or services. To request this information in an alternative format or to request a reasonable accommodation, please contact the City Clerk's Office at (253) 591-5505. TTY or speech to speech users please dial 711 to connect to Washington Relay Services.

ANNUAL

TACOMA WATER

2017

**FINANCIAL
REPORT**



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DEPARTMENT OF PUBLIC UTILITIES

CITY OF TACOMA

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TACOMA WATER

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FINANCIAL DATA

Report of Independent Auditors

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

Report on the Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Department of Public Utilities, Water Division (the Division), which comprise the statements of net position as of December 31, 2017 and 2016, 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, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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 City of Tacoma, Department of Public Utilities, Water Division as of December 31, 2017 and 2016, and the results of its operations and 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, schedule of proportionate share of net pension liability, and schedule of employer contributions, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The statistical data on pages 50 through 69 and the superintendent's report on pages 70 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 basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated April 20, 2018, on our consideration of the City of Tacoma, Department of Public Utilities, Water Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.



Tacoma, Washington
April 20, 2018

MANAGEMENT'S DISCUSSION AND 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, 2017, 2016, and 2015. 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, 2017 and 2016, 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.

Financial Highlights

- The net position of Tacoma Water was \$556.7 million in 2017, \$549.7 million in 2016 and \$542.5 million in 2015. Of these amounts, \$58.1 million in 2017, \$57.1 million in 2016, and \$53.8 million in 2015 is reported as Unrestricted net position and is available to finance day-to-day operations without constraints established by debt covenants or other legal requirements.
- Tacoma Water's total net positions increased by \$7.1 (1.3%) million in 2017, \$7.2 (1.3%) million in 2016 and \$24.7 (4.8%) million in 2015.
- Operating revenues were \$94.6 million in 2017, an increase of \$1.8 million (2.0%) compared to 2016 which is primarily due to an average rate increase of 4.0% and a decrease in consumption. Operating revenues were \$92.8 million in 2016, a decrease of \$5.3 million (5.4%) compared to 2015. While sales and other revenue increased by \$1.5 million from 2015 to 2016, contract resource obligation revenue decreased by \$6.9 million. The decrease in contract resource revenue is primarily

due to a shift in focus from building the Green River Filtration Facility to operating the facility and the partners were billed accordingly.

- In 2017, Tacoma Water's net utility plant of \$873.5 million represented a decrease of \$6.0 million (0.7%) compared to the 2016 \$879.5 million balance. This is primarily due to a net increase of \$24.4 million in plant in service offset by an increase in accumulated depreciation of \$21.8 million and a decrease in construction work in progress of \$8.7 million. In 2016, Tacoma Water's net utility plant of \$879.5 million represented a decrease of \$5.2 million (0.6%) compared to the 2015 \$884.7 million balance. This is primarily due to a net increase of \$15.5 million in plant in service offset by an increase in accumulated depreciation of \$20.6 million.

Overview of the Financial Statements

Tacoma Water reported net operating income of \$16.8, \$17.4 and \$34.6 million in 2017, 2016 and 2015 respectively. In 2017, operating revenues increased by \$1.8 million and operating expenses increased \$2.5 million. For 2016, operating revenues decreased by \$5.3 million and operating expenses increased \$11.8 million.

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

Operating Results (In thousands)

Category	2017	2016	2015	17/16 Increase (Decrease)	16/15 Increase (Decrease)
Operating Revenues	\$ 94,644	\$ 92,802	\$ 98,139	\$ 1,842	\$ (5,337)
Operating Expenses	77,866	75,356	63,588	2,510	11,768
Net Operating Income	16,778	17,446	34,551	(668)	(17,105)
Net Non-Operating Income (Expense)	(15,342)	(17,395)	(15,595)	2,053	(1,800)
Capital Contributions	9,139	10,274	9,053	(1,135)	1,221
Federal BAB Subsidies & Grants	3,582	3,579	3,610	3	(31)
Transfers Out	(7,093)	(6,754)	(6,874)	(339)	120
Change in Net Position	\$ 7,064	\$ 7,150	\$ 24,745	\$ (86)	\$ (17,595)

Gallons Billed
(In millions)

Type of Customer	2017	2016	2015	17/16 Increase (Decrease)	16/15 Increase (Decrease)
Residential	8,251.3	8,371.3	8,483.5	(120.0)	(112.2)
Commercial & Industrial	8,838.2	8,763.4	9,140.7	74.8	(377.3)
Wholesale	935.5	1,275.6	1,881.1	(340.1)	(605.5)
Total	18,025.0	18,410.3	19,505.3	(385.3)	(1,095.0)

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	2017	2016	2015	17/16 Increase (Decrease)	16/15 Increase (Decrease)
Net Utility & Non-Utility Plant	\$ 874,012	\$ 880,041	\$ 885,214	\$ (6,029)	\$ (5,173)
Current & Other Assets	229,630	228,621	212,475	1,009	16,146
Total Assets	1,103,642	1,108,662	1,097,689	(5,020)	10,973
Deferred Outflows	10,034	10,623	4,003	(589)	6,620
Total Assets & Deferred Outflows	\$ 1,113,676	\$ 1,119,285	\$ 1,101,692	\$ (5,609)	\$ 17,593
Net Position:					
Net Investment in Capital Assets	\$ 445,996	\$ 446,518	\$ 446,538	\$ (522)	\$ (20)
Restricted for:					
Water Capital and Sys Dev Chg	50,149	43,534	39,439	6,615	4,095
Debt Service Funds	2,506	2,496	1,852	10	644
Net Pension Asset	-	-	881	-	(881)
Unrestricted	58,066	57,104	53,792	962	3,312
Total Net Position	556,717	549,652	542,502	7,065	7,150
Long-Term Debt	463,619	478,617	478,401	(14,998)	216
Current & Other LT Liabilities	55,981	54,919	44,283	1,062	10,636
Total Liabilities	519,600	533,536	522,684	(13,936)	10,852
Deferred Inflows	37,359	36,097	36,506	1,262	(409)
Total Net Position, Liabilities & Deferred Inflows	\$ 1,113,676	\$ 1,119,285	\$ 1,101,692	\$ (5,609)	\$ 17,593

Revenues

Tacoma Water's operating revenues were \$94.6 million in 2017, an increase of \$1.8 million (2.0%) compared to 2016. Sales of water increased in 2017 by a net of \$2.0 million of which \$3.7 million is due to an average rate increase of 4.0% effective April 1, 2017 and a decrease in usage of \$1.7 million. This is offset by a decrease in contract resource obligations of \$0.2 million from Regional Water Second Supply (RWSS) Partners to reimburse Tacoma Water for operating & maintenance related expenses.

Tacoma Water's operating revenues were \$92.8 million in 2016, a decrease of \$5.3 million (5.4%) compared to 2015. Sales of water increased in 2016 by a net of \$1.0 million of which \$4.2 million is due to an average rate increase of 4.0% effective January 1, 2016 and a decrease in usage of \$3.2 million. This is offset by a decrease in contract resource obligations of \$6.9 million. RWSS Partners reimbursed Tacoma Water for the final expenses related to building the Green River Filtration Facility in the first quarter of 2016. Contract resource revenue for the remainder of the year includes recovery of primarily operating & maintenance related expenses, resulting in a net reduction.

The following table highlights water sales by type of customer for 2017, 2016 and 2015.

Water Sales (In thousands)

Type of Customer	2017	2016	2015	17/16 Increase (Decrease)	16/15 Increase (Decrease)
Residential & Domestic	\$ 52,540	\$ 50,742	\$ 48,263	\$ 1,798	\$ 2,479
Commercial & Industrial	17,409	17,559	17,234	(150)	325
Special Rate	6,322	5,846	5,951	476	(105)
Wholesale	3,069	3,972	5,192	(903)	(1,220)
Unbilled Revenue	660	(138)	319	798	(457)
Total	<u>\$ 80,000</u>	<u>\$ 77,981</u>	<u>\$ 76,959</u>	<u>\$ 2,019</u>	<u>\$ 1,022</u>

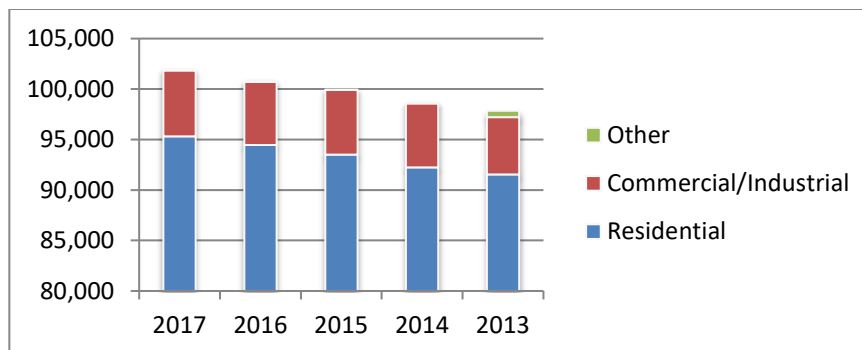
Approximately 65.7%, 65.1% and 62.7% of water sales were to residential and domestic customers in 2017, 2016 and 2015 respectively. Commercial and industrial sales were 21.8%, 22.5% and 22.4% of total sales for each year. Special rate sales were 7.9%, 7.5%, 7.7% of sales respectively.

Customers

Over the last five years, the overall number of customers has remained relatively stable. In 2017, 93.6% of all customers were residential compared to 93.8% in 2016 and 93.6% in 2015. Commercial and industrial customers were 6.4% of all customers in 2017, 6.2% in 2016 and 6.4% in 2015.

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

Number of Customers

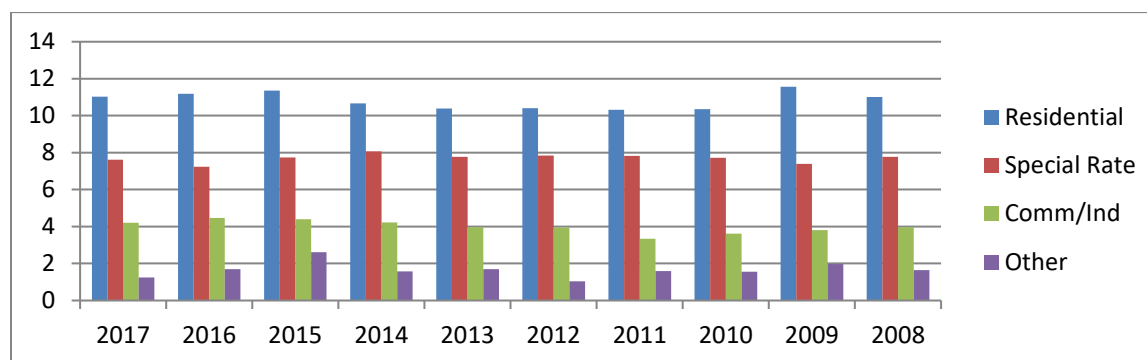


Water Users

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 2017, 2016 and 2015 residential customers used 11.0 million CCF (45.8%), 11.2 million CCF (45.5%) and 11.3 million CCF (43.5%) of total consumption respectively. Special Rate customers used approximately 7.6 million CCF (31.6%), 7.2 million CCF (29.4%) and 7.7 million CCF (29.7%) respectively. Commercial and industrial customers used 4.2 million CCF (17.5%), 4.5 million CCF (18.2%) and 4.4 million CCF (16.8%) respectively. The remaining 1.3 million CCF (5.2%), 1.7 million CCF (6.9%) and 2.6 million CCF (10.0%) 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 2017, operating expenses increased \$2.5 million (3.3%), compared to an increase of \$11.8 million (18.5%) in 2016. Two major projects took place in 2017 contributing to an increase in operating expense of \$0.8 million: the Integrated Resource Plan (IRP) and the Water System Plan. The IRP will be used by Tacoma Water to enhance the ability to manage water resources. The plan will evaluate Tacoma Water's groundwater sources and help to decide where additional focus may be needed. In addition, the IRP will develop a water supply yield model that will look at both short and long-term use and be able to look at yield under several different scenarios. The Department of Health requires the creation of a Water System Plan every 10 years. Tacoma Water uses input from stakeholders and the public to create the plan which is meant to provide an overview of the system as well as outline the different parts of the system, changes from the last plan and projects planned for the future. The increase affected Source of Supply by \$0.3 million, Treatment by \$0.1 million, and Admin & General by \$0.4 million.

Depreciation expense increased by \$0.2 million (0.9%) in 2017 due to a net increase in depreciable assets of \$15.5 million during 2016.

Pension expense increased \$0.6 million in 2017. This expense was allocated across the Division causing increases in labor expense as follows: Source \$0.1 million, Treatment \$0.1 million, Distribution \$0.3 million, and Admin & General \$0.1 million.

In 2016, operating expenses increased \$11.8 million (18.5%), compared to an increase of \$5.0 million (8.6%) in 2015. Source of Supply saw expenses returning to normal in 2016. Increased use of in-town wells due to the 2015 drought caused a labor shift from other sections of Tacoma Water to focus on operating the wells. In 2016, the wells were used significantly less which resulted in a decrease in expenses of \$0.5 million (6.4%) when compared to 2015. Similarly, the cost to pump the well water decreased by \$0.3 million (34.0%), as well as the costs related to Transmission and Storage which decreased by \$0.1 million (1.9%).

Treatment experienced an increase of \$1.8 million (37.1%) compared to 2015 as expenses shifted back from in-town supply sources to the planned operation of the Green River Filtration Facility (GRFF). Although the GRFF came online in 2015, due to the statewide drought and the requirements to ensure adequate fish passage in the Green River, it was used less than expected. When compared to 2015, chemical expenses increased by \$0.6 million, solid handling costs increased by \$0.1 million and electricity increased by \$0.3 million. Also contributing nearly \$0.1 million to the increased treatment costs was the response to lead detected in our water system in April of 2016.

Expenses related to the Distribution system increased by approximately \$2.0 million (16.6%) in 2016. This is primarily due to a shift from capital work to a focus on operations and maintenance, which accounted for an additional \$0.4 million in labor and equipment charged to operating expenses rather than capital projects. Also contributing to the variance in Distribution was \$0.3 million that was spent in 2016 on condition assessment for distribution lines.

Due primarily to an increase in assessments, Administrative and General and Customer Accounting expenses experienced increases of \$1.6 million (18.3%) and \$0.5 million (11.6%) respectively.

Depreciation expense increased by \$6.7 million (39.3%) in 2016 due to a net increase in depreciable assets of \$192.3 million during 2015.

GASB 68, *Accounting and Financial Reporting for Pensions*, resulted in an increase in expense of \$1.4 million in 2016. This expense was allocated across the Water sections as follows: Source \$0.3 million, Treatment \$0.2 million, Transmission \$0.1 million, Distribution \$0.6 million, and Admin & General \$0.2 million.

The following table highlights Tacoma Water's operating expenses for 2017 – 2015.

Operating Expenses (In thousands)					
Category	2017	2016	2015	17/16 Increase (Decrease)	16/15 Increase (Decrease)
Production Expense					
Source of Supply	\$ 7,657	\$ 7,541	\$ 8,056	\$ 116	\$ (515)
Water Treatment	7,144	6,794	4,957	350	1,837
Total Production Expense	14,801	14,335	13,013	466	1,322
Power Pumping Expense	558	559	847	(1)	(288)
Transmission & Storage Expense	2,633	2,770	2,823	(137)	(53)
Distribution Expense	14,691	13,882	11,902	809	1,980
Customer Accounting & Service	5,017	4,830	4,327	187	503
Taxes	4,776	4,639	4,681	137	(42)
Depreciation	24,038	23,823	17,103	215	6,720
Administrative & General	11,352	10,518	8,892	834	1,626
Total Operating Expenses	<u>\$ 77,866</u>	<u>\$ 75,356</u>	<u>\$ 63,588</u>	<u>\$ 2,510</u>	<u>\$ 11,768</u>

Capital Assets

Tacoma Water invests in a broad range of utility assets and at the end of 2017 had \$873.5 million in net utility plant, a decrease of \$6.0 million from 2016.

Plant in Service increased \$24.4 million compared to 2016. This increase is largely due to the allocation of \$12.2 million of capitalized interest to assets. Also in 2017, 9.5 miles of water main were added or replaced and construction was completed on 25 private contracts resulting in 7.34 miles.

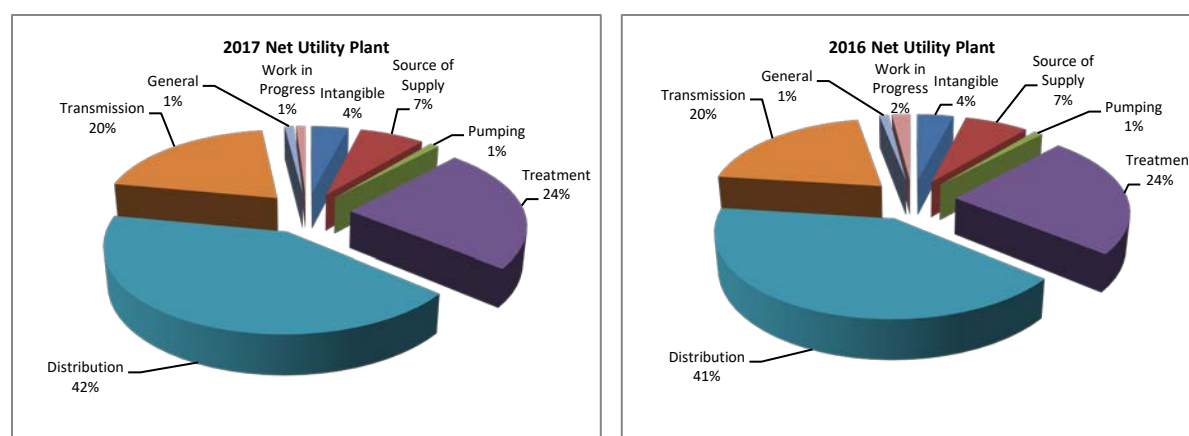
At the end of 2016 Tacoma Water had \$879.5 million in net utility plant, a decrease of \$5.2 million from 2015. Plant in Service increased \$15.5 million compared to 2015. In 2016, 11.6 miles of water main were added or replaced. Construction was completed on 27 private contracts in 2016, resulting in 8.33 miles. The \$20.6 million increase in accumulated depreciation is due to the net increase in Plant in Service in 2015 of \$192.3 million.

The following table summarizes Tacoma Water's capital assets, net of accumulated depreciation, for 2017 – 2015.

Capital Assets, Net of Accumulated Depreciation
(In thousands)

				17/16	16/15
				Increase	Increase
Net Utility Plant	2017	2016	2015	(Decrease)	(Decrease)
Intangible Plant	\$ 36,922	\$ 36,581	\$ 36,368	\$ 341	\$ 213
Source of Supply Plant	58,872	60,348	60,534	(1,476)	(186)
Pumping Plant	5,362	5,448	5,542	(86)	(94)
Water Treatment Plant	210,052	206,273	213,512	3,779	(7,239)
Transmission Plant	172,672	176,439	180,209	(3,767)	(3,770)
Distribution Plant	365,830	361,693	355,557	4,137	6,136
General Plant	11,907	12,194	12,368	(287)	(174)
Construction Work In Progress	11,902	20,572	20,631	(8,670)	(59)
Total	<u>\$ 873,519</u>	<u>\$ 879,548</u>	<u>\$ 884,721</u>	<u>\$ (6,029)</u>	<u>\$ (5,173)</u>

The following graphs provide a visual presentation of the allocation of Tacoma Water's capital investments in 2017 and 2016.



Additional information on capital assets can be found in Note 4 of the financial statements.

Debt Administration

At December 31, 2017 Tacoma Water had outstanding revenue bond obligations of \$384.4 million (net of unamortized bond premiums), a decrease of \$7.9 million compared to 2016. As of year-end 2016, the Utility had outstanding revenue bond obligations of \$392.3 million (net of unamortized bond premiums), a decrease of \$7.6 million compared to 2015.

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 2.32, 2.29, and 2.33 in 2017, 2016 and 2015 respectively.

At the end of 2017, Tacoma Water had an outstanding State loan balance of \$92.6 million compared to \$99.5 million in 2016 and \$89.0 million in 2015.

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 independently 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.



Linda McCrea
Interim Director of Utilities/CEO



Andrew Cherullo
Finance Director

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATEMENTS OF NET POSITION

	DECEMBER 31,	
	2017	2016
ASSETS AND DEFERRED OUTFLOWS		
UTILITY PLANT		
In Service, at Original Cost	\$1,098,436,212	\$1,073,997,566
Less - Accumulated Depreciation	(236,819,423)	(215,021,698)
Total	861,616,789	858,975,868
Construction Work In Progress	11,901,984	20,571,782
Net Utility Plant	873,518,773	879,547,650
NON-UTILITY PROPERTY	492,963	492,963
SPECIAL FUNDS		
Construction Funds	32,591,351	41,717,595
Debt Service Funds	4,366,165	4,394,278
Bond Reserve Funds	21,969,849	22,030,885
System Development Charge Fund	61,645,713	58,617,922
Other Cash & Equity in Pooled Investments	33,389,300	30,066,803
Total Special Funds	153,962,378	156,827,483
CURRENT ASSETS		
Operating Funds Cash and Equity in Pooled Investments	59,076,540	54,768,598
Accounts Receivable	5,312,300	5,496,341
(Net of Allowance for Doubtful Accounts of \$526,979 in 2017 and \$439,846 in 2016)		
BABs Interest Subsidies Receivable	298,940	297,980
Accrued Unbilled Revenues	5,457,221	4,797,144
Materials and Supplies	2,403,305	2,341,548
Interfund Receivable	69,262	107,970
Prepayments.....	1,239,676	1,118,062
Total Current Assets	73,857,244	68,927,643
OTHER ASSETS		
Regulatory Asset-Public Fire Protection Fees ...	456,635	1,297,001
Regulatory Asset-Surcharges	1,353,795	1,569,477
Total Other Assets	1,810,430	2,866,478
TOTAL ASSETS	1,103,641,788	1,108,662,217
DEFERRED OUTFLOWS OF RESOURCES		
Unamortized Losses on Refunding Bonds	1,363,428	1,629,071
Deferred Outflows for Pensions	8,671,039	8,994,103
Total Deferred Outflows of Resources	10,034,467	10,623,174
TOTAL ASSETS AND DEFERRED OUTFLOWS	<u>\$1,113,676,255</u>	<u>\$1,119,285,391</u>

The accompanying notes are an integral part of these financial statements

	DECEMBER 31,	
NET POSITION, LIABILITIES AND DEFERRED INFLOWS	2017	2016
NET POSITION		
Net Investment in Capital Assets	\$445,995,256	\$446,518,253
Restricted for:		
Water Capital and System Development Charge	50,149,083	43,533,806
Debt Service Funds	2,506,278	2,495,984
Unrestricted	58,066,018	57,104,183
Total Net Position	556,716,635	549,652,226
LONG-TERM DEBT		
Revenue Bonds	377,995,249	386,065,146
Public Works Trust Fund Loans	20,011,236	22,708,007
Drinking Water State Revolving Fund Loan	65,612,800	69,844,046
Total Long-Term Debt	463,619,285	478,617,199
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	13,378,017	13,153,017
Current Maturities of Long-Term Liabilities	181,355	185,889
Accrued Taxes	1,556,338	1,492,476
Accrued Expenses and Contracts Payable	1,369,234	1,547,790
Salaries, Wages and Fringe Benefits Payable	725,775	680,647
Interest Payable	1,859,887	1,898,294
Customers' Deposits	356,929	349,725
Interfund Payables	1,096,829	1,678,889
Total Current Liabilities	20,524,364	20,986,727
LONG-TERM LIABILITIES		
Muckleshoot Agreements	6,762,451	6,943,806
Customer Advances for Construction	5,905,910	4,748,046
Unearned Revenue	7,609,819	7,568,812
Long-Term Accrued Compensated Absences	2,068,503	2,428,375
Net Pension Liability	8,278,522	7,788,151
Other Long-Term Liabilities	4,831,577	4,455,228
Total Long-Term Liabilities	35,456,782	33,932,418
TOTAL LIABILITIES	519,600,431	533,536,344
DEFERRED INFLOWS OF RESOURCES		
Rate Stabilization	35,575,447	35,575,447
Deferred Inflows for Pensions	1,783,742	521,374
Total Deferred Inflows of Resources	37,359,189	36,096,821
TOTAL NET POSITION, LIABILITIES, AND DEFERRED INFLOWS	<u>\$1,113,676,255</u>	<u>\$1,119,285,391</u>

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	YEAR ENDED DECEMBER 31,	
	2017	2016
OPERATING REVENUES		
Sale of Water	\$79,999,893	\$77,980,741
Other Operating Revenues	10,059,774	9,997,213
Contract Resource Obligation Revenues	4,584,754	4,823,656
Total Operating Revenues	94,644,421	92,801,610
OPERATING EXPENSES		
Operations	17,881,176	17,211,669
Production	14,801,501	14,334,563
Administrative and General	16,369,139	15,348,131
Depreciation	24,038,103	23,822,527
Taxes	4,776,164	4,639,031
Total Operating Expenses	77,866,083	75,355,921
Net Operating Income	16,778,338	17,445,689
NON-OPERATING REVENUES (EXPENSES)		
Interest Income	1,762,813	1,826,299
Other	1,216,295	(221,125)
Interest on Long-Term Debt (Net of AFUDC)	(19,675,339)	(20,270,161)
Amortization of Premium and Loss on Refunding ..	1,354,254	1,269,625
Total Non-Operating Expenses	(15,341,977)	(17,395,362)
Net Income Before Capital Contributions and Transfers	1,436,361	50,327
Capital Contributions		
Cash	5,510,752	5,707,338
Donated Fixed Assets	3,627,682	4,566,692
Federal BAB Subsidies	3,582,475	3,577,355
Grants	-	1,752
Transfers		
City of Tacoma Gross Earnings Tax	(7,143,861)	(6,753,061)
Transfer to/from Other Funds	51,000	-
CHANGE IN NET POSITION	7,064,409	7,150,403
NET POSITION - BEGINNING OF YEAR	549,652,226	542,501,823
TOTAL NET POSITION - END OF YEAR	\$556,716,635	\$549,652,226

The accompanying notes are an integral part of these financial statements

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATEMENTS OF CASH FLOWS

	YEAR ENDED DECEMBER 31,	
	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash from Customers	\$95,231,637	\$93,706,684
Cash Paid to Suppliers	(21,982,429)	(18,676,633)
Cash Paid to Employees	(26,213,607)	(25,874,134)
Taxes Paid	(4,712,302)	(5,010,207)
Net Cash From		
Operating Activities	42,323,299	44,145,710
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Transfer to Other Funds	51,000	-
Transfer Out for Gross Earnings Tax	(7,143,861)	(6,753,061)
Net Cash From Non-Capital		
Financing Activities	(7,092,861)	(6,753,061)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital Expenditures, net.....	(14,041,704)	(13,598,285)
Proceeds from State Drinking Water Loan	-	16,800,000
Debt Issuance Costs	-	13,680
Principal Payments on Long-Term Debt	(13,153,019)	(12,370,124)
Principal Payments on Muckleshoot LT Liability ...	(185,889)	(190,536)
Interest Paid	(20,053,586)	(20,637,794)
BABs Federal Interest Subsidies	3,581,515	3,577,675
Grants Received	-	1,752
Contributions in Aid of Construction	5,510,752	5,707,338
System Development Charges & Other LT Liabilities.	1,575,222	220,270
Net Cash From Capital and		
Related Financing Activities	(36,766,709)	(20,476,024)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest Received on Investments	1,762,813	1,826,299
Other Net Non-Op Revenues and Expenses	1,216,295	(234,804)
Net Cash From Investing Activities	2,979,108	1,591,495
Net Change in Cash and Equity in		
Pooled Investments	1,442,837	18,508,120
Cash & Equity in Pooled Investments at January 1 ...	211,596,081	193,087,961
Cash & Equity in Pooled Investments at December 31 .	\$213,038,918	\$211,596,081

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

	YEAR ENDED DECEMBER 31,	
	2017	2016
Reconciliation of Net Operating Income to Net Cash From Operating Activities:		
Net Operating Income	\$16,778,338	\$17,445,689
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	24,038,103	23,822,527
Pension (Credits) Expense	2,075,803	1,358,655
Cash from changes in operating assets and liabilities:		
Accounts Receivable and Unbilled Revenue	(476,036)	(37,301)
Interfund Receivables	38,708	578,060
Regulatory Asset-Public Fire Protection Fees	840,366	827,572
Regulatory Asset-Surcharges.....	215,682	113,871
Materials and Supplies	(61,757)	145,527
Prepayments	(121,614)	(147,731)
Accrued Taxes	63,862	(371,176)
Salaries, Wages and Fringe Benefits Payable	45,128	96,319
Long-Term Accrued Compensated Absences	(359,872)	87,949
Customers' Deposits	7,204	932
Accrued Expenses and Contracts Payable	(178,556)	128,920
Interfund Payables	(582,060)	95,897
Total Adjustments	25,544,961	26,700,021
Net Cash From Operating Activities	<u>\$42,323,299</u>	<u>\$44,145,710</u>
Reconciliation of Cash and Equity in Pooled Investments to Balance Sheet:		
Cash and Equity in Pooled Investments in Special Funds	\$153,962,378	\$156,827,483
Cash and Equity in Pooled Investments in Operating Funds	59,076,540	54,768,598
Cash and Equity in Pooled Investments at December 31	<u>\$213,038,918</u>	<u>\$211,596,081</u>

**CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER**

**NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016**

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 101,871 customers and had 236 employees as of December 31, 2017. 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 Finance and Analytics.

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 needed 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 – Designs, constructs, operates and maintains the following of the City's water supply structures: transmission mains and appurtenances, rights-of-ways, wells, pump stations and other mechanical/electrical equipment, storage tanks and reservoirs, pressure reducing stations, Tacoma Water buildings and properties, communication and telemetry systems (including the Water Control Center), corrosion control facilities, and administers water rights and tracks water system security issues, while overseeing and managing Tacoma Water's emergency preparedness and coordinating with outside agencies.

WATER ASSET AND INFORMATION MANAGEMENT – Prepares system and strategic plans, supports Tacoma Water's Geographic Information System and Hydraulic Model operating technologies, promotes use and maturity of TPU information technologies, and oversees asset management implementation which incorporates risk, levels of service, and lifecycle costs into the Tacoma Water decision making process.

WATER FINANCE AND ANALYTICS – Is responsible for the utility's long range financial plan, rates and charges, budget development and monitoring, and rate and financial policies. This group provides financial, supply and demand, and customer analytics and reports to support decision-making by executive management, policymakers and the Regional Water Supply System Partners. This group develops and administers special retail and wholesale water supply agreements in pursuit of the utility's strategic objectives, and is responsible for leading new performance management, risk management, and advanced metering objectives through cross-functional engagement with the utility and TPU.

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. For additional information see Note 6.

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.

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 certificates of deposit with East West Bank and Opus Bank.

The Division's equity in that portion of the City of Tacoma Investment Pool held in qualified public depositories at December 31, 2017 and 2016 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.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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 (NARUC) 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, Hyada Surcharges, Andrain Surcharges and Curran Road 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 GAAP 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.

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. Sick leave pay is recorded as a liability and an expense in the year earned.

The accrued liability is computed at 100% vacation and PTO while sick leave is accrued at 10%, which is considered the amount vested or 25% if the employee meets retirement criteria. Based on historical information, 10% of compensated absences are considered short term.

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 deferred outflows and liabilities and deferred inflows 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.

NOTE 3 INVESTMENTS MEASURED AT FAIR VALUE

The City measures and records its investments within the fair value hierarchy established by generally accepted accounting principles.

The hierarchy is based on the valuation inputs used to measure the fair value of the asset, where fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. These guidelines recognize a three-tiered fair value hierarchy, as follows:

- Level 1 – Level 1 inputs are quoted (unadjusted) prices in active markets for identical assets or liabilities that the government can access at the measurement date. Observable markets include exchange markets, dealer markets, brokered markets and principal-to-principal markets.
- Level 2 – Level 2 inputs are other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs are sourced from pricing vendors using models that are market-based and corroborated by observable market data including: quoted prices; nominal yield spreads; benchmark yield curves; and other corroborated inputs.
- Level 3 – Level 3 inputs are unobservable inputs for the asset or liability and should only be used when relevant Level 1 or Level 2 inputs are unavailable.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

The fair value evaluations are provided by Interactive Data. Interactive Data utilizes evaluated pricing models that vary by asset class and incorporate available trade, bid and other market information and for structured securities, cash flow and, when available, loan performance data. Because many fixed income securities do not trade on a daily basis, Interactive Data's evaluated pricing applications apply available information as applicable through processes such as benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing, to prepare evaluations. In addition, Interactive Data uses model processes, such as the Option Adjusted Spread model to assess interest rate impact and development payment scenarios. Their models and processes take into account market convention. For each asset class, a team of evaluators gathers information from market sources and integrates relevant credit information, perceived market movements and sector news into the evaluated pricing applications and models.

Cash and cash equivalents include highly liquid investments including short-term investment funds. Cash and cash equivalents are valued at cost and, therefore, excluded from the fair value schedule.

Data regarding the City's investments, valued and categorized according to the above outlined levels, is below:

	As of			
	12/31/2017	Level 1	Level 2	Level 3
Debt Securities				
U.S. Treasury Securities	\$ 218,142,864	\$ -	\$ 218,142,864	\$ -
U.S. Agency Securities	517,345,818	-	517,345,818	-
Supranational Securities	19,966,040	-	19,966,040	-
Municipal Bonds	40,760,727	-	40,760,727	-
Total	<u>\$ 796,215,449</u>	<u>\$ -</u>	<u>\$ 796,215,449</u>	<u>\$ -</u>

	As of			
	12/31/2016	Level 1	Level 2	Level 3
Debt Securities				
U.S. Treasury Securities	\$ 146,824,628	\$ -	\$ 146,824,628	\$ -
U.S. Agency Securities	544,579,831	-	544,579,831	-
Municipal Bonds	61,450,051	-	61,450,051	-
Total	<u>\$ 752,854,510</u>	<u>\$ -</u>	<u>\$ 752,854,510</u>	<u>\$ -</u>

Tacoma Water's share of the City Investments shown in the table above is 23.01% and 24.45% as of December 31, 2017 and 2016.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

NOTE 4 UTILITY PLANT

A summary of the balances and changes in utility plant for 2017 and 2016 follows:

	Balance December 31, 2016			Transfers & Adjustments		Balance December 31, 2017	
		Additions	Retirements				
Intangible Plant	\$ 36,581,485	\$ 561,168	\$ (220,314)	\$ -	\$ -	\$ 36,922,339	
Source of Supply Plant	85,484,873	467,498	-	-	-	85,952,371	
Pumping Plant	9,543,873	158,143	-	-	-	9,702,016	
Water Treatment Plant	230,820,998	12,026,741	-	-	-	242,847,739	
Transmission Facilities	230,989,672	7,250	(1,423,664)	-	-	229,573,258	
Distribution Facilities	444,794,626	12,355,245	(592,914)	-	-	456,556,957	
General Plant	35,782,039	1,107,115	-	(7,622)	-	36,881,532	
Total Water Plant in Service	1,073,997,566	26,683,160	(2,236,892)	(7,622)	-	1,098,436,212	
Less Accumulated Depreciation	(215,021,698)	(24,038,103)	2,005,998	234,380	-	(236,819,423)	
	858,975,868	2,645,057	(230,894)	226,758	-	861,616,789	
Construction Work in Progress	20,571,782	20,188,617	-	(28,858,415)	-	11,901,984	
Net Utility Plant	\$ 879,547,650	\$ 22,833,674	\$ (230,894)	\$ (28,631,657)	\$ -	\$ 873,518,773	

	Balance December 31, 2015			Transfers & Adjustments		Balance December 31, 2016	
		Additions	Retirements				
Intangible Plant	\$ 36,367,666	\$ 783,399	\$ (569,580)	\$ -	\$ -	\$ 36,581,485	
Source of Supply Plant	83,671,496	1,813,377	-	-	-	85,484,873	
Pumping Plant	9,400,042	143,831	-	-	-	9,543,873	
Water Treatment Plant	229,764,871	1,056,127	-	-	-	230,820,998	
Transmission Facilities	230,986,906	2,766	-	-	-	230,989,672	
Distribution Facilities	433,734,385	13,210,948	(2,150,707)	-	-	444,794,626	
General Plant	34,608,449	1,189,967	(16,377)	-	-	35,782,039	
Total Water Plant in Service	1,058,533,815	18,200,415	(2,736,664)	-	-	1,073,997,566	
Less Accumulated Depreciation	(194,443,324)	(23,822,527)	2,167,084	1,077,069	-	(215,021,698)	
	864,090,491	(5,622,112)	(569,580)	1,077,069	-	858,975,868	
Construction Work in Progress	20,630,616	18,141,410	-	(18,200,244)	-	20,571,782	
Net Utility Plant	\$ 884,721,107	\$ 12,519,298	\$ (569,580)	\$ (17,123,175)	\$ -	\$ 879,547,650	

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

Total Water Plant in Service includes non-depreciable assets of \$59,468,271 for 2017 and \$59,139,334 for 2016. The total amount of interest incurred and capitalized is \$492,012 for 2017 and \$484,093 for 2016.

NOTE 5 LONG-TERM DEBT

The Division's Long-term Liabilities are primarily for the purpose of capital improvements. Long-term debt activities for 2017 and 2016 were as follows:

	Balance December 31, 2016	Additions	Reductions	Balance December 31, 2017	Due Within One Year
Revenue Bonds	\$ 378,625,000	\$ -	\$ (6,225,000)	\$ 372,400,000	\$ 6,450,000
Plus: Unamortized Premium	13,665,146	-	(1,619,897)	12,045,249	-
Net Revenue Bonds	392,290,146	-	(7,844,897)	384,445,249	6,450,000
Public Works Trust Fund Loans	25,404,777	-	(2,696,770)	22,708,007	2,696,771
Drinking Water State Revolving Fund Loans	74,075,293	-	(4,231,247)	69,844,046	4,231,246
Total Long-Term Debt	<u>\$ 491,770,216</u>	<u>\$ -</u>	<u>\$ (14,772,914)</u>	<u>\$ 476,997,302</u>	<u>\$ 13,378,017</u>
	Balance December 31, 2015	Additions	Reductions	Balance December 31, 2016	Due Within One Year
Revenue Bonds	\$ 384,705,000	\$ -	\$ (6,080,000)	\$ 378,625,000	\$ 6,225,000
Plus: Unamortized Premium	15,216,093	-	(1,550,947)	13,665,146	-
Net Revenue Bonds	399,921,093	-	(7,630,947)	392,290,146	6,225,000
Public Works Trust Fund Loans	28,101,548	-	(2,696,771)	25,404,777	2,696,771
Drinking Water State Revolving Fund Loans	60,868,644	16,800,000	(3,593,351)	74,075,293	4,231,246
Total Long-Term Debt	<u>\$ 488,891,285</u>	<u>\$ 16,800,000</u>	<u>\$ (13,921,069)</u>	<u>\$ 491,770,216</u>	<u>\$ 13,153,017</u>

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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

SENIOR LIEN BONDS

	2017	2016
2005 Water System Revenue and Refunding Bonds, with interest rate of 5.0%, due in 2025.		
Original Issue: \$46,550,000	\$ 5,000	\$ 5,000
Current Portion: \$0		
2009 Water System Revenue Bonds, with interest rate at 5.751%, with Build America Bond (BAB) rebate ranging from 32.45% to 32.62%, due in yearly installments starting in 2033 ranging from \$9,800,000 to \$12,210,000 through 2039.		
Original Issue: \$76,775,000	76,775,000	76,775,000
Current Portion: \$0		
2010A Water System Revenue Refunding Bonds, with interest rates ranging from 4.0% to 5.0%, due in yearly installments ranging from \$3,935,000 to \$4,655,000 through 2023.		
Original Issue: \$29,100,000	25,825,000	26,395,000
Current Portion: \$3,935,000		
2010B Water System Revenue Bonds, with interest rates ranging from 4.581% to 5.621%, with Build America Bond (BAB) Rebate ranging from 32.45% to 32.62% 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	74,985,000	74,985,000
Current Portion: \$0		
2010A Regional Water Supply System Revenue Bonds, with interest rates ranging from 3.0% to 4.0%, due in yearly installments ranging from \$290,000 to \$355,000 through 2024. (See Note 6)		
Original Issue: \$3,595,000	2,245,000	2,525,000
Current Portion: \$290,000		

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

SENIOR LIEN BONDS CONTINUED

	<u>2017</u>	<u>2016</u>
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 32.45% to 32.62% 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	44,245,000	44,245,000
Current Portion: \$0		
2013 Water System Revenue and Refunding Bonds, with interest rates of 4.0%, due in yearly installments starting in 2041 ranging from \$23,820,000 to \$25,765,000 through 2043.		
Original Issue: \$78,305,000	74,355,000	74,355,000
Current Portion: \$0		
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 \$765,000 to \$6,425,000 through 2032. (See Note 6)		
Original Issue: \$64,795,000	60,165,000	60,910,000
Current Portion: \$765,000		
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 \$2,025,000 through 2025.		
Original Issue: \$16,645,000	13,800,000	16,645,000
Current Portion: \$1,460,000		
2015B Water System Refunding Bonds with interest rate of 1.15%, final installment due in the amount of \$1,785,000 in 2017.		
Original Issue: \$6,365,000	-	1,785,000
Current Portion: \$0		
	<u> </u>	<u> </u>
Subtotal Sr. Lien Debt	\$ 372,400,000	\$ 378,625,000
Unamortized Premium	12,045,249	13,665,146
Less Current Portion of Revenue Bond Debt	<u>(6,450,000)</u>	<u>(6,225,000)</u>
Long-term Portion of Revenue Bond Debt	<u>\$ 377,995,249</u>	<u>\$ 386,065,146</u>

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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

Year	Principal	Interest
2018	\$ 6,450,000	\$ 18,690,919
2019	7,610,000	18,428,169
2020	7,950,000	18,094,669
2021	8,355,000	17,703,369
2022	8,725,000	17,333,568
2023-2027	48,715,000	79,968,002
2028-2032	60,640,000	66,446,937
2033-2037	88,350,000	47,711,156
2038-2042	109,840,000	20,934,445
2043	25,765,000	1,030,600
	\$ 372,400,000	\$ 306,341,834

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 Division was in compliance with all debt covenants at December 31, 2017.

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

	2017	2016
Public Works Trust Fund Loans		
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 \$52,632 through 2021.	\$ 210,526	\$ 263,158
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.	2,133,334	2,666,667
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.	216,718	270,898

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

JUNIOR LIEN DEBT CONTINUED

	<u>2017</u>	<u>2016</u>
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.	2,656,250	3,187,500
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.	373,538	426,901
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.	3,335,294	3,705,882
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.	6,004,569	6,550,439
2012 Public Works Trust Fund construction loan for the Green River Filtration Facility, with interest of .5% per annum, due in yearly installments of \$555,555 through 2031.	7,777,778	8,333,333
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 \$161,052 through 2021.	644,211	805,263
2008 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.5% per annum, due in yearly installments of \$215,108 through 2028.	2,366,192	2,581,300
2009 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.0% per annum, due in yearly installments of \$367,088 through 2032.	5,506,318	5,873,406
2010 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.5% per annum, due in yearly installments of \$303,000 through 2032.	4,545,000	4,848,000

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

JUNIOR LIEN DEBT CONTINUED

	<u>2017</u>	<u>2016</u>
2010 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$304,579 through 2034.	5,177,842	5,482,421
2011 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.5% per annum, due in yearly installments of \$121,524 through 2033.	1,944,378	2,065,902
2011 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$303,000 through 2035.	5,454,000	5,757,000
2012 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$606,000 through 2035.	10,908,000	11,514,000
2013 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$606,000 through 2035.	10,908,000	11,514,000
2013F construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$606,000 through 2035.	10,908,000	11,514,000
2015 construction loan for the Green River Water Treatment Plant Filtration Facility, with interest of 1.5% per annum, due in yearly installments of \$637,895 through 2035.	<u>11,482,105</u>	<u>12,120,000</u>
Subtotal Junior Lien Debt	92,552,053	99,480,070
Less Current Portion of Debt	<u>(6,928,017)</u>	<u>(6,928,017)</u>
Long-term Portion of Junior Lien Debt	<u><u>\$ 85,624,036</u></u>	<u><u>\$ 92,552,053</u></u>

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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

Year	Principal	Interest
2018	\$ 6,928,017	\$ 1,082,701
2019	6,928,017	1,009,162
2020	6,928,017	935,624
2021	6,928,017	862,087
2022	6,126,820	788,548
2023-2027	27,447,173	2,975,436
2028-2032	22,258,626	1,453,465
2033-2035	9,007,366	244,693
	<u>\$ 92,552,053</u>	<u>\$ 9,351,716</u>

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

Contracted sales to WestRock CP LLC accounted for 7.9% and 7.5% of Tacoma Water's total water sales in 2017 and 2016, respectively. There were no outstanding accounts receivables from WestRock at year-end 2017 or 2016.

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 2017 and 2016 were \$3,354,191 and \$2,148,122, 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 2017 and 2016, Fleet Services returned 75% of the

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

interest earned on the capital replacement reserve to Tacoma Water's replacement fund. The amounts refunded in 2017 and 2016 were \$38,840 and \$36,966, 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 2017 and 2016. Assets in the Self-Insurance Fund total \$7.0 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 GAAP. 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.

Other 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 property insurance policy has a deductible of \$250,000 for buildings and property within buildings and \$10,000 per vehicle. General government obtains coverage on general government's buildings and property within buildings with a limit of \$500,000 and a retention of \$150,000 with exceptions. For the Department 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 \$20 million of excess coverage with a \$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 or System), 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

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

by state and federal retirement plans. Employees of the Tacoma-Pierce County Health Department, as well as, certain employees of the Pierce Transit and 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, 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 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, 2016 (measurement date) is as follows:

Retirees and beneficiaries currently receiving benefits	2,303	
Terminated vested and other terminated participants	675	
Active members:		
City of Tacoma	2,687	
South Sound 911	2	
Pierce Transit	8	
Tacoma-Pierce County Health Department	267	
Total active members		2,964
Total membership		5,942

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 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.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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.

In fiscal year 2017, 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%. On November 28, 2017 the Tacoma City Council approved the TERS Board's recommendation to increase the contribution rate by 1% (split 0.54% for employers and 0.46% for employees) effective the first pay period in February 2018, 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, 2016
Valuation Date	January 1, 2017
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• 3.75% amortization growth rate
Asset Valuation Method	4 year smoothing period; Corridor - None
Inflation	2.75%
Salary Increases	Varies by service
Investment Rate of Return	7.00%
Cost of Living Adjustment	2.125%
Retirement Age	Varies by age, gender, eligibility
Turnover	Varies by service, and gender
Mortality	RP-2014 Mortality for Employees, Healthy and Disabled Annuitants. Generational improvements with projection scale based on Social Security Administration Data.

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. The following changes in assumptions occurred since the January 1, 2016 Actuarial Valuation:

1. The amortization growth rate decreased from 4% to 3.75%
2. The inflation rate decreased from 3% to 2.75%
3. The investment rate of return decreased from 7.25% to 7%

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

Target Allocations - The long-term expected rate of return is determined by adding expected inflation to expected long-term real returns and reflecting expected volatility and correlation. The capital market assumptions are per Milliman's (the System's actuary) investment consulting practice as of December 31, 2016. The target asset allocation is based on the Tacoma Employees' Retirement System Investment Policy Statement dated March 2016.

Asset Class	Target Allocation	Long-Term Expected Arithmetic Real Rate of Return
Investment Grade Fixed Income	15.0%	1.63%
US Inflation-Indexed Bonds	5.0%	1.21%
High Yield Bonds	9.0%	5.00%
Emerging Market Debt	5.0%	3.74%
Global Equity	41.5%	5.50%
Public Real Estate	2.0%	5.80%
Private Real Estate	2.5%	3.56%
Private Equity	10.0%	9.04%
Master Limited Partnerships	4.0%	4.12%
Timber	2.0%	3.79%
Infrastructure	2.0%	5.03%
Agriculture	2.0%	4.33%
Assumed Inflation - Mean		2.75%
Assumed Inflation - Standard Deviation		1.85%
Portfolio Arithmetic Real Mean Return		4.76%
Portfolio Median Nominal Geometric Return		6.72%
Portfolio Standard Deviation		11.77%
Long-Term Expected Rate of Return, net of investment expenses		7.00%

Sensitivity Analysis - The following presents the net pension liability (asset) of the System, calculated using the discount rate of 7%, 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%) or 1 percentage point higher (8%) than the current rate.

	1% Decrease 6.00%	Current Discount Rate 7.00%	1% Increase 8.00%
Net Pension Liability (asset)	\$ 26,509,122	\$ 8,278,522	\$ (6,516,306)

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

As of December 31, 2017, the deferred inflows and outflows of resources are as follows:

	Deferred Inflows of Resources	Deferred Outflows of Resources
Difference Between Expected and Actual Experience	\$ (1,781,842)	\$ -
Changes of assumptions	-	2,749,460
Net Difference Between Projected and Actual Earnings	-	3,767,336
Changes in Employer Proportion	(1,900)	4,038
Contributions Made Subsequent to the Measurement Date	-	2,150,205
Total	\$ (1,783,742)	\$ 8,671,039

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.

Amounts will be recognized in pension expense as follows:

Year-ended December 31,	
2018	\$ 1,475,069
2019	1,475,069
2020	1,701,164
2021	(64,035)
2022	149,825
Thereafter	-
	<u>\$ 4,737,092</u>

The proportionate share of the Water Division is 8.91% of total System's pension liability. 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 (3.50%).

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 in accordance with GAAP. 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 2017 is 20 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 statements of net position. The City has a Net OPEB Obligation as of December 31, 2017 as the City has not set aside funds for OPEB.

Excise Tax for High Cost or “Cadillac” Health Plans in 2020 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 Consolidated Appropriations Act (CAA), which was signed into law in December 2015, delays the tax for two years, until 2020.

GAAP 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. 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.

There is significant uncertainty with respect to the excise tax at this time. President Trump recently signed an executive order which gives instruction to the leaders of the new administration to unwind certain aspects of the ACA, especially those components deemed “burdensome.” It remains unclear how this would be implemented, especially due to the interconnected nature of the ACA. The City has continued to value the excise tax as it currently appears in the tax code, but will monitor this situation carefully going forward.

Summary of Changes – As of the January 1, 2017 valuation the total AAL was \$240,449,771, for the City, 12.5% higher than expected primarily due to changes demographic experience, medical cost expectations and medical trend assumptions, and demographic and economic assumptions.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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

	<u>January 1, 2015</u>	<u>January 1, 2017</u>
Total Membership:		
Active Employees	3,404	3,492
Terminated vested employees	442	476
Retired employees & dependents	<u>744</u>	<u>691</u>
Total	<u><u>4,590</u></u>	<u><u>4,659</u></u>
Annual Benefit Payments	\$ 8,963,089	\$ 9,010,942
Discount Rate	3.75%	3.50%
Present Value of Benefits (PVB)	\$ 262,184,195	\$ 289,047,229
Actuarial Accrued Liability (AAL)	\$ 208,814,312	\$ 240,449,771
Assets	<u>-</u>	<u>-</u>
Unfunded Actuarial Accrued Liability (UAAL)	<u><u>\$ 208,814,312</u></u>	<u><u>\$ 240,449,771</u></u>
Normal Cost	\$ 3,832,131	\$ 3,261,947
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 19,529,549

The following table shows the total value of the benefits provided, the member paid premiums and the City paid benefits as of January 1, 2017.

<u>Value of Subsidy at 3.50% Interest Rate</u>	<u>Total Value of</u> <u>Benefits</u>	<u>Member Paid</u> <u>Premiums</u>	<u>City Paid</u> <u>Benefits</u>
Present Value of Benefits (PVB)	\$ 399,300,824	\$ 110,253,595	\$ 289,047,229
Actuarial Accrued Liability (AAL)	\$ 285,825,708	\$ 45,375,937	\$ 240,449,771
Normal Cost	\$ 7,595,595	\$ 4,443,955	\$ 3,151,640
Annual Benefit Payments	\$ 11,674,734	\$ 2,663,793	\$ 9,010,941

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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, 2017.

	City	Division
Determination of Annual Required Contribution:		
Normal Cost at Year-end	\$ 3,261,947	\$ 204,804
Amortization of UAAL	16,267,602	79,407
Annual Required Contribution (ARC)	<u>\$ 19,529,549</u>	<u>\$ 284,211</u>
Determination of Net OPEB Obligation:		
Annual Required Contribution (ARC)	\$ 19,529,549	\$ 284,211
Interest on prior year Net OPEB Obligation	2,895,939	118,463
Adjustments to ARC	<u>(4,743,612)</u>	<u>(165,382)</u>
Annual OPEB Cost	17,681,876	237,292
Actual benefits paid	<u>(9,010,941)</u>	<u>(79,449)</u>
Increase in Net OPEB Obligation	8,670,935	157,843
Net OPEB Obligation - beginning of year	<u>82,741,128</u>	<u>3,384,649</u>
Net OPEB Obligation - end of year	<u>\$ 91,412,063</u>	<u>\$ 3,542,492</u>

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 cost and net OPEB obligation for three years. This table is based upon a 3.50% interest rate.

	Annual OPEB Cost		Benefits Paid		Net OPEB Obligation	
Year Ended	City	Division	City	Division	City	Division
12/31/2015	\$ 15,954,387	\$ 357,394	\$ 8,963,089	\$ 115,102	\$ 73,129,502	\$ 3,150,430
12/31/2016	\$ 18,151,028	\$ 348,917	\$ 8,539,402	\$ 114,698	\$ 82,741,128	\$ 3,384,649
12/31/2017	\$ 17,681,876	\$ 237,292	\$ 9,010,941	\$ 79,449	\$ 91,412,063	\$ 3,542,492

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 ARC, 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 20 years.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

Actuarial Methods and Significant Actuarial Assumptions:

Valuation Date:	January 1, 2017
Census Date:	January 1, 2017
Actuarial Cost Method:	Entry Age
Amortization Date:	Combination of level percentage and level dollar amount, see note above.
Remaining Amortization Period:	20 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: 3.50% for pay-as-you-go funding

Medical Cost Trend:	2017	9.10%
	2018	6.40%
	2019	5.80%
	2020	5.30%
	2030	5.40%
	2040	5.50%
	2050	5.20%

The trend for year 2017 reflects the amount by which 2018 medical costs are expected to exceed 2017 medical costs. The medical cost rate is assumed to continue grading downward until achieving the ultimate rate of 4.40% in 2073 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): 3.50%

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 12 ACQUISITION OF WATER ASSOCIATION

The Curran Road Mutual Water Association (Curran Road) provided services to more than 620 customers, in the vicinity of 128th Street East and Canyon Road East in Pierce County. Curran Road was a Tacoma Water wholesale customer and had received all of its water from Tacoma Water since the 1940's. As a requirement of the Washington State Department of Health, Curran Road was due to develop a new water system plan. In-lieu of developing a water system plan and securing financing to make system improvements, Curran Road requested Tacoma Water acquire the Curran Road service area and provide direct retail service to its members.

In 2017, Tacoma Water acquired Curran Road and over a period of 8-10 years will replace more than 6-miles of asbestos cement water main and complete other system improvements. The asbestos main is expected to be abandoned in place and no remediation liability is anticipated to be incurred at this time. The estimated cost of this water system improvement work is \$12 million, which will be paid for by those customers within the boundaries of the Curran Road water system through a customer surcharge over an estimated 33-year period, in accordance with the City Council's Expansion Policy.

The acquired balances of Curran Road's assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position as of the beginning of the period, were determined on the basis of carrying values reported in their financial statements as of December 31, 2016. Tacoma Water acquired \$196,000 in current assets and \$4,316 in capital assets.

NOTE 13 COMMITMENTS AND CONTINGENCIES

Capital Improvements – The financial requirement for Tacoma Water's 2017-2018 biennial Capital Improvement program is approximately \$48.1 million and Tacoma Water has substantial contractual commitments relating to the program. At December 31, 2017 the remaining financial requirement for Capital Improvement Programs relating to all prior biennia is approximately \$3.8 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 Water Division 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.

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REQUIRED SUPPLEMENTARY INFORMATION

Proportionate Share of the Net Pension Liability Last 10 Years*

	Fiscal Year Ended December 31st,		
	2017	2016	2015
Employer's proportion of the net pension liability (asset) as a percentage	8.91%	8.99%	9.17%
Employer's proportion share of net pension liability (asset)	\$8,278,522	\$7,788,151	(\$881,279)
Employer's covered payroll	\$20,220,795	\$21,148,347	\$20,099,527
Employer's proportionate share of net pension liability (asset) as a percentage of its covered employee payroll	40.94%	36.83%	-4.17%
Plan fiduciary net position as a percentage the total pension liability	93.91%	93.94%	100.71%

Schedule of Contributions Last 10 Fiscal Years*

	Fiscal Year Ended December 31st,		
	2017	2016	2015
Contractually required employer contribution	\$2,150,205	\$2,124,252	\$2,086,719
Contributions in relation to the contractually required employer contribution	(2,150,205)	(2,124,252)	(2,086,719)
Employer contribution deficiency (excess)	-	-	-
Employer's covered employee payroll	\$20,914,658	\$20,220,795	\$21,148,347
Employer contribution as a percentage of covered-employee payroll	10.28%	10.51%	9.87%

* The above schedules are intended to show information for 10 years, the additional years' information will be displayed as it becomes available.

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STATISTICAL DATA (Unaudited)

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

TEN-YEAR FINANCIAL REVIEW

STATEMENTS OF NET POSITION	2017	2016	2015	2014
ASSETS				
Utility Plant - Net	\$873,518,773	\$879,547,650	\$884,721,107	\$872,083,357
Special Funds & Non-Util Prop	154,455,341	157,320,446	143,802,732	146,933,170
Current Assets	73,857,244	68,927,643	64,476,112	58,737,269
Other Assets	1,810,430	2,866,478	4,689,200	3,769,208
Total Assets	1,103,641,788	1,108,662,217	1,097,689,151	1,081,523,004
Deferred Outflows	10,034,467	10,623,174	4,002,699	1,587,851
TOTAL ASSETS AND DEFERRED OUTFLOWS .	1,113,676,255	1,119,285,391	1,101,691,850	1,083,110,855
NET POSITION	556,716,635	549,652,226	542,501,823	516,673,245
LIABILITIES AND EQUITY				
Long-Term Debt	463,619,285	478,617,199	478,400,742	483,542,005
Current Liabilities	20,524,364	20,986,727	18,261,548	20,767,576
Long-Term Liabilities	35,456,782	33,932,418	26,021,937	26,552,582
Total Liabilities	519,600,431	533,536,344	522,684,227	530,862,163
Deferred Inflows	37,359,189	36,096,821	36,505,800	35,575,447
TOTAL NET POSITION, LIABILITIES, AND DEFERRED INFLOWS	\$1,113,676,255	\$1,119,285,391	\$1,101,691,850	\$1,083,110,855
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION				
OPERATING REVENUES				
Residential and Domestic	\$52,539,643	\$50,742,135	\$48,263,128	\$44,655,076
Commercial and Industrial	17,408,529	17,558,905	17,233,617	15,406,078
Special Rate-Simpson/Other	6,322,195	5,845,719	5,951,348	5,801,842
Municipal	-	-	-	-
Wholesale	3,069,448	3,971,839	5,192,149	3,718,315
Unbilled	660,078	(137,857)	318,945	121,346
Total Water Sales	79,999,893	77,980,741	76,959,187	69,702,657
Other Operating Revenues	14,644,528	14,820,869	21,179,637	28,617,297
Total Operating Revenues	94,644,421	92,801,610	98,138,824	98,319,954
OPERATING EXPENSES				
Operation and Maintenance	49,051,816	46,894,363	41,804,233	37,993,563
Taxes	4,776,164	4,639,031	4,681,114	3,779,373
Depreciation	24,038,103	23,822,527	17,102,664	16,783,698
Total Operating Expenses	77,866,083	75,355,921	63,588,011	58,556,634
NET OPERATING INCOME (LOSS)	16,778,338	17,445,689	34,550,813	39,763,320
NON-OPERATING REVENUES (EXPENSES)				
Other Income	1,216,295	(221,125)	(30,042)	537,052
Interest Income	1,762,813	1,826,299	1,112,850	1,718,226
Gain from Disposition of Property	-	-	-	-
Interest Charges (Net)	(18,321,085)	(19,000,536)	(16,677,645)	(11,911,850)
Net Income (Loss) Before Contributions & Transfers	1,436,361	50,327	18,955,976	30,106,748
Total Capital Contributions	9,138,434	10,274,030	9,052,674	8,670,639
Grants & Federal BAB Subsidies	3,582,475	3,579,107	3,609,706	3,959,446
Transfers Out	(7,092,861)	(6,753,061)	(6,873,467)	(6,352,561)
CHANGE IN NET POSITION	\$7,064,409	\$7,150,403	\$24,744,889	\$36,384,272

In accordance with Governmental Accounting Standards Board Statement No. 65 both 2012 and 2011 were restated for comparative purposes. Years prior to 2011 are shown as originally reported.

2013	2012	2011	2010	2009	2008
\$813,050,518	\$722,852,270	\$661,153,297	\$636,592,771	\$604,657,775	\$590,593,258
157,311,979	161,863,075	214,619,106	240,132,895	133,949,294	80,858,401
63,568,675	56,407,560	31,403,521	30,200,303	35,753,843	22,151,467
4,679,599	5,300,185	4,664,090	4,654,608	3,654,494	3,319,156
1,038,610,771	946,423,090	911,840,014	911,580,577	778,015,406	696,922,282
1,813,858	1,764,332	2,056,555	-	-	-
1,040,424,629	948,187,422	913,896,569	911,580,577	778,015,406	696,922,282
480,288,973	449,858,136	425,932,810	417,695,083	412,592,671	404,010,304
455,876,975	401,465,338	419,800,757	421,228,553	292,165,406	218,869,015
42,478,805	35,106,590	18,201,697	20,548,451	15,167,938	16,288,305
26,204,429	26,181,911	19,385,858	52,108,490	58,089,391	57,754,658
524,560,209	462,753,839	457,388,312	493,885,494	365,422,735	292,911,978
35,575,447	35,575,447	30,575,447	-	-	-
\$1,040,424,629	\$948,187,422	\$913,896,569	\$911,580,577	\$778,015,406	\$696,922,282
\$40,928,355	\$38,737,505	\$36,730,275	\$35,503,069	\$36,695,919	\$34,651,756
13,507,899	12,478,932	11,868,976	11,703,099	11,467,636	10,600,262
5,242,359	5,031,760	4,774,237	3,798,922	4,153,327	4,371,527
445,844	383,385	400,322	364,357	380,267	349,722
3,519,409	2,090,430	1,625,163	1,530,116	1,776,686	1,251,815
468,030	416,986	478,594	(648,438)	187,966	417,145
64,111,896	59,138,998	55,877,567	52,251,125	54,661,801	51,642,227
32,007,524	21,541,733	9,526,467	10,735,630	9,331,955	5,382,313
96,119,420	80,680,731	65,404,034	62,986,755	63,993,756	57,024,540
35,906,356	32,602,452	32,821,611	34,453,742	34,055,463	33,387,663
3,918,944	3,485,243	3,106,516	3,142,772	3,093,311	2,881,877
16,072,243	15,262,686	14,389,681	14,474,964	13,845,799	13,016,544
55,897,543	51,350,381	50,317,808	52,071,478	50,994,573	49,286,084
40,221,877	29,330,350	15,086,226	10,915,277	12,999,183	7,738,456
(1,246,053)	288,182	(12,371)	33,795	497,331	61,265
807,466	2,320,753	3,141,374	2,370,993	1,955,385	3,730,407
-	-	-	-	26,100	-
(14,141,036)	(14,462,441)	(14,867,263)	(15,175,660)	(9,076,156)	(8,406,264)
25,642,254	17,476,844	3,347,966	(1,855,595)	6,401,843	3,123,864
7,175,575	7,834,345	9,250,677	9,713,596	7,120,993	14,137,605
3,535,426	3,840,767	4,006,209	2,355,132	244,683	-
(5,922,418)	(5,226,630)	(4,960,736)	(5,110,721)	(5,185,152)	(5,014,482)
\$30,430,837	\$23,925,326	\$11,644,116	\$5,102,412	\$8,582,367	\$12,246,987

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
REGIONAL WATER SUPPLY SYSTEM

TEN-YEAR FINANCIAL REVIEW

STATEMENTS OF NET POSITION	2017	2016	2015	2014
ASSETS				
Utility Plant - Net	\$279,190,310	\$287,187,547	\$295,780,351	\$293,110,553
Current Assets	10,442,765	10,395,435	9,274,080	11,321,557
Total Assets	289,633,075	297,582,982	305,054,431	304,432,110
Deferred Outflows	240,210	256,313	272,417	288,520
TOTAL ASSETS AND DEFERRED OUTFLOWS .	289,873,285	297,839,295	305,326,848	304,720,630
NET POSITION	174,701,516	180,852,158	186,712,448	183,898,541
LIABILITIES AND EQUITY				
Long-Term Debt	112,594,314	114,364,416	116,113,730	117,798,157
Current Liabilities	1,564,360	1,601,549	1,496,773	1,993,880
Total Liabilities	114,158,674	115,965,965	117,610,503	119,792,037
Deferred Inflows	1,013,095	1,021,172	1,003,897	1,030,052
TOTAL NET POSITION, LIABILITIES, AND DEFERRED INFLOWS	289,873,285	297,839,295	305,326,848	304,720,630
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION				
OPERATING REVENUES				
CRO - Debt Service	\$5,554,208	\$5,582,030	\$6,047,314	\$6,008,599
CRO - O&M	3,858,622	3,858,714	2,840,435	2,706,023
CRO - Capital	202,255	483,498	7,621,901	15,132,508
Other Operating Revenue	-	-	1,675	-
Total Operating Revenues	9,615,085	9,924,242	16,511,325	23,847,130
OPERATING EXPENSES				
Operation and Maintenance	3,881,686	3,871,737	2,864,326	2,735,246
Depreciation	8,266,685	8,263,267	4,582,300	4,542,912
Total Operating Expenses	12,148,371	12,135,004	7,446,626	7,278,158
NET OPERATING INCOME (LOSS)	(2,533,286)	(2,210,762)	9,064,699	16,568,972
NON-OPERATING REVENUES (EXPENSES)				
Other Income	-	-	(120,564)	(18,732)
Interest Income	91,554	87,696	64,497	114,387
Interest Charges (Net)	(4,697,999)	(4,715,565)	(4,072,780)	(880,966)
Net Income (Loss) Before Contributions & Transfers	(7,139,731)	(6,838,631)	4,935,852	15,783,661
Total Capital Contributions	179,156	456,685	(2,924,135)	13,024,297
Grants & Federal BAB Subsidies	809,933	808,775	802,190	805,374
Transfers Out	-	(287,119)	-	-
CHANGE IN NET POSITION	(\$6,150,642)	(\$5,860,290)	\$2,813,907	\$29,613,332

In accordance with Governmental Accounting Standards Board Statement No. 65 both 2012 and 2011 were restated for comparative purposes. Years prior to 2011 are shown as originally reported.

2013	2012	2011	2010	2009	2008
\$264,883,717	\$223,896,711	\$203,938,358	\$207,242,527	\$206,708,069	\$231,099,649
20,473,681	41,256,611	55,640,447	59,811,400	15,845,604	9,519,659
285,357,398	265,153,322	259,578,805	267,053,927	222,553,673	240,619,308
304,624	-	-	1,194,533	807,387	856,484
285,662,022	265,153,322	259,578,805	268,248,460	223,361,060	241,475,792
154,285,209	136,200,206	132,830,089	138,246,799	142,801,029	151,581,061
120,006,348	122,882,652	124,045,739	124,890,764	77,694,584	88,122,323
10,436,851	5,253,742	1,931,325	5,110,897	2,865,447	1,772,408
130,443,199	128,136,394	125,977,064	130,001,661	80,560,031	89,894,731
933,614	816,722	771,652	-	-	-
285,662,022	265,153,322	259,578,805	268,248,460	223,361,060	241,475,792
\$6,208,432	\$6,272,476	\$6,239,797	\$5,119,047	\$4,293,912	\$2,016,804
2,740,645	2,478,238	1,778,186	2,732,956	2,517,129	6,074,980
18,535,695	5,665,557	274,081	1,301,346	(339,930)	-
-	-	-	-	-	-
27,484,772	14,416,271	8,292,064	9,153,349	6,471,111	8,091,784
2,895,385	2,510,085	2,485,977	2,458,379	2,629,850	2,300,026
4,505,158	4,495,971	4,482,820	4,426,113	4,792,037	4,803,549
7,400,543	7,006,056	6,968,797	6,884,492	7,421,887	7,103,575
20,084,229	7,410,215	1,323,267	2,268,857	(950,776)	988,209
(373,899)	-	-	-	-	14,360
51,743	407,622	396,391	861,775	184,332	293,709
(2,665,310)	(4,901,784)	(7,574,948)	(4,833,300)	(3,918,240)	(3,411,937)
17,096,763	2,916,053	(5,855,290)	(1,702,668)	(4,684,684)	(2,115,659)
148,865	(414,376)	(508,791)	(4,593,787)	8,085,876	1,287,306
799,296	868,328	868,328	306,327	-	-
40,079	112	79,043	1,435,898	(12,181,224)	3,060,607
\$18,085,003	\$3,370,117	(\$5,416,710)	(\$4,554,230)	(\$8,780,032)	\$2,232,254

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATEMENTS OF NET POSITION

	ASSETS		RWSS		ADJUSTMENTS		TACOMA WATER STATEMENTS	
	UTILITY PLANT	W/O RWSS	W/O RWSS	RWSS	ADJUSTMENTS		STATEMENTS	
In Service, at Original Cost		\$ 754,566,673	\$ 754,566,673	\$ 343,869,539	\$ -	\$	\$ 1,098,436,212	
Less - Accumulated Depreciation		(171,081,256)	(171,081,256)	(65,738,167)	-		(236,819,423)	
Total		583,485,417	583,485,417	278,131,372	-		861,616,789	
Construction Work In Progress		10,843,046	10,843,046	1,058,938	-		11,901,984	
Net Utility Plant		594,328,463	594,328,463	279,190,310	-		873,518,773	
NET UTILITY PROPERTY		492,963	492,963	-	-		492,963	
SPECIAL FUNDS								
Construction Funds		32,591,351	32,591,351	-	-		32,591,351	
Debt Service Funds		4,065,742	4,065,742	300,423	-		4,366,165	
Bond Reserve Funds		13,575,539	13,575,539	8,394,310	-		21,969,849	
System Development Charge Fund		61,645,713	61,645,713	-	-		61,645,713	
Other Cash & Equity in Pooled Investments		32,371,772	32,371,772	-	1,017,528		33,389,300	
Total Special Funds		144,250,117	144,250,117	8,694,733	1,017,528		153,962,378	
CURRENT ASSETS								
Operating Funds Cash & Equity in								
Pooled Investments		59,076,540	59,076,540	1,017,528	(1,017,528)		59,076,540	
Accounts Receivable		4,721,094	4,721,094	591,206	-		5,312,300	
(Net of Allowance for Doubtful Accounts of \$526,979 in 2017)								
BABs Interest Subsidies Receivable		231,355	231,355	67,585	-		298,940	
Accrued Unbilled Revenues		5,457,221	5,457,221	-	-		5,457,221	
Materials and Supplies		2,403,305	2,403,305	-	-		2,403,305	
Interfund Receivable		66,921	66,921	2,341	-		69,262	
Prepayments		1,170,304	1,170,304	69,372	-		1,239,676	
		73,126,740	73,126,740	1,748,032	(1,017,528)		73,857,244	
OTHER ASSETS								
Regulatory Asset - Public Fire Protection Fees		456,635	456,635	-	-		456,635	
Regulatory Asset - Surcharges		1,353,795	1,353,795	-	-		1,353,795	
Total Other Assets		1,810,430	1,810,430	-	-		1,810,430	
DEFERRED OUTFLOWS OF RESOURCES								
Unamortized Losses on Refunding Bonds		1,123,218	1,123,218	240,210	-		1,363,428	
Pension Contributions		8,671,039	8,671,039	-	-		8,671,039	
Total Deferred Outflows		9,794,257	9,794,257	240,210	-		10,034,467	
TOTAL ASSETS AND DEFERRED OUTFLOWS		\$ 823,802,970	\$ 823,802,970	\$ 289,873,285	\$ -		\$ 1,113,676,255	

NET ASSETS AND LIABILITIES									
NET ASSETS		WATER		RWSS		ADJUSTMENTS		WATER STATEMENTS	
		W/O	RWSS						
Invested in Capital Assets, Net of Related Debt	\$	271,819,740	\$	174,175,516	\$	-	\$	445,995,256
Restricted for:									
Water Capital and System Development Charge		50,149,083		-		-		50,149,083
Debt Service Funds		2,654,379		(148,101)		-		2,506,278
Unrestricted		57,391,917		674,101		-		58,066,018
Total Net Position		382,015,119		174,701,516		-		556,716,635
LONG-TERM DEBT									
Revenue Bonds		265,400,935		112,594,314		-		377,995,249
Public Works Trust Fund Loans		20,011,236		-		-		20,011,236
Drinking Water State Revolving Fund Loan		65,612,800		-		-		65,612,800
Total Long-Term Debt			351,024,971		112,594,314		-		463,619,285
CURRENT LIABILITIES									
Current Maturities of Long-Term Debt		12,323,017		1,055,000		-		13,378,017
Current Maturities of Long-Term Liabilities		181,355		-		-		181,355
Accrued Taxes		1,556,338		-		-		1,556,338
Accrued Expenses and Contracts Payable		1,375,280		(6,046)		-		1,369,234
Salaries, Wages and Fringe Benefits Payable		725,775		-		-		725,775
Interest Payable		1,411,363		448,524		-		1,859,887
Customers' Deposits		356,929		-		-		356,929
Interfund Payables		1,029,947		66,882		-		1,096,829
Total Current Liabilities		18,960,004		1,564,360		-		20,524,364
LONG-TERM LIABILITIES									
Muckleshoot Agreements		6,762,451		-		-		6,762,451
Customer Advances for Construction		5,905,910		-		-		5,905,910
Unearned Revenue		6,596,724		1,013,095		-		7,609,819
Long-Term Accrued Compensated Absences		2,068,503		-		-		2,068,503
Pension Liability		8,278,522		-		-		8,278,522
Other Long-Term Liabilities		4,831,577		-		-		4,831,577
Total Long-Term Liabilities		34,443,687		1,013,095		-		35,456,782
DEFERRED INFLOWS OF RESOURCES									
Rate Stabilization		35,575,447		-		-		35,575,447
Pension Contribution		1,783,742		-		-		1,783,742
Total Inflows of Resources		37,359,189		-		-		37,359,189
TOTAL NET POSITION, LIABILITIES, AND DEFERRED INFLOWS									
		\$	823,802,970		\$ 289,873,285		\$ -		\$ 1,113,676,255

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	WATER		RWSS		ADJUSTMENTS		TACOMA WATER
	W/O RWSS						STATEMENTS
OPERATING REVENUES							
Sale of Water	\$	79,999,893	\$	-	\$	-	\$ 79,999,893
Other Operating Revenues		10,059,774		-		-	10,059,774
Contract Resource Obligation Revenues		-		9,615,085		(5,030,331)	4,584,754
Total Operating Revenues		90,059,667		9,615,085		(5,030,331)	94,644,421
OPERATING EXPENSES							
Operations		17,704,426		176,750		-	17,881,176
Production		11,309,215		3,492,286		-	14,801,501
Administrative and General		21,186,820		212,650		(5,030,331)	16,369,139
Depreciation		15,771,418		8,266,685		-	24,038,103
Taxes		4,776,164		-		-	4,776,164
Total Operating Expenses		70,748,043		12,148,371		(5,030,331)	77,866,083
Net Operating Income		19,311,624		(2,533,286)		-	16,778,338
NON-OPERATING REVENUES (EXPENSES)							
Interest Income		1,671,259		91,554		-	1,762,813
Other		1,216,295		-		-	1,216,295
Interest on Long-Term Debt		(14,586,802)		(5,428,377)		-	(20,015,179)
Amortization of Premium and Loss on Refunding		655,255		698,999		-	1,354,254
Interest Charged to Construction		308,461		31,379		-	339,840
Total Non-Operating Expenses		(10,735,532)		(4,606,445)		-	(15,341,977)
Net Income Before Capital Contributions and Transfers		8,576,092		(7,139,731)		-	1,436,361
Capital Contributions							
Cash		5,331,596		179,156		-	5,510,752
Donated Fixed Assets		3,627,682		-		-	3,627,682
Federal BABs Subsidies		2,772,542		809,933		-	3,582,475
Transfers							
City of Tacoma Gross Earnings Tax		(7,143,861)		-		-	(7,143,861)
Transfer to/from Other Funds		51,000		-		-	51,000
CHANGE IN NET POSITION		13,215,051		(6,150,642)		-	7,064,409
TOTAL NET POSITION - BEGINNING OF YEAR		368,800,068		180,852,158		-	549,652,226
TOTAL NET POSITION - END OF YEAR		\$ 382,015,119		\$ 174,701,516		\$ -	\$ 556,716,635

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

BOND DEBT SERVICE REQUIREMENTS
DECEMBER 31, 2017

YEAR	WATER W/O RWSS		RWSS		TOTAL
	PRINCIPAL	INTEREST	PRINCIPAL	INTEREST	
2018	5,395,000	13,308,633	1,055,000	5,382,286	25,140,919
2019	5,620,000	13,092,833	1,990,000	5,335,336	26,038,169
2020	5,850,000	12,852,833	2,100,000	5,241,836	26,044,669
2021	6,150,000	12,560,333	2,205,000	5,143,036	26,058,369
2022	6,410,000	12,297,633	2,315,000	5,035,935	26,058,568
2023	6,240,000	11,977,133	2,455,000	4,923,486	25,595,619
2024	4,300,000	11,665,133	4,930,000	4,804,186	25,699,319
2025	4,465,000	11,460,042	5,190,000	4,561,236	25,676,278
2026	4,930,000	11,244,560	5,420,000	4,300,364	25,894,924
2027	5,085,000	11,003,926	5,700,000	4,027,936	25,816,862
2028	5,265,000	10,730,811	5,970,000	3,741,451	25,707,262
2029	5,445,000	10,448,028	6,300,000	3,441,430	25,634,458
2030	5,640,000	10,155,577	6,595,000	3,124,854	25,515,431
2031	5,835,000	9,852,652	6,880,000	2,855,021	25,422,673
2032	6,050,000	9,524,667	6,660,000	2,572,446	24,807,113
2033	11,915,000	9,184,597	4,495,000	2,298,427	27,893,024
2034	12,360,000	8,502,115	4,655,000	2,045,763	27,562,878
2035	12,820,000	7,794,144	4,830,000	1,784,105	27,228,249
2036	13,295,000	7,059,824	5,005,000	1,512,611	26,872,435
2037	13,790,000	6,298,290	5,185,000	1,231,280	26,504,570
2038	14,305,000	5,508,406	5,375,000	939,831	26,128,237
2039	14,835,000	4,689,020	5,570,000	637,703	25,731,723
2040	15,390,000	3,839,272	5,775,000	324,613	25,328,885
2041	23,820,000	2,974,200	-	-	26,794,200
2042	24,770,000	2,021,400	-	-	26,791,400
2043	25,765,000	1,030,600	-	-	26,795,600
	<u>\$265,745,000</u>	<u>\$231,076,662</u>	<u>\$106,655,000</u>	<u>\$75,265,172</u>	<u>\$678,741,834</u>

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER
without RWSS
FUNDS AVAILABLE FOR DEBT SERVICE

	2017	2016	2015	2014	2013
Total Income	\$98,305,474	\$94,688,383	\$92,203,086	\$86,134,608	\$77,677,321
Less: Operating Exp	54,976,625	52,762,243	48,438,968	43,722,021	41,649,837
Income Available for Debt Service	<u>\$43,328,849</u>	<u>\$41,926,140</u>	<u>\$43,764,118</u>	<u>\$42,412,587</u>	<u>\$36,027,484</u>
Bond Redemption	5,216,251	5,140,416	4,873,754	5,551,250	6,957,496
Bond Interest	13,447,439	13,156,254	13,913,407	14,303,864	14,032,328
Debt Service Payable	<u>\$18,663,690</u>	<u>\$18,296,670</u>	<u>\$18,787,161</u>	<u>\$19,855,114</u>	<u>\$20,989,824</u>
Times Debt Service Covered	2.32	2.29	2.33	2.14	1.72

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

SUMMARY OF WATER SALES - 2017

	AVERAGE MONTHS BILLED	CONSUMPTION (CCF)	REVENUE	% of TOTAL REVENUE	MGD	% of TOTAL MGD
RESIDENTIAL AND DOMESTIC SERVICE						
Inside City						
Single and Multiple House	55,629	4,579,323	\$ 22,531,860	28.3%	9.39	18.9%
Multiple Unit Dwellings	3,230	1,631,136	\$ 5,616,852	7.0%	3.34	6.8%
Parks & Irrigation Services	183	102,780	\$ 427,550	0.5%	0.21	0.4%
Private Fire Services	104	869	\$ 81,344	0.1%	0.00	0.0%
	59,146	6,314,108	\$ 28,657,606	35.9%	12.94	26.1%
Outside City						
Single and Multiple Houses	34,003	3,556,737	\$ 18,864,255	23.7%	7.29	14.8%
Multiple Unit Dwellings	1,845	1,024,559	\$ 4,350,874	5.4%	2.10	4.3%
Parks & Irrigation Services	237	134,960	\$ 631,483	0.8%	0.28	0.6%
Private Fire Services	75	4	\$ 35,425	0.0%	0.00	0.0%
	36,160	4,716,260	\$ 23,882,037	29.9%	9.67	19.7%
COMMERCIAL AND INDUSTRIAL SERVICE						
Inside City						
Large Volume Service	2	303,552	\$ 517,439	0.6%	0.62	1.3%
General Service	3,799	2,323,594	\$ 8,074,712	10.1%	4.76	9.6%
Parks & Irrigation Services	372	362,735	\$ 1,527,724	1.9%	0.74	1.5%
Private Fire Services	1,062	6,061	\$ 2,472,861	3.1%	0.01	0.0%
	5,235	2,995,942	\$ 12,592,736	15.7%	6.13	12.4%
Outside City						
Large Volume Service	4	623,904	\$ 1,267,171	1.6%	1.28	2.6%
General Service	994	465,831	\$ 2,021,801	2.5%	0.96	1.9%
Parks & Irrigation Services	95	123,371	\$ 574,501	0.7%	0.25	0.5%
Private Fire Services	219	864	\$ 952,320	1.2%	0.00	0.0%
	1,312	1,213,970	\$ 4,815,793	6.0%	2.49	5.0%
WESTROCK	1	7,606,966	\$ 6,322,195	7.9%	15.59	31.6%
WHOLESALE	17	1,250,618	\$ 3,069,448	3.8%	2.56	5.2%
Unbilled Revenue			\$ 660,078	0.8%		
TOTAL WATER SALES	101,871	24,097,864	\$ 79,999,893	100.0%	49.38	100.0%

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATISTICS
AS OF DECEMBER 31, 2017

Tacoma Water System:		
Average daily delivery exclusive of pulp mill		37.80 MG
Average daily delivery of pulp mill		15.68 MG
Total average daily delivery		<hr/> 53.48 MG
Maximum daily production	8/2/2017	90.99 MG
Minimum daily production	1/25/2017	29.42 MG
Total water produced in 2017*		19,512 MG
Regional Water Supply System (RWSS):		
Total average daily delivery		13.98 MG
Average daily consumption per single family residential service (Inside City)		168.7 GPD
Miles of transmission and wells supply mains - 28" to 96" diameter (includes North Fork wells system)		150 mi
Miles of distribution mains - 2" to 24" in diameter		1,259.80 mi
Fire Hydrants (Inside)		6,085
Fire Hydrants (Outside)		4,770

The primary source of Tacoma's water supply is the Green River. Additionally the North Fork well field provides blending options during periods of excessive river turbidity. The Green River source consists of a 73 million gallons per day (MGD) water right. Tacoma is also partner in the Regional Water Supply System (RWSS) and holds a 27 MGD average share of that 64.6 MGD interruptible, junior water right on the Green River. Tacoma also has ground water rights totaling 87 MGD with an installed pumping capacity of 55 MGD.

Tacoma's water supply is robust and of very high quality, benefiting from decades of source protection and substantial investment in treatment. City of Tacoma business and residents continued to receive extraordinary service reliability while meeting or exceeding all regulatory requirements of the United States Environmental Protection Agency and the Washington Department of Health.

Storage facilities are provided at 15 locations. These facilities consist of 10 concrete tanks and 12 steel standpipes. The combined storage capacity is equal to approximately 140.7 million gallons. Of this storage capacity 67.6 million gallons are located at the McMillin Reservoir approximately 14 miles southeast of Tacoma.

**Includes losses and water for self-consumption excludes RWSS*

MG equals million gallons

GPD equals gallons per day

mi equals miles

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

TAXES AND EMPLOYEE WELFARE CONTRIBUTIONS
FOR THE YEAR 2017

FEDERAL

Social Security (FICA)		\$1,590,162
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STATE OF WASHINGTON

Retail Sales Tax	560,978	
Utilities and Business Activities Tax	4,115,951	
Total		4,676,929

COUNTY

Real Property	46,901	
Total		46,901

MUNICIPALITIES

City of Tacoma Gross Earnings Tax	7,143,861	
City of Fircrest Administrative Fee	6,586	
City of Lakewood Administrative Fee	5,472	
City of Puyallup Administrative Fee	19,414	
City of University Place Administrative Fee	615,540	
		7,790,873

TOTAL TAXES		<u>\$14,104,865</u>
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Taxes as a % of Non-CRO Revenues of \$90,059,667 ..		15.66%
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EMPLOYEE WELFARE CONTRIBUTIONS

Industrial Insurance and Medical Aid	\$526,549
Pensions	\$2,107,449
Medical Insurance	\$3,928,992
Dental Insurance	\$346,026

TOTAL EMPLOYEE WELFARE CONTRIBUTIONS	<u>\$6,909,016</u>
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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

2017 WATER RATES

			READY TO SERVE CHARGE PER MONTH	
			INSIDE TACOMA	OUTSIDE TACOMA
METER SIZE				
5/8	inch	.....	\$21.20	\$25.44
3/4	inch	.....	\$31.80	\$38.16
1	inch	.....	\$53.00	\$63.60
1-1/2	inch	.....	\$106.00	\$127.20
2	inch	.....	\$169.60	\$203.52
3	inch	.....	\$318.00	\$381.60
4	inch	.....	\$530.00	\$636.00
6	inch	.....	\$1,060.00	\$1,272.00
8	inch	.....	\$1,696.00	\$2,035.20
10	inch	.....	\$2,438.00	\$2,925.60
12	inch	.....	\$3,577.50	\$4,293.00

			CHARGE FOR WATER USED PER MONTH PER 100 CUBIC FEET	
			INSIDE TACOMA	OUTSIDE TACOMA
<u>Residential Service</u>				
Each 100 cubic ft. of water consumption during the winter months of October through May			\$1.825	\$2.190
First 500 cubic ft. of water consumption per month during the summer months of June through September			\$1.825	\$2.190
Each 100 cubic ft. of water consumption over 500 cubic ft. during the summer months of June through September			\$2.281	\$2.738
<u>Commercial and Industrial</u>				
General Service			\$2.032	\$2.438
Large Volume Service (over 65,000 cubic feet annually)			\$1.666	\$1.999
<u>Parks and Irrigation Service</u>				
Each 100 cubic feet of water consumption			\$3.115	\$3.738

City of Tacoma water services are 100% metered.

Where service conditions are considered extraordinary, the Water Division may, with City Council approval, enter into contracts for periods up to 20 years.

Water rates were established by Ordinance No. 28423 and were effective April 1, 2017.

Residential service rate for outside Tacoma does not include Fircrest, Puyallup, University Place, and Lakewood.

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

2017 FIRE PROTECTION RATES

RATES FOR PRIVATE FIRE PROTECTION SERVICE ON A SEPARATE METER INSIDE THE CITY OF TACOMA ARE AS FOLLOWS:

METER SIZE		MONTHLY CHARGE	WATER INCLUDED FOR MONTHLY LEAKAGE AND TESTING PURPOSES (100 Cubic Feet)
2	inch	\$25.89	2.99
3	inch	\$37.70	2.99
4	inch	\$62.98	2.99
6	inch	\$141.27	2.99
8	inch	\$251.49	2.99
10	inch	\$393.37	2.99
12	inch	\$629.19	2.99

No charge is made for water used through a fire service in extinguishing fires of incendiary or accidental origin if the customer, at the location where the use occurs, gives written notice to the Division within ten days from the time of such fire. Use of water through a fire service for purposes other than extinguishing fires of incendiary or accidental origin is charged as follows:

MONTHLY CHARGE

12 times the monthly service charge (minimum).

CONSUMPTION

Rates per 100 cubic feet per month \$3.960

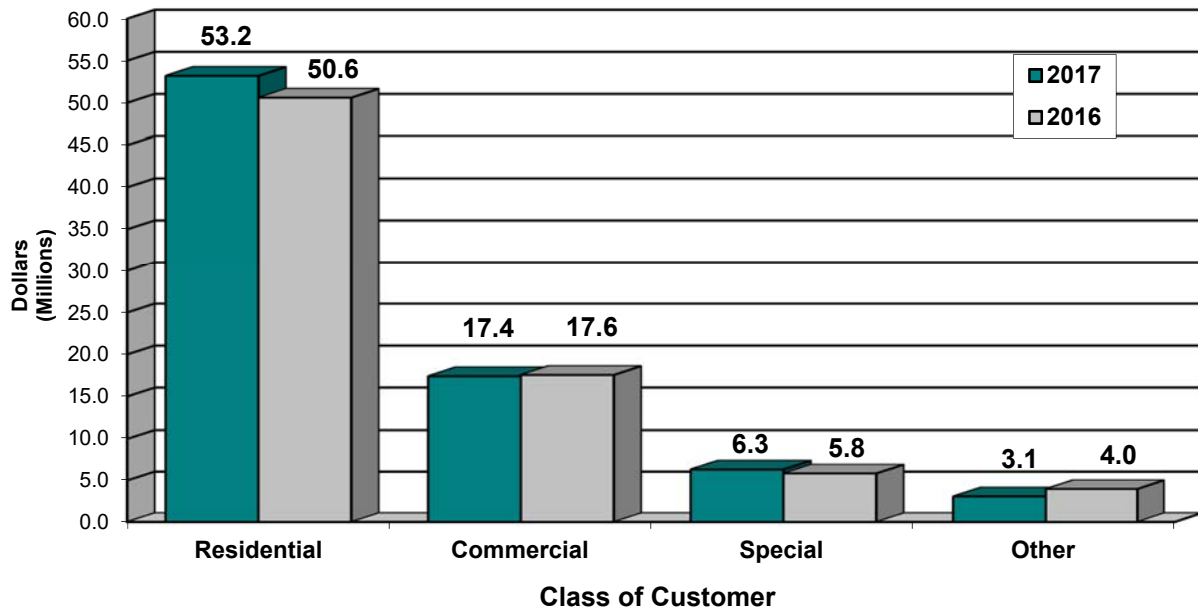
The above rates for fire service shall apply where City water is used for all purposes on such premises exclusive of that amount allowed for testing and leakage.

Costs associated with fire hydrant services are currently recovered from customers in two different ways, depending on their location in the service area. Customers outside the City of Tacoma with residential and commercial accounts pay a flat monthly franchise "Franchise Hydrant Service Fee" as shown below:

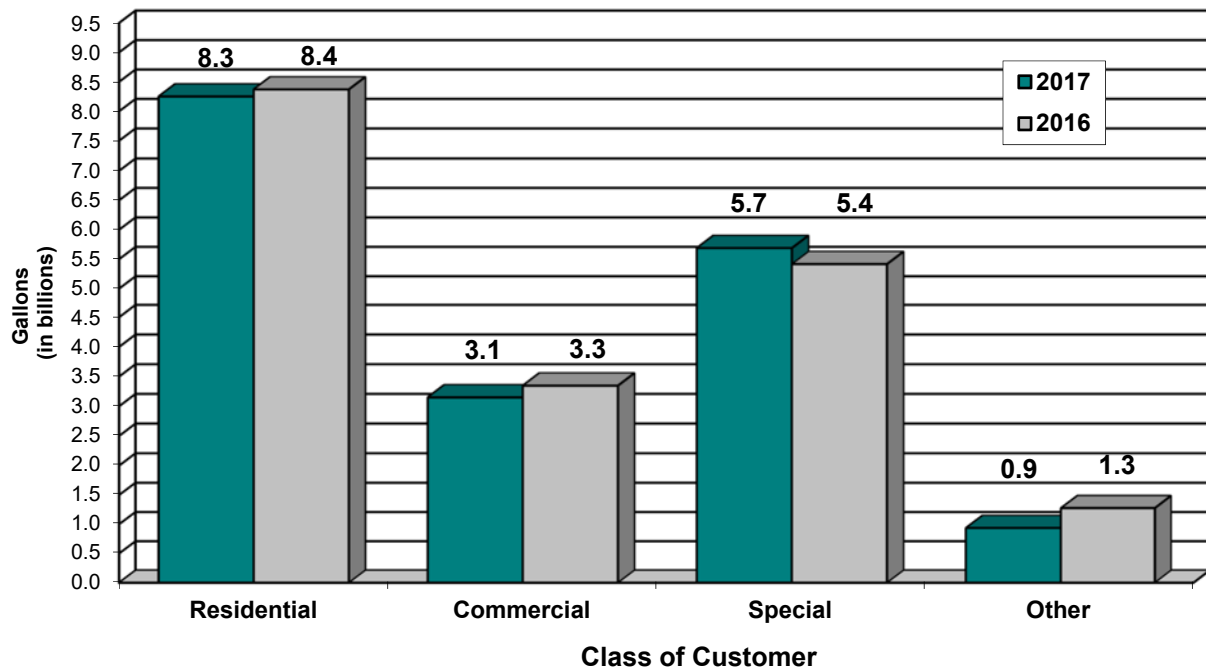
Outside City, other contract.....	\$4.752
Fircrest Franchise.....	\$4.752
Lakewood, Puyallup, and University Place Franchises.	\$4.752

The Fire Protection Rates were established by Ordinance No. 28423 and were effective April 1, 2017.

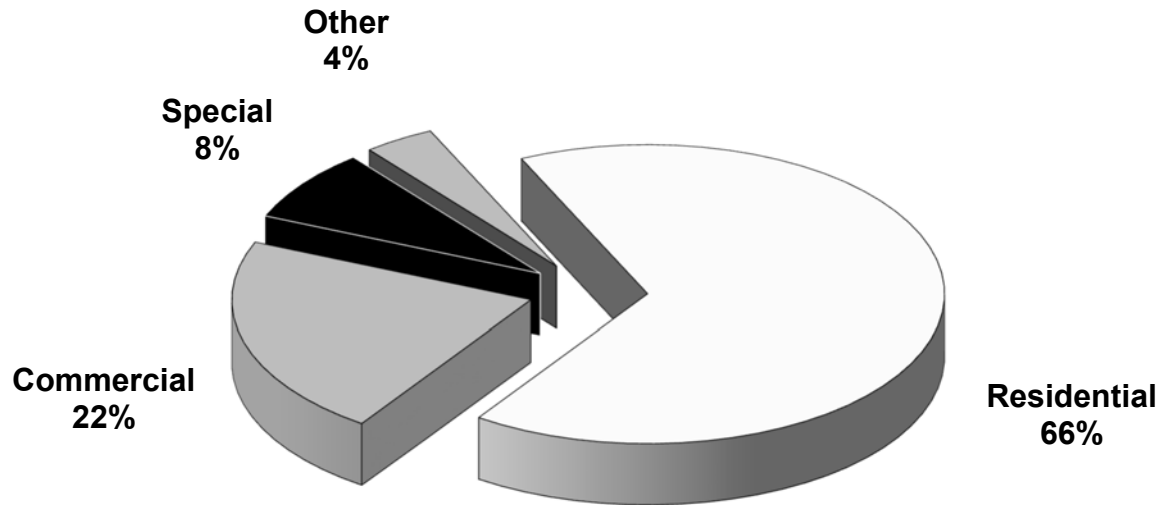
WATER SALES
Year to Date - December 2017 & 2016



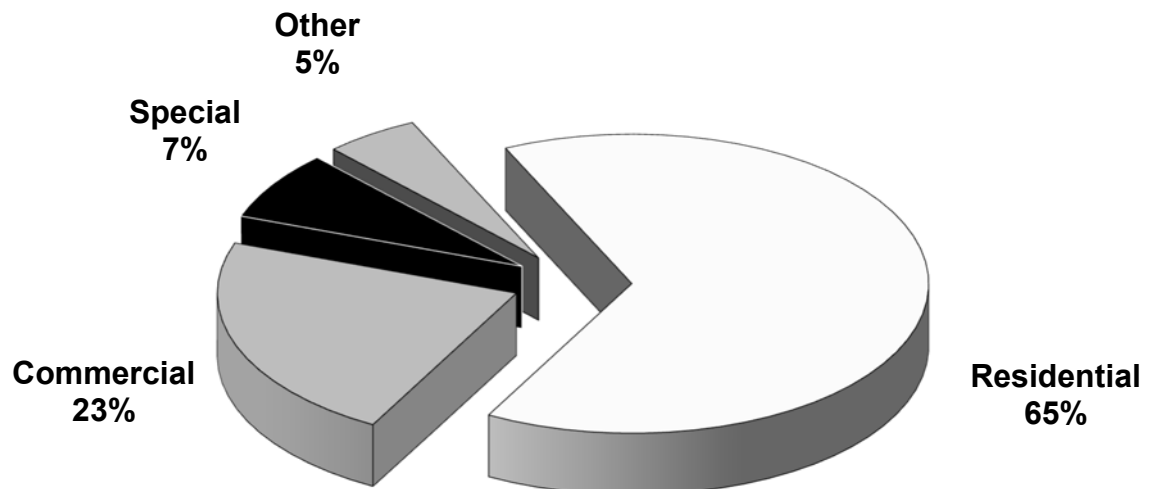
WATER CONSUMPTION
Year to Date - December 2017 & 2016



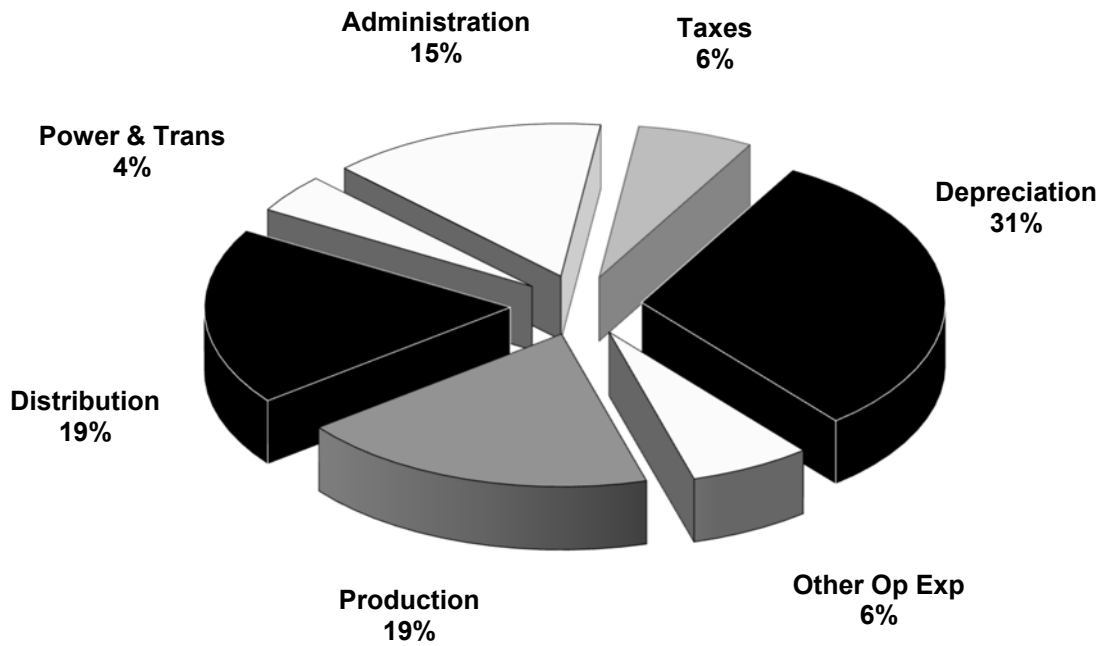
WATER SALES
Year to Date - December 2017
(\$79,999,893)



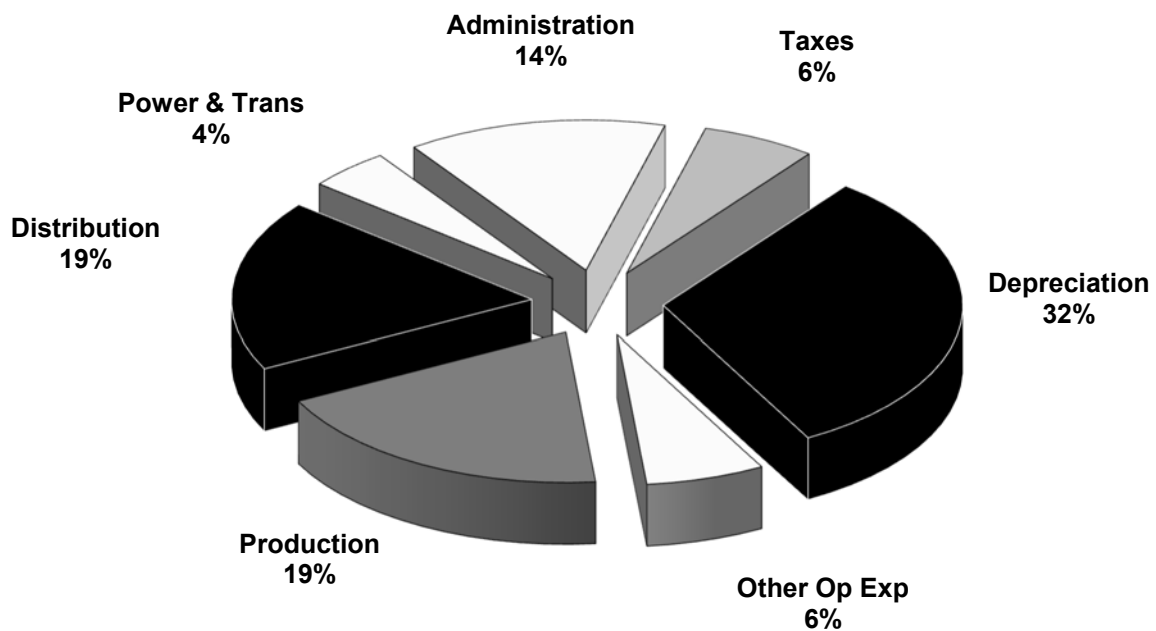
WATER SALES
Year to Date - December 2016
(\$77,980,741)



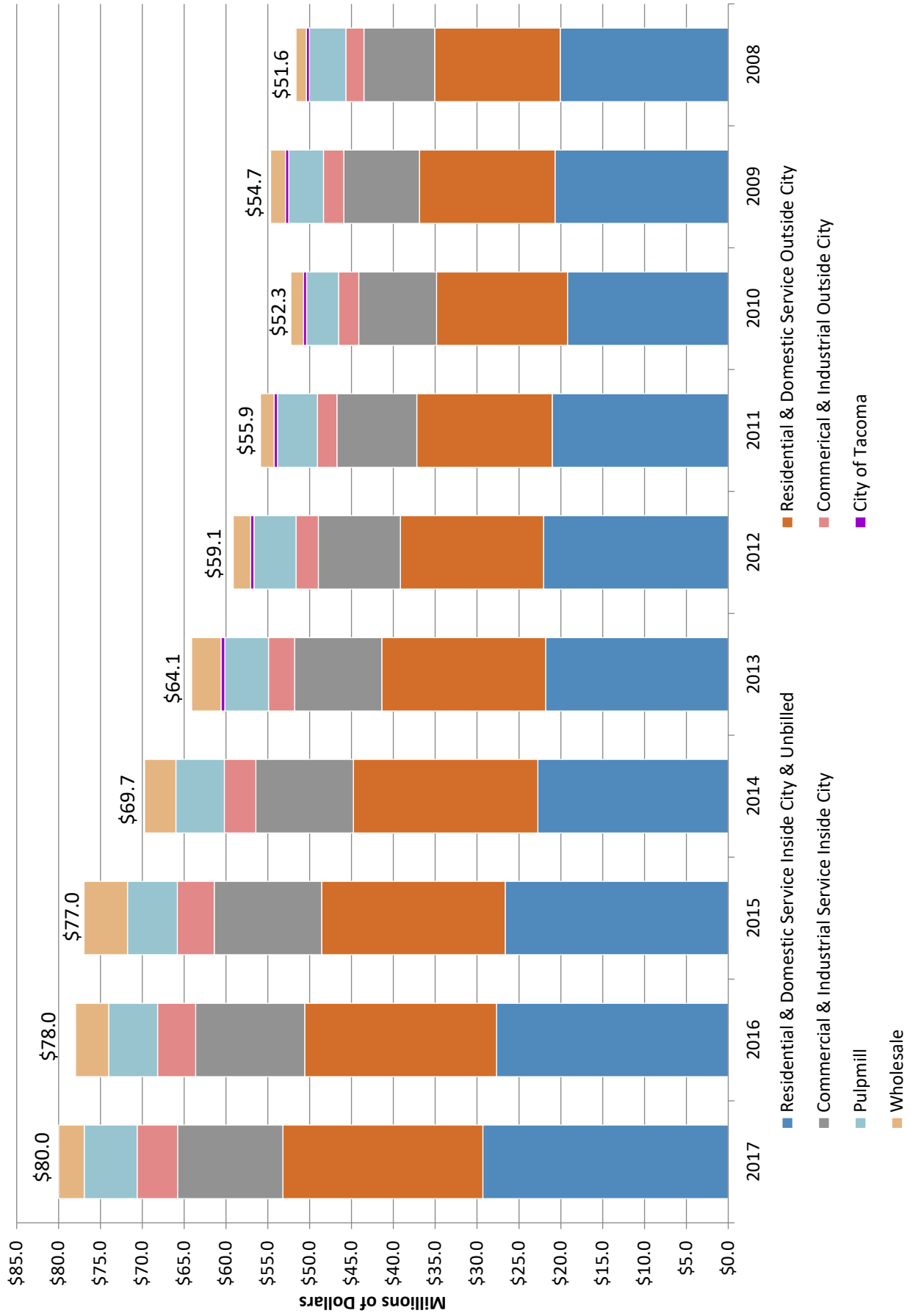
TOTAL OPERATING EXPENSES
Year to Date - December 2017
(\$77,866,083)



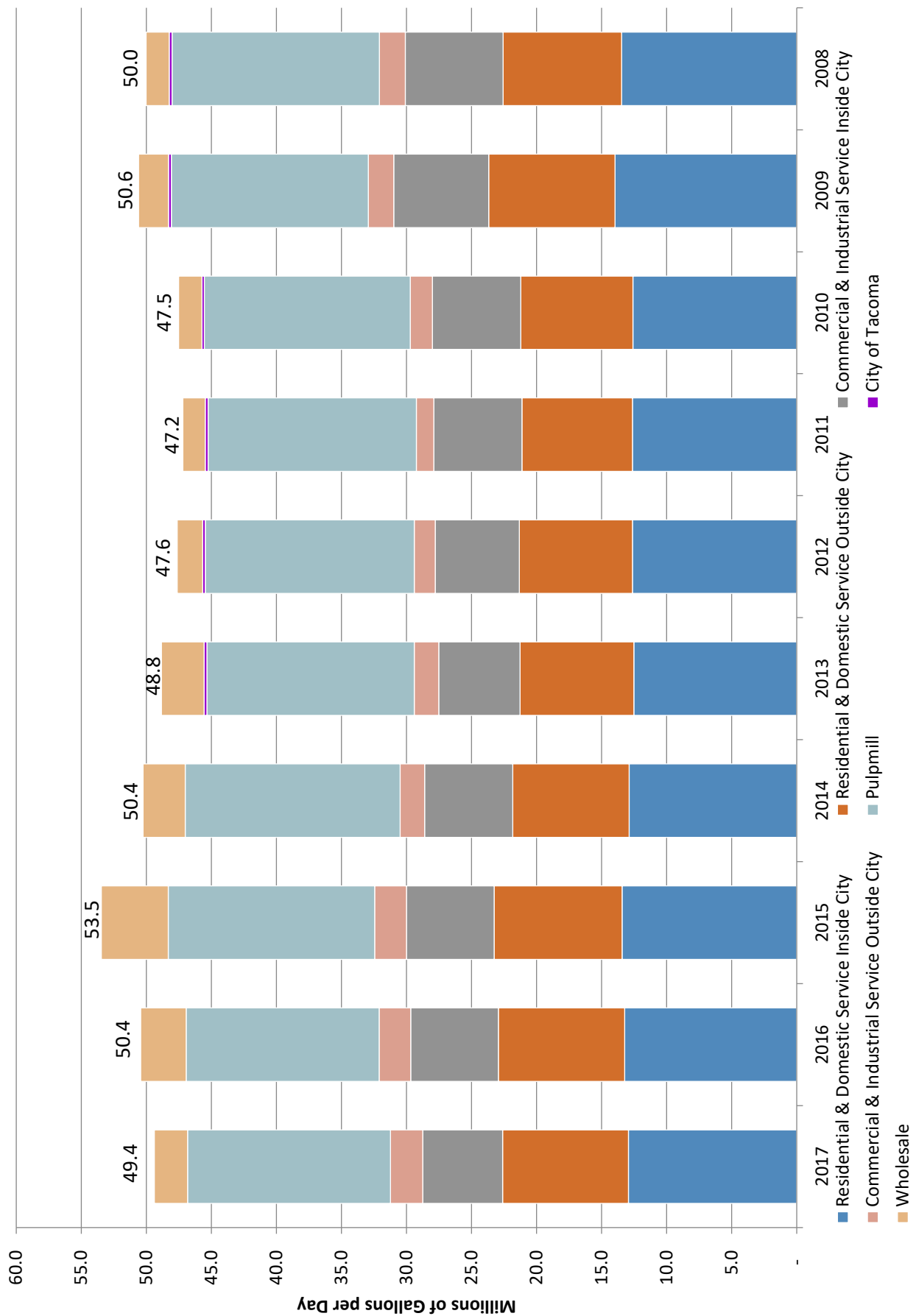
TOTAL OPERATING EXPENSES
Year to Date - December 2016
(\$75,355,921)



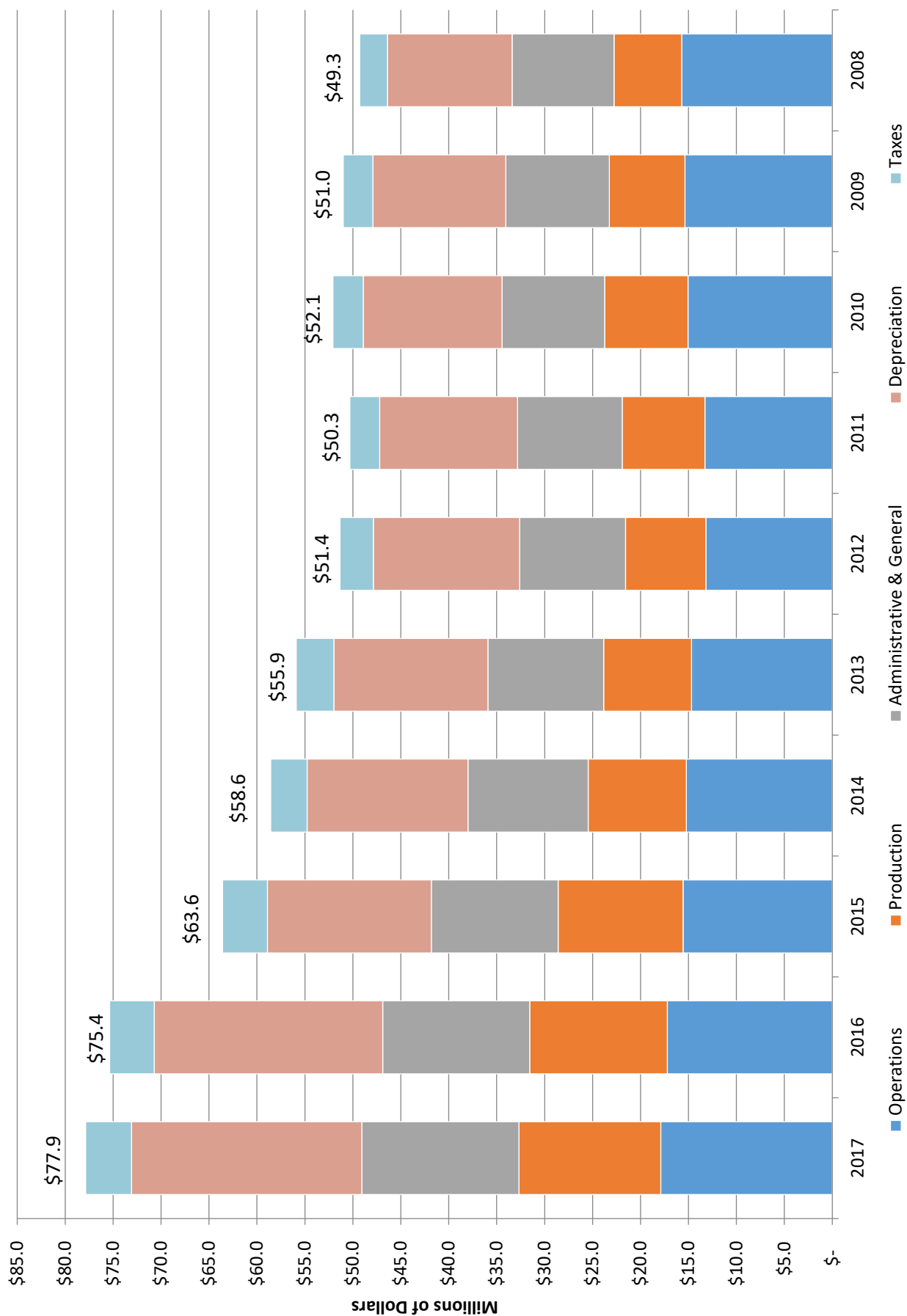
TEN-YEAR SUMMARY OF WATER SALES (MILLIONS OF \$)



TEN-YEAR SUMMARY OF WATER DEMAND (MGD)



TEN-YEAR SUMMARY OF O&M EXPENSE (MILLIONS OF \$)



2017 SUPERINTENDENT'S REPORT TACOMA WATER

2017 was a year of transition at Tacoma Water with the retirement of Linda McCrea, a long-time employee and water superintendent. Likewise for me as the new superintendent, moving from Virginia to Washington was a major change! Joining Tacoma Water in October, I have spent my first few months working hard to get to know the staff and trying to understand the most pressing issues here. In many ways it is striking how similar utilities are across the country. One thing I have noted is the depth of talented staff at Tacoma Water and how hard they work every day to ensure that our customers have reliable, safe, clean drinking water. It is my pleasure to share with you now the major accomplishments of 2017 and provide a glimpse into where we are moving in 2018!

One of the major tasks this year was to update the Water System Plan (WSP). Our primary regulatory agency, the Washington Department of Health (WDOH), requires the WSP be updated every 10 years. This was an update to the plan submitted in July 2007. It involved a complete review of the entire water system from source to treatment to transmission and distribution to all of our customers. As part of the process, the sub systems that make up the distribution system were analyzed in depth to ensure compliance with WDOH regulations and to verify that the system is properly planned to accommodate growth and other needs.

Coupled with the Water System Plan update was the development of an Integrated Resource Plan (IRP). Tacoma Water has robust and diversified sources of supply from the Green River to high production groundwater wells. One of the outputs of the IRP is a model that will allow Tacoma Water to know how best to use each of these sources year-to-year and season-to-season based on environmental conditions. A more detailed discussion of the IRP process is provided in the Water Supply section.

Finally, another key initiative that you will read about in more detail is what has been termed "planning and scheduling." It sounds like a simple concept, but it is truly a paradigm shift into how water utility assets have been managed and cared for in the past. Best practice Strategic Maintenance Management Programs utilize planning and scheduling concepts to ensure overall system reliability, improve safety and environmental compliance, reduce perceived emergencies, improve coordination between operations, maintenance, engineering and the warehouse, and ultimately increase productivity, quality and consistency of operation and maintenance activities. The Strategic Maintenance Management Program (SMMP) ensures Tacoma Water is doing the right thing, the right way at the right time. You will see this topic mentioned in a few different sections in the following paragraphs as each section is implementing this based upon the types of assets they manage.

So I hope you will enjoy a summary of what each of our operating sections has accomplished in 2017.

ASSET & INFORMATION MANAGEMENT

Strategy Management

2017 marked the fifth year of Tacoma Water using a Balanced Scorecard approach to manage strategic work. Each year the strategy map is updated to identify the strategic objectives that will

be addressed in that year. Through strategy management efforts Tacoma Water has worked to ensure that the strategic work is prioritized, adequately resourced, actions are planned, progress measured, and issues resolved.

A total of 9 initiatives were completed in 2017, reflecting significant strategic progress Tacoma Water is making while continuing to provide a high level of reliable, safe, clean water at affordable rates to our customers. Our growing strategy management maturity helped ensure alignment, progress, and continuity during a year of uncertainty and leadership change.

An example of one of the initiatives completed is Si140 - Develop and promote a forum for sharing information about employee development opportunities. Through this initiative, a cross-functional team from across the organization developed a centralized, standardized platform that all employees can access and understand. This effort demonstrates our shared commitment to support, encourage and value employees and foster a culture of continuous employee development. It allows employees to take ownership of their development and facilitates improved discussions with supervisors. This initiative was employee-driven, and it highlights the value of pulling together cross-functional teams at Tacoma Water.

A final note, in 2017 Tacoma Water hired a dedicated Strategy Manager to oversee and facilitate the Strategy Management and Strategic Planning process. For the last several years, these responsibilities have been shared amongst several employees, and the filling of this role should allow those employees to better focus on their primary roles as well as bring more maturity and focus to the Strategy Management program.

Asset Management

Tacoma Water went through some major transitions and endured several personnel changes in 2017 that made meaningful progress on planned Asset Management work challenging.

A large focus on the year was around gaining alignment between Operating Sections and seeking to move together as a cohesive team with respect to implementation of our Strategic Maintenance Management Program. With the forthcoming arrival of a long awaited mobile work management platform on the horizon, much focus was put on trying to better understand our entire work management process and assist sections in documenting both current state and future state processes.

Strategic Maintenance Management Program (SMMP)

- A Planning and Scheduling Steering Team was created to ensure consistency with respect to the implementation of planning and scheduling concepts within each of the operating sections at Tacoma Water by providing the framework and necessary support for this effort.
- Following plans laid in 2016, we finalized a vendor contract to provide coaching, technical documentation and training related to our SMMP and work management efforts for 2017 and 2018.
- Working with the vendor, we documented current business state in a “brown paper” exercise with Distribution Operations.
- Asset Management developed a strawman work management business process diagram that can be used by operating sections as a framework for our desired future state.

Treatment and Monitoring Strategic Asset Management Plan (SAMP)

- In 2017, Asset Management teamed up with the Water Quality section to update the Treatment and Monitoring SAMP. The report now covers the Green River Filtration Facility (GRFF) and the Hood Street groundwater treatment system to our system.
- A large focus on this effort was to document the high level maintenance plan strategies for these facilities, complete a criticality review of the GRFF systems (to aid in work prioritization) and to develop actionable recommendations for future SAMP related work.

Other

- Asset Management supported lead gooseneck planning and coordination including a plan to identify and replace remaining goosenecks and development of a tracking tool. Additionally, over 250 specific services were identified for immediate replacement based on criteria such as street type, coordination with the City and ensuring equitable distribution of the work across our service area.
- Staff developed and completed the Day Island Pressure Release Valve Business Case to identify the best option going forward to deal with a corroded PRV, which if followed will result in a savings of over \$100,000 when compared to our historically preferred option.
- A standard repair plan was developed to successfully retrofit 6 Air Valves on Pipeline 1 to protect against possible cross contamination. Staff worked with crews, planners and warehouse to run the work management through SAP using future state business process.
- Tacoma Water received the PNWS AWWA Excellence in Engineering Award (Planning Category) for our Economic Model.

Information Management

The first Tacoma Water interactive public map is now available on mytpu.org to display hydrant flushing status. It allows our customers to view a map via the internet of the areas we are working in during our annual flushing program.

The Economic Model application was enhanced with new functionality and directly integrated to our asset systems of record.

An emergency GIS map application was developed that allows our staff to view our service area and related assets; disconnected from the internet; during emergency response operations.

A new mobile application was created for capturing system fire flows and storing results on SharePoint.

Tacoma Water's GIS, BlueWave, was updated with 49 construction projects including 3,142 services and 52,567 LF of main and much more.

WATER QUALITY

Lead and Corrosion Control Evaluation

Following the Lead Response in 2016, the Water Quality Section proceeded with bringing in a consulting team of nationally recognized experts to evaluate Tacoma's corrosion control

treatment. Staff constructed 5 experimental pipe loop rigs that allowed for extensive testing of water through a variety of plumbing materials (lead, copper, and brass) harvested from water system customer connections. Weekly samples were collected by staff for 7 months, with all of the data provided to the consulting team. Although the recommendation report won't be finalized until Q1 of 2018, preliminary results indicate that Tacoma Water's current corrosion control treatment approaches (where provided) are successfully reducing the risk of lead being absorbed from customer plumbing fixtures. The final recommendation report will be submitted to the Department of Health, and pending their approval will establish optimized corrosion control treatment requirements for all of Tacoma Water's sources.

In addition to the ongoing work related to the evaluation of the corrosion control treatment process, Water Quality staff continued to process samples and results from the Customer Lead Sampling program. Through the end of 2017, 1,143 lead sample kits were requested by customers, and 570 samples were returned. Of these results, only 2 sample results were above the Action Level of 15 parts per billion (ppb) for Lead, and 89% of the results were below 1 ppb. Water Quality staff followed up with the 2 customers with high results, and follow up sampling results were well below the Lead Action Level for both of these homes.

Green River Filtration Facility (GRFF) Optimization and Filter Surveillance

An engineering consultant was selected through a competitive bid process to help with process optimization and to guide testing for biological activity monitoring. A 2-day workshop was held in September that covered filter evaluation, biological filtration/monitoring, settled turbidity optimization and seasonal manganese control. A schedule was drafted for sample frequency in 2018 and will analyze various water quality parameters and biological activity in order to establish baseline conditions. Core samples of filter media for each season will be collected and analyzed for 2 selected filters evaluating bed expansion percentage, media depth and creating a backwash turbidity profile and solids retention profile. This will allow calibration of the backwash sequence for an optimal duration and flowrate for summer and winter operations.

Green River Filtration Facility (GRFF) Performance Based Training (PBT)

Tacoma Water was invited to participate in the PBT program hosted by the Washington Department of Health along with other major utilities in the state including: Seattle, Everett, City of Bellingham, Pasco, City of Richland, Skagit PUD, City of Anacortes and Yakima. This program is a 15 month commitment designed to create a collaborative group that other operators can gain knowledge and valuable experience on lessons learned and best practices. Three employees from the Green River Filtration Facility were selected to represent Tacoma Water at each of the 3-day workshops, but everyone at the plant is participating in the continued effort to implement changes to further optimize the operations of the GRFF. Tacoma hosted the last session in October of 2017 and the group will be travelling to Skagit PUD the first week in February before wrapping up in June of 2018.

Sawmill Creek Fire

On September 4, a wildfire started in the Sawmill Creek area, near the abandoned town of Lester – part of the Green River Watershed. Tacoma Water activated its Incident Command System (ICS) with Watershed Manager Bryan King serving as the primary Incident Commander. Tacoma Water's ICS was incorporated into a larger Unified Command with Tacoma supporting and coordinating with the Washington Department of Natural Resources by providing access, helping set up camp, assisting with navigation of the watershed, and helping patrol and enforce the closed

area of the fire response. In addition, Water Quality engineering and GRFF operations staff researched the potential wildfire impacts to water quality, evaluated contingency plans if the fire spread rapidly, and developed and implemented a Water Quality Sampling Plan. The fire spread to an approximate 1,061 acres, and was eventually contained to its final boundary as fall rains began. The fire was eventually allowed to burn out until extinguished by winter rains and snows. Tacoma's ICS activation was closed out on October 4.

Watershed Management Plan Update

As part of the Water System Plan update, Water Quality staff were heavily involved in the update of the Watershed Management Plan (part of the Water System Plan). Staff guided the development of the detailed Scope of Work, and provided significant input and review in the drafting of this plan update.

Emergency Response Drills

The Watershed Management group led a planning effort and exercise in coordination with the Burlington Northern-Santa Fe (BNSF) railroad, and the US Army Corps of Engineers (USACOE), simulating a locomotive derailment and oil spill. We now have a cooperative "Spill Response Plan" with BNSF and USACOE, and this drill involved the deployment of absorptive booms in the vicinity of Tacoma Water's intake on the Green River. We believe this to be an important risk issue, and this coordinated response is a strong step forward in preparedness in this area.

Property Management

The Environmental Stewardship Group of Water Quality was involved in a number of significant property sales in 2017, including a portion of the property adjacent to the McMillin Reservoir, Hyada, and the Wapato Triangle sites. We have evaluated all of our property holdings and determined which ones are no longer needed for system growth and are divesting those based on market conditions.

Water System Flushing

Water Quality continued implementation of the revised unidirectional flushing program with assistance from Distribution Operations. We are continuing to collect and evaluate data from the crew work and are developing metrics which can be used to monitor the effectiveness and guide us in decisions related to additional program improvements. Working with Water GIS, we developed and deployed a public facing flushing map that allows our customers to see where our flush crews are and help them plan accordingly to minimize impacts from stirred up sediments in the mains. We also began developing a new flushing app for the crews that will improve how we collect data while minimizing the time impact on the crews in collecting the data. We anticipate rolling out the new app along with other program improvements in 2018.

WATER SUPPLY

Integrated Resource Plan

The Integrated Resource Plan (IRP) will ensure Tacoma Water has sufficient water resources, and provide an effective platform to communicate that capability. The utility primarily relies on its Green River surface water source, which is constrained at times by environmental commitments (such as guaranteed minimum instream flows) and natural weather phenomena. Groundwater is

an important supplemental source, and is used when needed. There are uncertainties regarding drought, climate change, water law, and growth.

We partnered with an engineering consulting firm to develop an analytical model to support a recommended resource strategy and action plan. Three Public Advisory Committee meetings were held in 2017 to increase awareness, solicit input, and inform policy. A Water Yield Supply and Demand Model is in development for both drought management (seasonal projections that can be applied in any given year) and capacity planning (60 years out). A preliminary version of this model was provided in October 2017. Tacoma Water staff are being trained to update, operate, and maintain the model moving forward.

Technical memoranda have been finalized documenting model selection, groundwater resource availability, and conservation program elements. A component of the groundwater review included evaluating the long-standing contamination at Well 12A, and the impact of that contamination on operating rules in place. This review has triggered Tacoma Water to request enhanced participation in the Final Remedy evaluation by the Environmental Protection Agency for the Time Oil Superfund site.

An ongoing delay in receipt of the latest climate change projections for Green River streamflow from the University of Washington Climate Impacts Group (CIG) has affected progress. The latest project schedule indicates a working draft IRP document without model results will be done early 2018. A complete draft with model results will be available in late May, and then the IRP will be finalized in late June.

Water Supply Forum – Resiliency

Building on the Phase I regional work completed in 2016, a Phase II project was initiated in 2017, and remains ongoing. This work builds on several key learnings from Phase I including:

- Development of regional level of service restoration times for water service following design earthquake events (Post earthquake level of service)
- Summarized inventory of key emergency response infrastructure and mutual aid agreements
- Evaluations of peer emergency operating plans
- Enhanced understanding of other key lifeline services affected in a seismic event
- A refined understanding of best practices in pre-event earthquake mitigation strategies
- An analysis of specific stressors that could impact water quality in water systems at a regional scale
- Procedures for restoration of acceptable water quality after a significant event
- Regional workshop on best practices for Climate change modeling

The final reports for these elements will be completed in 2018.

Planning & Scheduling

We continue to create and improve Preventive Maintenance (PMs) plans for all maintenance work that we do. This year we focused on updating existing plans with feedback from the supervisors and field staff. This is the first step in our continual improvement process and will be something we work on every year.

In 2017 we created approximately 2,500 discrete work orders tied to specific locations in our system. These work orders connect specific maintenance/repairs to specific pieces of equipment allowing us to better understand the time and cost of ownership for our assets. There remain opportunities to improve and expand the work captured, and we continue to grow this capability.

Electrical System Improvements

Standby power

Tacoma Water owns a total of 27 standby generators to provide power at critical facilities during utility power outages. Some of these generators have been in service for more than 25 years and show increasing signs of degradation. Following analyses of system risks, replacement of two of these generators was initiated. These upgrades to the electrical system will maintain the desired level of service, reduce system complexity and maintenance, and increase reliability and capacity.

Groundwater control systems

To provide better operational management of the groundwater system, significant control system upgrades were completed in 2017. The upgrades include replacing the Programmable Logic Controller (PLC), power supplies and communication devices. New Operator Touch Panel otherwise known as the Human Machine Interface (HMI) has also been installed to replace the obsolete paper chart recorders. The new HMI provides graphic local control and status and at the same time stores historical data trends of local operating values that makes up the well pumping process. Control system upgrades were completed for five wells this year; a remaining seven wells will be upgraded in 2018.

Seismic Evaluation of Essential Facilities

In 2017, Tacoma Water implemented recommendations contained in the 2016 All-Hazards Vulnerability Assessment (VA) to investigate the seismic resiliency of the Hood Street Reservoir, two buildings adjacent to the Hood Street Reservoir (the chlorination building and the pump station/hydro generation station), the South Tacoma Pump Station, and the Water Operations Building. Through VA analysis process, these facilities were identified as essential infrastructure and initial high level evaluations indicated they would not perform well in seismic events.

A consultant was hired to perform a more detailed seismic evaluation of the reservoir and four buildings. The work in 2017 involved the inspection of the reservoir and the existing buildings, the analysis of the performance of the reservoir and the existing buildings in three specific earthquake scenarios, and the identification of mitigation alternatives for the reservoir and those buildings that did not perform well in the specific earthquake scenarios.

The consultant performed geotechnical analysis of the sites and structural analysis of the reservoir and four buildings. Detailed technical memoranda were prepared identifying geotechnical and structural findings.

In 2018, the results from the investigation will be used to develop mitigation options and a final alternative selection workshop will be convened to determine the best seismic hazard mitigation for these facilities. Design work, though not included in this initial contract, may follow the selection of the final seismic hazard mitigation alternatives.

FINANCE AND ANALYTICS

In 2017, the Water Rates & Financial Planning group changed its name to Finance and Analytics, which reflects the group's recent reorganization and expansion into the areas of organizational performance management and analytics. This reorganization, and the hiring of staff dedicated to both "Financial Stewardship" and "Programs & Analytics" functions of this new group, will enable Tacoma Water to advance its analytical capabilities while continuing to improve financial management.

2017-2018 Cost of Service Rate Adoption and Implementation

Approval from the Tacoma Public Utility Board and City Council was received early in 2017 for a four percent overall rate increase beginning April 1, 2017. The impact to a typical residential bill was about \$1.50 per month. Approval was also received for an additional four percent increase effective January 1, 2018.

Project Management

Tacoma Water completed a project management maturity assessment in 2017, which took stock of Tacoma Water's maturity across "Project Management Knowledge Areas" and "Project Management Process Groups" according to Project Management Institute (PMI) standards. Because the organization scored low in a variety of areas, the assessment resulted in a number of recommendations to improve project management maturity over time, to include the development of a common project management lexicon, development and publication of an electronic "PM Notebook," staff training and the deployment of project management tools.

Tacoma Water also completed an initiative to improve capital project reporting through a system of capital reports that are made visible to the entire organization and updated on a quarterly basis.

Advanced Metering Infrastructure (AMI)

The Public Utility Board approved AMI as a "project of limited duration" in 2017, which provided conceptual support for the project and enabled the hiring of critical project staff to formally begin the project, to include the hiring of an AMI Program Manager. A series of business process workshops were conducted in late 2017 which set the table for procurement of meters and a meter data management system in early 2018.

Wholesale Market Pricing Development

Water achieved conceptual support from executive leadership to move forward with a holistic evaluation of its fixed fees, system development charge, and wholesale pricing platform, to include associated policy development. Tacoma Water met with its wholesale customers in September to discuss the current state of the regional wholesale market, and some of the concepts that will be considered in the coming year.

DISTRIBUTION ENGINEERING

Lead Gooseneck Replacement Plan

Distribution Engineering, Distribution Operations and Asset & Information Management collaborated to develop a Lead Gooseneck Replacement Plan. The replacement plan lays out means for removing all of the 1,215 suspected lead goosenecks from the distribution system within the next five years. The project's objectives will complete the work in a geographically equitable manner, provide relevant regular communication to staff and public, and involve a coordinated effort with area partners in an effort to minimize disruptions to staffing levels and planned work. The plan has been implemented and 226 suspected lead gooseneck locations were either removed or verified not to have a gooseneck by Distribution Operations staff in 2017.

System Acquisition

On November 1, 2017, Tacoma Water took over system operation of the Curran Road Mutual Water Association water system. Tacoma Water and Curran Road staff worked collaboratively to transition more than 620 accounts to Tacoma Water. Design for initial main replacement projects has begun, with main replacement work continuing for the next 8-10 years. Improvements to the acquired water system will be paid for through a customer surcharge for those customers living within the former Curran Road service area.

Main Replacement Program

Over 7 miles of new distribution main was added to the system and 31 design plans were completed for new developments. Approximately 2 miles of distribution main were replaced in 2017 as prioritized through the distribution mains economic model. Almost 13 miles of distribution mains were added to the system through the acquisition of Curran Road Mutual Water Association.

In 2017, Tacoma Water was the recipient of the PNWS AWWA Award for Engineering Planning Excellence for the development and use of the Distribution Mains Economic Model.

Tacoma Water has worked with the Department of Public Works and Sound Transit to develop final plans for the extension of the Tacoma Link Light Rail system. Due to the location of the proposed tracks, nearly two miles of water main will be replaced to facilitate the construction of the Light Rail extension.

Decant Facility

Tacoma Power and Tacoma Water collaborated to develop a bid package for a shared decant facility located at Tacoma Power's Southwest Substation. The decant facility is being constructed in response to concerns from the Tacoma Pierce County Health Department regarding how hydro-excavated soil is managed. The new decant facility will comply with requirements for the handling of solid waste, and protect groundwater resources in the South Tacoma Groundwater Protection District. Completion of the decant facility is expected in mid-2018.

Conservation and Efficiency Programs

Tacoma Water created a new ten-year conservation plan and goal, using valuable feedback from staff, stakeholder groups, and public input. In 2017, our conservation program attended 20 community events, totaling over 1,700 conversations about conservation with our customers. We gave out over 1,400 water-efficient showerheads and over 1,500 faucet aerators. Working with TPU's account executives, we also completed two water conservation rebate projects with Multicare, which are estimated to save over 7 million gallons per year.

New Services

The Customer Support Group continued to execute at a high level to meet the developer demand for the construction of schools, short plats, shopping centers, restaurants, residential homes and apartments. The workload production statistics match the sentiment around the Puget Sound region regarding economic development for new business and real estate. We saw numbers that are close to the peak economic period boom from a decade ago.

In 2017, we created over 1,000 fixed fee orders, which was near the average from 2004-2008, and is over triple the amount from the low of 297 in 2010. The number of time and material orders remained strong and steady compared to the past 5 years bringing in a record breaking \$2 million for private development work. Pierce County growth was the strongest we've seen since 2010, we issued a record breaking 250 water availability letters for development. It was the second year for the Permit Counter to serve the walk-in customers in the TPU Main Lobby through the Qmatic queuing system serving over 1,000 walk-in customers.

H2O TO GO – Water Bottle Refill Stations

Tacoma Water partnered with Metro Parks Tacoma to install its first combination water bottle refill station-drinking fountain and water conservation messaging at the STAR Community Center in South Tacoma. The project goal is to communicate the value of Tacoma's water to customers by linking tap water to the Green River, to promote thoughtful and efficient water use and water as a renewable resource. Further installations are planned for 2018 and beyond with additional partners that include the City of Tacoma Public Works Department and Tacoma Pierce County Health Department.

DISTRIBUTION OPERATIONS

Construction

New water service installations were up from a year ago totaling 1,060, and the number of new meter installations increased significantly for the second year in a row to 1,908. The numbers reflect a steady pattern of growth over the past few years.

Operations

In 2017, the system experienced 55 main breaks (4.4 breaks/100 miles of pipe/year). Up from last year's 36 main breaks (2.9 breaks/100 miles of pipe/year), this is still well below the industry target of 15 breaks/100 miles of pipe/year and reflects a highly reliable water system.

Meters

In an effort to target high-use meters, a High Consumption Meter project was started with dedicated staff and planning. The team exchanged 481 meters.

Flushing

The unidirectional flush teams cleaned 228 miles of main in 2017, approximately 17% of the distribution system. Additionally, 2,045 dead end mains were flushed.

In effort to refine and enhance the outputs of our hydraulic model, Tacoma Water conducted fire hydrant flow tests at approximately 150 locations throughout the water system. These tests will help the utility better understand how water flows through and the pressures in its water mains.

Planning & Scheduling

In 2017, Distribution Operations completed an initiative to begin implementing planning and scheduling. Organization structure was set up, dedicated staff was hired, and a consultant was brought in to facilitate the completion of strategic milestones. Notable milestones include holding a two day training with Operations Managers, Planners, and Supervisors, multiple brown paper exercises to document current work processes, and established desired future state work processes to align with the capabilities of the mobile project.

A Planning and Scheduling steering committee was stood up to create alignment between the operating groups focusing on organizational structure and communication. Multiple meetings were held to promote and educate staff on the effort.

Safety

Tacoma Water's recordable injuries continued to trend downward with a 29% reduction from 2016 (61% reduction from 2012). Much of the success can be attributed to the continued effort to raise Safety awareness through increased communication and open dialogue between all employees. Safety centric field audits, monthly trainings, morning supervisor meetings, onsite daily tailgate meetings, as well as manager's attendance at Safety Committee meetings have all increased in regularity and have been refined to promote a heightened regard for Safety.

Emphasis and improvements were applied to the Confined Space and Silica programs which will ensure long lasting and durable mitigations to these specific hazards.

Tacoma Water's success can also be attributed to the increased efforts to promote Safety at the TPU level. An inaugural meeting of all Safety Committee members throughout TPU was held to discuss the promotion of Safety through posters, banners and quarterly magazines. A consultant was hired to review the safety culture at TPU and provide a report and recommendations for action. The review will include interviews with a subset of employees at all levels of the organization, and a survey to all employees.

Scott Dewhirst
Water Superintendent



The City of Tacoma does not discriminate on the basis of disability in any of its programs, activities, or services. To request this information in an alternative format or to request a reasonable accommodation, please contact the City Clerk's Office at (253) 591-5505. TTY or speech to speech users please dial 711 to connect to Washington Relay Services.

ANNUAL

FLEET SERVICES FUND

2017

**FINANCIAL
REPORT**



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DEPARTMENT OF PUBLIC UTILITIES

CITY OF TACOMA

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES

FLEET SERVICES FUND

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FINANCIAL DATA

MANAGEMENT DISCUSSION AND ANALYSIS

The following discussion and analysis of the financial performance of the Fleet Services Fund provides an overview of the financial activities for the years ended December 31, 2017, 2016 and 2015. The information presented here should be read in conjunction with the financial statements as a whole, including the footnotes and other supplementary information that is provided.

Overview of the Financial Statements

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

The basic financial statements, presented on a comparative basis for the years ended December 31, 2017 and 2016, 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 the Fund'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 operations, investing and financing activities.

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

Management has established and maintains a system of internal control that provides reasonable assurance as to the integrity and reliability of the financial statements, the protection of assets from unauthorized use or disposition and the prevention and detection of fraudulent financial reporting. The system of internal control provides for appropriate division of responsibility and is documented by written policies and procedures. The concept of reasonable assurance is based on the recognition that the cost of a system of internal control should not exceed the benefits derived.

Financial Statement Analysis

During 2017, Fleet Services realized net loss of \$1.5 million compared to net gain of \$1.2 million recorded in 2016. Operating revenues decreased \$2.2 million in 2017 (26.5%). Operating expenses increased \$656,000 (8.8%). The overall result is a net decrease in operating income of \$2.9 million from a year earlier.

In 2016, Fleet Services realized net gain of \$1.2 million compared to net gain of \$1.4 million recorded in 2015. Operating revenues increased \$223,000 in 2016 (2.8%). Operating expenses increased \$270,000 (3.7%). The overall result is a net decrease in operating income of \$47,000 from a year earlier.

Selected Financial Information

(in thousands)

Category	2015	2016	2017
Operating Revenues	8,074	8,297	6,096
Operating Expenses	7,211	7,481	8,137
Operating Income (Loss)	863	816	(2,041)
Other Income	169	397	526
Transfers In	339	2	-
Change in Net Position	<u>\$ 1,371</u>	<u>\$ 1,215</u>	<u>\$ (1,515)</u>
Current Assets	\$23,334	\$20,351	\$19,066
Other Assets	101	-	-
Deferred Outflows	240	965	916
Capital Assets (Net)	22,275	26,250	25,981
Total Assets	<u>45,950</u>	<u>47,566</u>	<u>45,963</u>
Total Liabilities	<u>1,476</u>	<u>1,928</u>	<u>1,708</u>
Deferred Inflows	107	56	188
Net Investment in Capital Assets	22,275	26,250	25,981
Restricted	26,387	26,276	26,276
Unrestricted	(4,295)	(6,945)	(8,190)
Total Net Position	<u>\$44,367</u>	<u>\$45,581</u>	<u>\$44,067</u>

Revenues

Fleet Services operating revenue is comprised of five categories: Maintenance, Capital Recovery, Administrative Overhead, Fuel and Fuel Loading and Pool Car Rental. Operating revenues were \$6.1 in 2017, \$8.3 in 2016 and \$8.1 million in 2015.

Maintenance revenues are mainly related to staff labor and were \$2.2 million in 2017, 2016 and 2015.

Capital recovery revenues are collected on each vehicle and piece of equipment based on anticipated equipment replacement needs for each business unit. Capital recovery revenues were \$2.4, \$5.1, and \$4.8 million in 2017, 2016, and 2015 respectively. Capital recovery revenue decreased \$2.8 million in 2017 compared to 2016, which had increased \$296,000 compared to 2015. The decline is primarily due to Tacoma Power discontinuing their contribution until an analysis of future purchase needs is complete.

Administrative Overhead revenue is the fee charged for each vehicle that is in service. The number of vehicles in service varies from month to month and the rate can vary based on type of vehicle. Administrative Overhead revenue was \$1.4 million, \$828,000 and \$853,000 in 2017, 2016, and 2015 respectively.

Fuel and fuel loading revenues are affected by year to year changes in vehicle usage and fluctuations in fuel prices. Fuel related revenues were \$54,000, \$47,000, and \$61,000 for 2017, 2016 and 2015 respectively.

Pool car revenues are based on usage and were \$126,000, \$123,000 and \$137,000 for 2017, 2016 and 2015 respectively.

Expenses

Fleet Services operating expense is comprised of four major categories: Repairs and service, stores operations, administration and depreciation. Fleet services expenses were \$8.1, \$7.5 and \$7.2 million in 2017, 2016 and 2015 respectively.

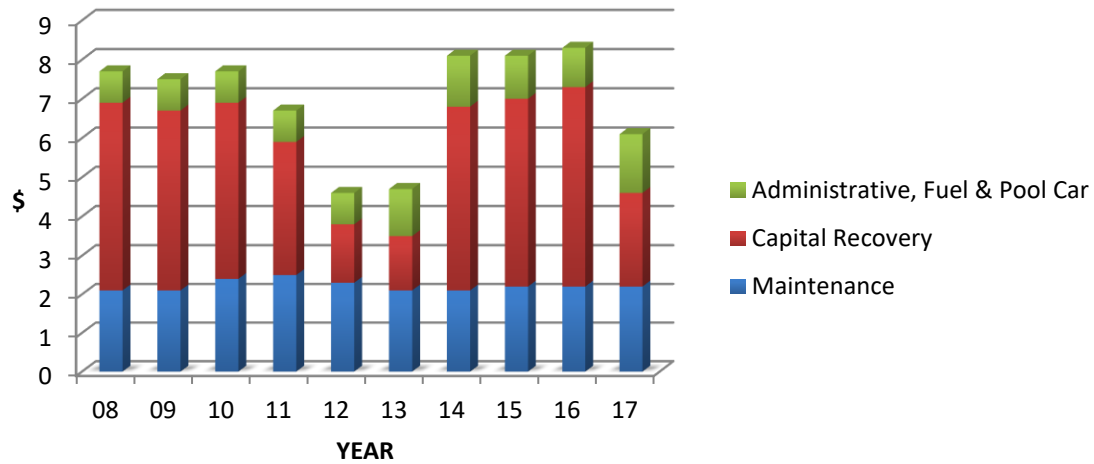
Repairs and service expense relates to shop operations which provide preventive and corrective maintenance and repairs to vehicles and pieces of equipment for Tacoma Public Utilities and other service groups. Repair and service expenses were \$2.7 million in 2017 and 2016 and \$2.6 million in 2015.

Stores operation is a parts warehouse maintained by Fleet which had expenses of \$338,000, \$329,000 and \$309,000 in 2017, 2016 and 2015 respectively.

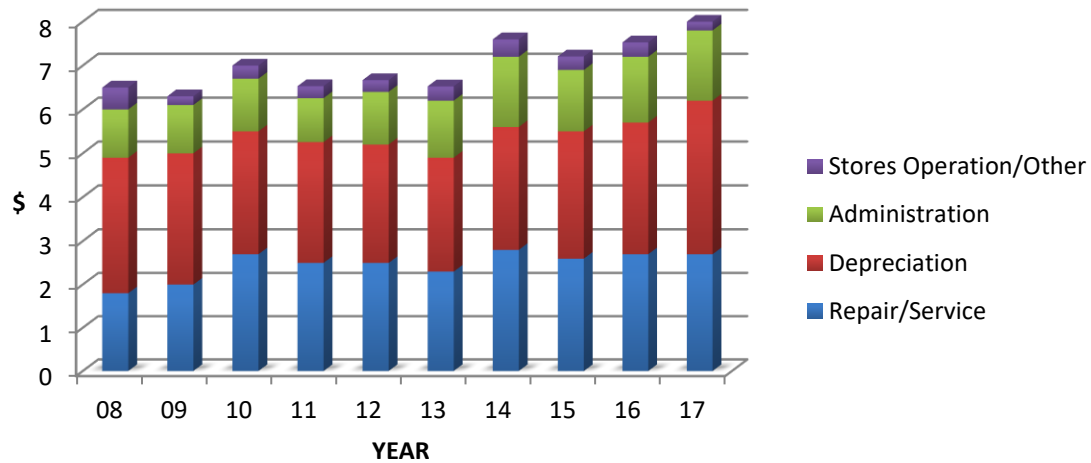
Administration expenses were \$1.6, \$1.5 and \$1.4 million in 2017, 2016 and 2015 respectively.

Depreciation expense was \$3.5, \$3.0 and \$2.9 million in 2017, 2016 and 2015 respectively. Fluctuations in depreciation expense are the result of timing in equipment retirements, capitalization of replacements and changes in fleet size.

OPERATING REVENUES (in millions)

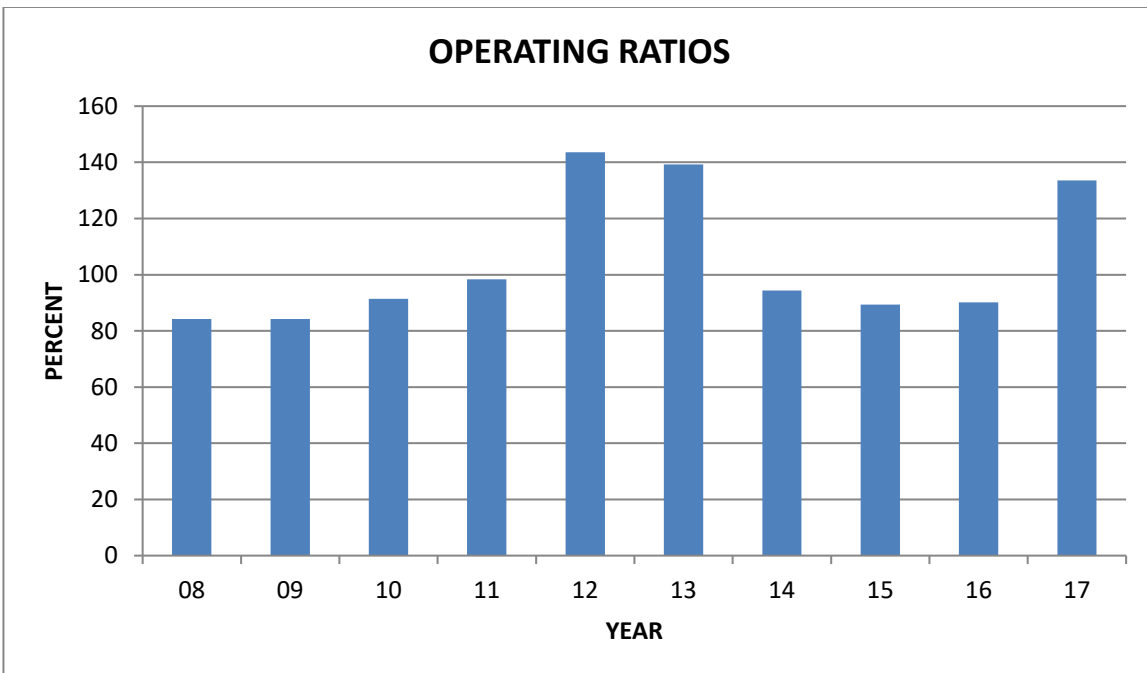


OPERATING EXPENSES (in millions)



Operating Ratio

The Fund's operating ratios, a common measure of efficiency and defined as operating expenses as a percentage of revenue, for 2017, 2016 and 2015 are 133.5%, 90.2%, and 89.3%. The Fund needs to maintain a low operating ratio in order to generate the funds necessary for its extensive capital outlay program. The graph shows how that percentage has fluctuated over the years.



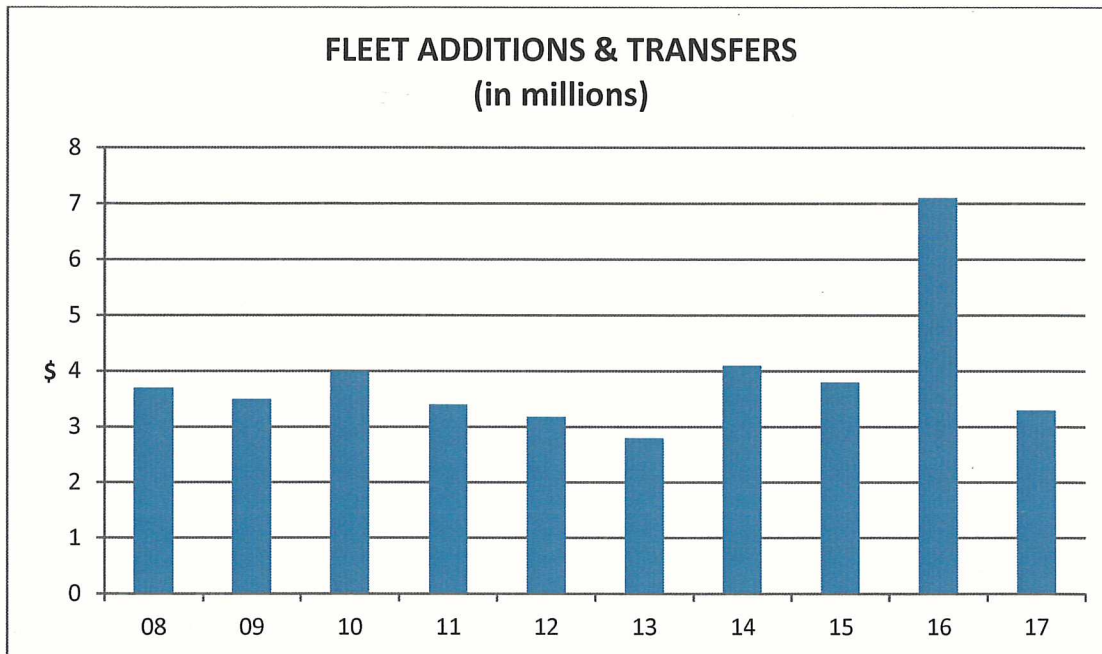
Non-Operating Revenues (Expenses)

Interest income decreased \$52,000 from \$49,000 in 2016 to (\$3,000) in 2017. Interest income in 2017 decreased due to less interest earned on the revenue pool and 2016 increased primarily due to the GASB 31 mark to market adjustment.

It is the practice of Fleet Services to arrange for public auction sale of vehicles and equipment that are declared surplus by the assigned sections. Fifty vehicles and pieces of equipment were retired in 2017 for a net gain of \$529,000, an increase of \$181,000 compared to 2016. Fleet Services reported a net gain of \$348,000 in 2016, an increase of \$155,000 compared to 2015.

Fixed Asset Additions

Purchases of fleet vehicles and equipment in 2017 were \$3.3 million with sixty-five vehicles and pieces of equipment placed into service compared with \$7.1 million in 2016 with sixty-three vehicles and pieces of equipment placed into service. Purchases of fleet vehicles and equipment in 2015 were \$3.8 million with forty-seven vehicles and pieces of equipment placed into service.



Summary

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the Fleet Services fund's finances and to show accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Division Manager of Utilities Accounting, 3628 South 35th Street, Tacoma, Washington, 98409.

Linda McCrea
Interim Director of Utilities/CEO

Andrew Cherullo
Finance Director

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

STATEMENTS OF NET POSITION
DECEMBER 31, 2017 AND DECEMBER 31, 2016

	<u>2017</u>	<u>2016</u>
ASSETS		
FIXED		
Office Furniture and Equipment	\$616,901	\$616,901
Stores and Shop Equipment	719,380	719,380
Transportation Equipment	44,411,067	44,284,166
Power-Operated Equipment	16,747,985	20,151,133
Accumulated Depreciation	<u>(37,242,725)</u>	<u>(39,776,755)</u>
Total Fixed Assets	25,252,608	25,994,825
Construction Work in Progress	<u>728,123</u>	<u>255,405</u>
Net Fixed Assets	25,980,731	26,250,230
CURRENT		
Current Fund Cash & Equity in Pooled Investments	18,652,494	19,808,702
Accounts Receivable	98,535	213,759
Interdivision Receivable	5,486	32,391
Materials and Supplies	<u>309,993</u>	<u>296,038</u>
Total Current Assets	19,066,508	20,350,890
DEFERRED OUTFLOWS OF RESOURCES		
Deferred Outflows for Pensions	<u>915,881</u>	<u>964,710</u>
TOTAL ASSETS AND DEFERRED OUTFLOWS.....	<u><u>\$45,963,120</u></u>	<u><u>\$47,565,830</u></u>

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

	2017	2016
NET POSITION AND LIABILITIES		
NET POSITION		
Net Investment in Capital Assets	\$25,980,731	\$26,250,230
Restricted for:		
Tacoma Power	18,095,346	18,095,346
Tacoma Water	7,199,933	7,199,933
Tacoma Rail	981,147	981,147
Net Pension Asset	-	-
Unrestricted	(8,190,226)	(6,944,959)
TOTAL NET POSITION	44,066,931	45,581,697
LIABILITIES		
CURRENT LIABILITIES		
Accounts Payable & Other	542,346	685,016
Wages Payable	68,548	73,607
Interdivision Payable	12,786	103,224
Total Current Liabilities	623,680	861,847
LONG-TERM LIABILITIES		
Employee Vacation and Sick Leave Accrual	209,679	231,004
Net Pension Liability	874,422	835,359
Total Long-term Liabilities	1,084,101	1,066,363
TOTAL LIABILITIES	1,707,781	1,928,210
DEFERRED INFLOW OF RESOURCES		
Deferred Inflows for Pensions	188,408	55,923
TOTAL NET POSITION, LIABILITIES AND DEFERRED INFLOWS	\$45,963,120	\$47,565,830

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

STATEMENTS OF REVENUE, EXPENSES AND CHANGES IN NET POSITION
DECEMBER 31, 2017 AND DECEMBER 31, 2016

	DECEMBER 2017	DECEMBER 2016
OPERATING REVENUE		
Maintenance Revenue	172,905	\$196,423
Capital Recovery	207,832	448,862
Administrative Overhead	116,453	69,014
Fuel and Fuel Loading	4,241	4,208
Pool Car Rental	23,077	8,624
Total Operating Revenue	<u>524,508</u>	<u>727,131</u>
OPERATING EXPENSES		
Repairs and Servicing		
Shop Operations	318,807	345,650
Outside Services	11,280	21,781
Total Repairs and Servicing	<u>330,087</u>	<u>367,431</u>
Stores Operations	48,583	47,247
Administration	189,863	218,799
Depreciation	285,130	247,714
Total Operating Expenses	<u>853,663</u>	<u>881,191</u>
OPERATING INCOME	(329,155)	(154,060)
NON-OPERATING REVENUES (EXPENSES)		
Interest Income	(115,799)	(58,742)
Gain (Loss) on Disposition of Equipment	76,350	138,374
Sale of Scrap	1,180	7,576
Total Non-Operating Revenues (Expenses)	<u>(38,269)</u>	<u>87,208</u>
Net Gain/Loss Before Transfers	(367,424)	(66,852)
Transfers In	<u>-</u>	<u>-</u>
CHANGE IN NET POSITION	<u>(\$367,424)</u>	<u>(\$66,852)</u>
TOTAL NET POSITION - BEGINNING OF YEAR		
TOTAL NET POSITION - END OF YEAR		

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

YEAR TO DATE	YEAR TO DATE		
DECEMBER 2017	DECEMBER 2016	2017/2016 VARIANCE	PERCENT CHANGE
\$2,176,378	\$2,176,445	(\$67)	0.0%
2,360,298	5,122,589	(2,762,291)	-53.9%
1,379,587	827,834	551,753	66.7%
54,116	46,533	7,583	16.3%
125,755	123,377	2,378	1.9%
6,096,134	8,296,778	(2,200,644)	-26.5%
2,677,135	2,664,324	12,811	0.5%
39,659	47,930	(8,271)	-17.3%
2,716,794	2,712,254	4,540	0.2%
337,500	329,268	8,232	2.5%
1,589,619	1,451,298	138,321	9.5%
3,492,861	2,988,385	504,476	16.9%
8,136,774	7,481,205	655,569	8.8%
(2,040,640)	815,573	(2,856,213)	-350.2%
(2,988)	48,726	(51,714)	-106.1%
514,559	323,198	191,361	59.2%
14,303	25,278	(10,975)	-43.4%
525,874	397,202	128,672	32.4%
(1,514,766)	1,212,775	(2,727,541)	-224.9%
-	2,181	(2,181)	-100.0%
(1,514,766)	1,214,956	(\$2,729,722)	-224.7%
45,581,697	44,366,741		
44,066,931	\$45,581,697		

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

STATEMENT OF NET POSITION
DECEMBER 31, 2017

Invested in Capital Assets:		
Balance January 1, 2017	\$26,250,230	
Capital Additions	(2,803,528)	
Depreciation	<u>2,534,029</u>	
Total Invested in Capital Assets		\$25,980,731
Restricted Net Position:		
Balance January 1, 2017	26,276,426	
Net Reductions through December 31, 2017	<u>-</u>	
Total Restricted Net Position December 31, 2017 ..		26,276,426
Unrestricted Net Position:		
Balance January 1, 2017	(6,944,959)	
Net Reductions through December 31, 2017	<u>(1,245,267)</u>	
Total Unrestricted Net Position December 31, 2017 ..		<u>(8,190,226)</u>
TOTAL NET POSITION DECEMBER 31, 2017		<u><u>\$44,066,931</u></u>

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

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

EQUITY DISTRIBUTION AS OF DECEMBER 31, 2017

	TACOMA POWER	TACOMA WATER	TACOMA RAIL	TOTAL
Balance January 1, 2017	\$30,343,339	\$13,713,445	\$1,524,913	\$45,581,697
Contributions During Year	-	-	-	-
Equity Contrib. at Dec 31, 2017	30,343,339	13,713,445	1,524,913	45,581,697
Current Year Operations:				
Total Operating Revenue *	4,058,143	1,834,048	203,943	6,096,134
Less: Repairs & Servicing Expense *	1,808,546	817,359	90,889	2,716,794
Administration Expense ** ...	1,423,620	432,417	71,082	1,927,119
Depreciation Expense	2,547,611	831,818	113,432	3,492,861
Total Expenses	5,779,777	2,081,594	275,403	8,136,774
Net Operating Revenue	(1,721,634)	(247,546)	(71,460)	(2,040,640)
Add: Other Income ***	346,165	162,038	17,671	525,874
Net Operating Results	(1,375,469)	(85,508)	(53,789)	(1,514,766)
Total Equity	<u>\$28,967,870</u>	<u>\$13,627,937</u>	<u>\$1,471,124</u>	<u>\$44,066,931</u>

* Allocated to each division based on total receipts from the divisions.

** Allocated to each division based on vehicle count.

*** Allocated to each division based on total equity in the Fund.

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

STATEMENTS OF CASH FLOWS

	YEAR TO DATE	
	DECEMBER 31, 2017	DECEMBER 31, 2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash From Customers	\$6,238,263	\$8,860,839
Cash Paid to Suppliers	(1,437,618)	(1,648,808)
Cash Paid to Employees	(3,259,365)	(3,077,771)
Net Cash Provided by (Used In) Operating Activities ...	1,541,280	4,134,260
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital Expenditures, Net	(3,223,362)	(6,961,213)
Disposition of Equipment/Scrap.....	528,862	348,476
Net Cash Used in Financing Activities	(2,694,500)	(6,612,737)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest Received (Used In)	(2,988)	48,726
Net Cash Provided by (Used In) Investing Activities	(2,988)	48,726
Net Change in Cash and Equity in Pooled Investments	(1,156,208)	(2,429,751)
Cash and Equity in Pooled Investments at January 1	19,808,702	22,238,453
Cash and Equity in Pooled Investments at December 31	<u>\$18,652,494</u>	<u>\$19,808,702</u>

These statements should be read in conjunction with the Notes to Financial Statements contained in the 2017 Annual Report.

	YEAR TO DATE	
	DECEMBER 31, 2017	DECEMBER 31, 2016
Reconciliation of Operating Income to Net Cash Provided by Operating Activities:		
Operating Income	(\$2,040,640)	\$815,573
Pension (Credits) Expenses	220,377	161,345
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	3,492,861	2,988,385
Accounts Receivable	115,223	(169,939)
Interdivision Receivable	26,906	733,999
Materials and Supplies	(13,955)	(11,614)
Accounts Payable & Other	(142,670)	275,924
Interdivision Payable	(67,140)	(682,026)
Absences Payable	(49,682)	22,613
Total Adjustments	3,361,543	3,157,342
Net Cash Provided by Operating Activities	\$1,541,280	\$4,134,260

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Fleet Services Fund was established in 1984 by City of Tacoma Ordinance No. 23295. On January 1, 1985, most vehicles owned by the Tacoma Power, Tacoma Water and Tacoma Rail were transferred to this Fund. The purpose of the Fund is to provide for scheduled maintenance, repair, and replacement of Department vehicles.

Basis of Financial Statements - The Fleet Service Fund is an Internal Service Fund of the City of Tacoma used for the operation of the Department of Public Utilities consolidated fleet management program with responsibilities for all vehicle administration under a fleet manager.

The Fund accounts for its financial operation by using a self-balancing set of accounts established primarily for handling transactions of a nature peculiar to Fleet Service operations. A description of the Fund's principal accounting policies follows.

Fixed Assets - Fixed assets are stated at cost and are depreciated primarily using a straight-line method over the estimated useful life of the asset.

Inventory - The inventory is valued on the moving average cost method.

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

Cash and Equity in Pooled Investments and Investments - The Fund'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 Assets. 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 Fund, 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 certificates of deposit with East West Bank and Opus Bank.

The Fund's equity in that portion of the City of Tacoma Investment Pool held in qualified public depositories at December 31, 2017 and 2016 is entirely covered by the Federal Deposit Insurance Corporation (FDIC) and the Washington State Public Deposit Protection Commission (WSPDPC).

FLEET SERVICES FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

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 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.

NOTE 2 INVESTMENTS MEASURED AT FAIR VALUE

The City measures and records its investments within the fair value hierarchy established by generally accepted accounting principles.

The hierarchy is based on the valuation inputs used to measure the fair value of the asset, where fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. These guidelines recognize a three-tiered fair value hierarchy, as follows:

- Level 1 – Level 1 inputs are quoted (unadjusted) prices in active markets for identical assets or liabilities that the government can access at the measurement date. Observable markets include exchange markets, dealer markets, brokered markets and principal-to-principal markets.
- Level 2 – Level 2 inputs are other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs are sourced from pricing vendors using models that are market-based and corroborated by observable market data including: quoted prices; nominal yield spreads; benchmark yield curves; and other corroborated inputs.
- Level 3 – Level 3 inputs are unobservable inputs for the asset or liability and should only be used when relevant Level 1 or Level 2 inputs are unavailable.

The fair value evaluations are provided by Interactive Data. Interactive Data utilizes evaluated pricing models that vary by asset class and incorporate available trade, bid and other market information and for structured securities, cash flow and, when available, loan performance data. Because many fixed income securities do not trade on a daily basis, Interactive Data's evaluated pricing applications apply available information as applicable through processes such as benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing, to prepare evaluations. In addition, Interactive Data uses model processes, such as the Option Adjusted Spread model to assess interest rate impact and development payment scenarios. Their models and processes take into account market convention. For each asset class, a team of evaluators gathers information from market sources and integrates relevant credit information, perceived market movements and sector news into the evaluated pricing applications and models.

FLEET SERVICES FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

Cash and cash equivalents include highly liquid investments including short-term investment funds. Cash and cash equivalents are valued at cost and, therefore, excluded from the fair value schedule.

Data regarding the City's investments, valued and categorized according to the above outlined levels, is below:

	As of			
Debt Securities	12/31/2017	Level 1	Level 2	Level 3
U.S. Treasury Securities	\$ 218,142,864	\$ -	\$ 218,142,864	\$ -
U.S. Agency Securities	517,345,818	-	517,345,818	-
Supranational Securities	19,966,040	-	19,966,040	-
Municipal Bonds	40,760,727	-	40,760,727	-
Total	<u>\$ 796,215,449</u>	<u>\$ -</u>	<u>\$ 796,215,449</u>	<u>\$ -</u>

	As of			
Debt Securities	12/31/2016	Level 1	Level 2	Level 3
U.S. Treasury Securities	\$ 146,824,628	\$ -	\$ 146,824,628	\$ -
U.S. Agency Securities	544,579,831	-	544,579,831	-
Municipal Bonds	61,450,051	-	61,450,051	-
Total	<u>\$ 752,854,510</u>	<u>\$ -</u>	<u>\$ 752,854,510</u>	<u>\$ -</u>

Fleet's share of the City Investments shown in the table above is 2.01% and 2.47% for 2017 and 2016.

NOTE 3 TACOMA EMPLOYEES' RETIREMENT SYSTEM FUND (TERS)

The Tacoma Employees' Retirement System (TERS or System), 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 South Sound 911 (formerly known as Law Enforcement Support Agency) who

FLEET SERVICES FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

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 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, 2016 (measurement date) is as follows:

Retirees and beneficiaries currently receiving benefits	2,303
Terminated vested and other terminated participants	675
Active members:	
City of Tacoma	2,687
South Sound 911	2
Pierce Transit	8
Tacoma-Pierce County Health Department	267
Total active members	<u>2,964</u>
Total membership	<u><u>5,942</u></u>

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 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.

FLEET SERVICES FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

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.

In fiscal year 2017, 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%. On November 28, 2017 the Tacoma City Council approved the TERS Board's recommendation to increase the contribution rate by 1% (split 0.54% for employers and 0.46% for employees) effective the first pay period in February 2018, 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, 2016
Valuation Date	January 1, 2017
Actuarial Cost Method	Entry Age Normal
Amortization Method	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: <ul style="list-style-type: none"> · Level percent · Open periods · 30 year amortization period at 01/01/2015 · 3.75% amortization growth rate
Asset Valuation Method	4 year smoothing period; Corridor - None
Inflation	2.75%
Salary Increases	Varies by service
Investment Rate of Return	7.00%
Cost of Living Adjustment	2.125%
Retirement Age	Varies by age, gender, and eligibility
Turnover	Varies by service, and gender
Mortality	RP-2014 Mortality for Employees, Healthy and Disabled Annuityants. Generational improvements with projection scale based on Social Security Administration Data.

FLEET SERVICES FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

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. The following changes in assumptions occurred since the January 1, 2016 Actuarial Valuation:

1. The amortization growth rate decreased from 4% to 3.75%
2. The inflation rate decreased from 3% to 2.75%
3. The investment rate of return decreased from 7.25% to 7%

Target Allocations - The long-term expected rate of return is determined by adding expected inflation to expected long-term real returns and reflecting expected volatility and correlation. The capital market assumptions are per Milliman's (the System's actuary) investment consulting practice as of December 31, 2016. The target asset allocation is based on the Tacoma Employees' Retirement System Investment Policy Statement dated March 2016.

Asset Class	Target Allocation	Long-term Expected
		Arithmetic Real Rate of Return
Investment Grade Fixed Income	15.0%	1.63%
US Inflation-Indexed Bonds	5.0%	1.21%
High Yield Bonds	9.0%	5.00%
Emerging Market Debt	5.0%	3.74%
Global Equity	41.5%	5.50%
Public Real Estate	2.0%	5.80%
Private Real Estate	2.5%	3.56%
Private Equity	10.0%	9.04%
Master Limited Partnerships	4.0%	4.12%
Timber	2.0%	3.79%
Infrastructure	2.0%	5.03%
Agriculture	2.0%	4.33%
Assumed Inflation - Mean		2.75%
Assumed Inflation - Standard Deviation		1.85%
Portfolio Arithmetic Real Mean Return		4.76%
Portfolio Median Nominal Geometric Return		6.72%
Portfolio Standard Deviation		11.77%
Long-Term Expected Rate of Return, net of investment expenses		7.00%

FLEET SERVICES FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

Sensitivity Analysis - The following presents the net pension liability (asset) of the System, calculated using the discount rate of 7.0%, 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 (6.0%) or 1 percentage point higher (8.0%) than the current rate.

	1% Decrease 6.00%	Current Discount Rate 7.00%	1% Increase 8.00%
Net pension liability (asset)	\$ 2,800,036	\$ 874,422	\$ (688,287)

As of December 31, 2017, the deferred inflows and outflows of resources are as follows:

	Deferred Inflows of Resources	Deferred Outflows of Resources
Difference Between Expected and Actual Experience	\$ (188,207)	\$ -
Changes of assumptions	-	290,412
Net Difference Between Projected and Actual Earnings	-	397,926
Changes in Employer Proportion	(201)	427
Contributions Made Subsequent to the Measurement Date	-	227,116
Total	\$ (188,408)	\$ 915,881

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.

Amounts will be recognized in pension expense as follows:

2018	\$ 155,805
2019	155,805
2020	179,686
2021	(6,764)
2022	15,825
Thereafter	-
	<u>\$ 500,357</u>

The proportionate share of the Fleet Division is 0.94% of total System's pension liability. The proportionate share was based on the actual contributions for the year.

FLEET SERVICES FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

NOTE 4 FLEET SERVICES REFUND

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 two budget cycles and to return any excess funds to customers based on their scheduled monthly payments. In 2017 and 2016, Fleet Services returned 75% of the interest earned on the capital replacement reserve to the appropriate users. The amounts refunded in 2017 and 2016 were \$155,807 and \$148,818 respectively.

REQUIRED SUPPLEMENTARY INFORMATION

Proportionate Share of the Net Pension Liability Last 10 Years*

	Fiscal Year Ended December 31st,		
	2017	2016	2015
Employer's proportion of the net pension liability (asset) as a percentage	0.94%	0.96%	1.05%
Employer's proportion share of net pension liability (asset)	\$874,422	\$835,359	(\$101,261)
Employer's covered payroll	\$2,152,532	\$2,244,782	\$2,183,372
Employer's proportionate share of net pension liability (asset) as a percentage of its covered employee payroll	40.62%	38.81%	-4.64%
Plan fiduciary net position as a percentage the total pension liability	93.91%	93.94%	100.71%

Schedule of Contributions Last 10 Fiscal Years*

	Fiscal Year Ended December 31st,		
	2017	2016	2015
Contractually required employer contribution	\$227,116	\$227,848	\$239,770
Contributions in relation to the contractually required employer contribution	(227,116)	(227,848)	(239,770)
Employer contribution deficiency (excess)	-	-	-
Employer's covered employee payroll	\$2,179,654	\$2,152,532	\$2,244,782
Employer contribution as a percentage of covered-employee payroll	10.42%	10.59%	10.68%

* The above schedules are intended to show information for 10 years, the additional years' information will be displayed as it becomes available.

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STATISTICAL DATA

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

TEN-YEAR FINANCIAL REVIEW

STATEMENTS OF NET POSITION	2008	2009	2010	2011
ASSETS				
Fixed - Net	\$17,666,394	\$18,100,171	\$19,164,435	\$19,631,756
Current	23,370,520	23,665,442	26,034,139	24,425,237
Other	-	-	-	-
Total Assets	41,036,914	41,765,613	45,198,574	44,056,993
Deferred Outflows	-	-	-	-
TOTAL ASSETS AND DEFERRED OUTFLOWS	41,036,914	41,765,613	45,198,574	44,056,993
LIABILITIES				
Current	1,802,197	753,706	2,728,220	431,649
Deferred Inflows	-	-	-	-
NET POSITION	39,234,717	41,011,907	42,470,354	43,625,344
TOTAL LIABILITIES, NET POSITION AND DEFERRED INFLOWS	\$41,036,914	\$41,765,613	\$45,198,574	\$44,056,993
STATEMENTS OF INCOME				
OPERATING REVENUES				
Maintenance Revenue	\$2,128,335	\$2,096,838	\$2,369,705	\$2,499,589
Capital Recovery	4,831,680	4,568,298	4,462,261	3,382,819
Pool Car Rental	98,226	93,436	86,625	68,411
Administrative and Fuel	756,571	723,748	731,116	730,871
Total Operating Revenues	7,814,812	7,482,320	7,649,707	6,681,690
OPERATING EXPENSES				
Repairs and Servicing	1,793,119	2,004,911	2,713,546	2,488,151
Stores Operations	546,055	202,206	257,075	274,399
Administration	1,143,615	1,092,601	1,181,369	1,047,029
Depreciation	3,100,034	2,999,842	2,838,774	2,756,785
Total Operating Expenses	6,582,823	6,299,560	6,990,764	6,566,364
OPERATING INCOME (LOSS)	1,231,989	1,182,760	658,943	115,326
NON-OPERATING INCOME (EXPENSE)				
Interest Income	222,535	148,018	(5,943)	360,639
Net Other Income (Expense)	14,828	112,895	230,375	253,627
Total Non-Operating Income (Expense)	237,363	260,913	224,432	614,266
Net Income (Loss) Before Contributions & Transfers ...	1,469,352	1,443,673	883,375	729,592
Total Capital Contributions	-	-	4,000.00	174,815
Transfers In	846,483	333,517	571,072	250,583
NET INCOME (LOSS)	\$2,315,835	\$1,777,190	\$1,458,447	\$1,154,990

2012	2013	2014	2015	2016	2017
\$20,043,909	\$20,270,054	\$21,386,337	\$22,275,221	\$26,250,230	\$25,980,731
26,873,162	22,007,068	23,472,087	23,333,088	20,350,890	19,066,508
-	-	-	101,261	-	-
46,917,071	42,277,122	44,858,424	45,709,570	46,601,120	45,047,239
-	-	-	240,412	964,710	915,881
46,917,071	42,277,122	44,858,424	45,949,982	47,565,830	45,963,120
4,558,862	1,039,418	1,987,209	1,476,341	1,928,210	1,707,781
-	-	-	106,900	55,923	188,408
42,358,209	41,237,704	42,871,215	44,366,741	45,581,697	44,066,931
\$46,917,071	\$42,277,122	\$44,858,424	\$45,949,982	\$47,565,830	\$45,963,120
\$2,333,084	\$2,101,367	\$2,097,335	\$2,196,833	\$2,176,445	\$2,176,378
1,497,410	1,372,888	4,689,984	4,826,427	5,122,589	2,360,298
82,423	73,772	125,367	136,685	123,377	125,755
727,395	1,115,860	1,141,785	914,378	874,367	1,433,703
4,640,312	4,663,887	8,054,471	8,074,323	8,296,778	6,096,134
2,451,583	2,274,301	2,844,024	2,578,812	2,712,254	2,716,794
267,989	326,773	398,011	308,946	329,268	337,500
1,228,920	1,323,636	1,592,691	1,386,437	1,451,298	1,589,619
2,716,103	2,570,362	2,768,745	2,937,475	2,988,385	3,492,861
6,664,595	6,495,072	7,603,471	7,211,670	7,481,205	8,136,774
(2,024,283)	(1,831,185)	451,000	862,653	815,573	(2,040,640)
92,913	(99,756)	54,921	(24,043)	48,726	(2,988)
247,292	165,334	474,892	193,493	348,476	528,862
340,205	65,578	529,813	169,450	397,202	525,874
(1,684,078)	(1,765,607)	980,813	1,032,103	1,212,775	(1,514,766)
46,877	-	-	-	-	-
370,066	645,102	652,698	338,904	2,181	-
(\$1,267,135)	(\$1,120,505)	\$1,633,511	\$1,371,007	\$1,214,956	(\$1,514,766)

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

FLEET PLANT IN SERVICE
FOR THE YEAR ENDED DECEMBER 31, 2017

FIXED ASSET ACCOUNTS

	Book Cost 1/1/17	Additions 2017
Office Furniture and Equipment	\$616,901	\$ -
Stores and Shop Equipment	719,380	-
Transportation Equipment	44,357,091	2,494,284
Power-Operated Equipment	20,151,133	106,849
Construction Work in Progress.....	255,405	725,112
TOTAL FIXED ASSETS	<u>\$66,099,910</u>	<u>\$3,326,245</u>

ACCUMULATED DEPRECIATION ACCOUNTS

	Depreciation Rate %	Accumulated Depreciation 1/1/17
Office Furniture and Equipment	Various	\$540,905
Stores and Shop Equipment	Various	586,929
Transportation Equipment	Various	23,853,192
Power-Operated Equipment	Various	14,795,729
TOTAL ACCUMULATED DEPRECIATION		<u>\$39,776,755</u>

Retirements 2017	Transfers & Adjustments	Book Cost 12/31/17
\$ -	\$ -	\$616,901
-	-	719,380
(2,692,702)	252,394	44,411,067
(3,509,997)	-	16,747,985
-	(252,394)	728,123
<u>(\$6,202,699)</u>	<u>\$ -</u>	<u>\$63,223,456</u>

Annual Accrual Cr.	Transfers & Adjustments	Accumulated Depreciation 12/31/17
\$5,422	\$ -	\$546,327
19,638	-	606,567
2,786,545	(2,563,843)	24,075,894
681,256	(3,463,048)	12,013,937
<u>\$3,492,861</u>	<u>(\$6,026,891)</u>	<u>\$37,242,725</u>

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
FLEET SERVICES FUND

TAXES AND EMPLOYEE WELFARE CONTRIBUTIONS
FOR THE YEAR 2017

FEDERAL

Social Security (FICA)		\$165,077
------------------------------	--	-----------

STATE OF WASHINGTON

Retail Sales Tax	273,642	
State Employment Security	3,453	
Total		<u>277,095</u>

TOTAL TAXES		<u><u>\$442,172</u></u>
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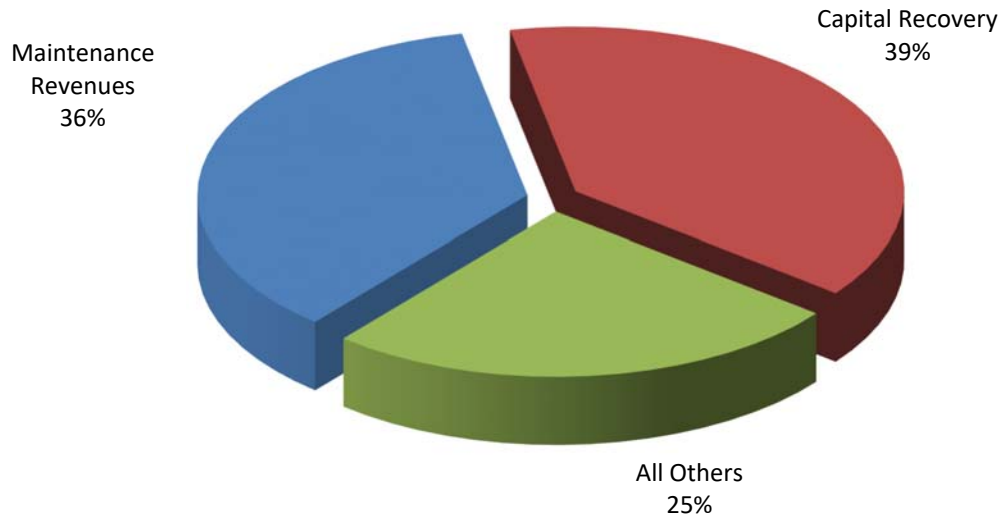
Taxes as a % of Total Revenues of \$6,096,134.....	7.25%
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EMPLOYEE WELFARE CONTRIBUTIONS

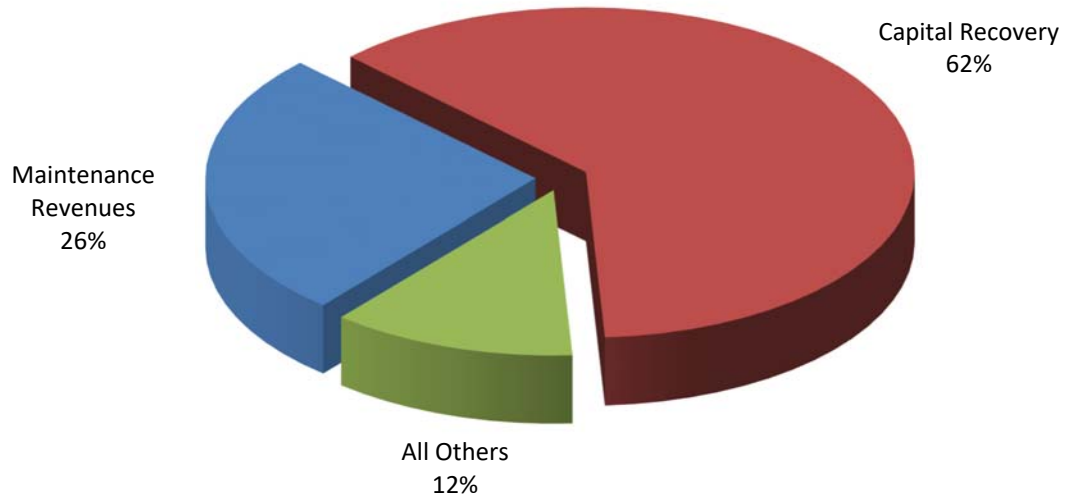
Industrial Insurance and Medical Aid	\$35,079
City of Tacoma Pension Fund	225,534
Washington Dental Service	39,663
Pierce County Medical Bureau	<u>467,984</u>

TOTAL EMPLOYEE WELFARE CONTRIBUTIONS	<u><u>\$768,260</u></u>
--------------------------------------------	-------------------------

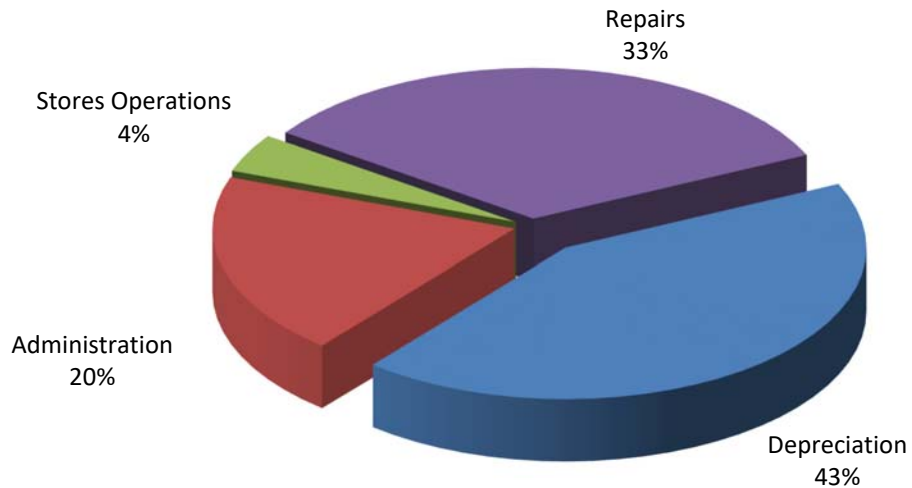
TOTAL OPERATING REVENUES
Year to Date - December 2017 (\$6,096,134)



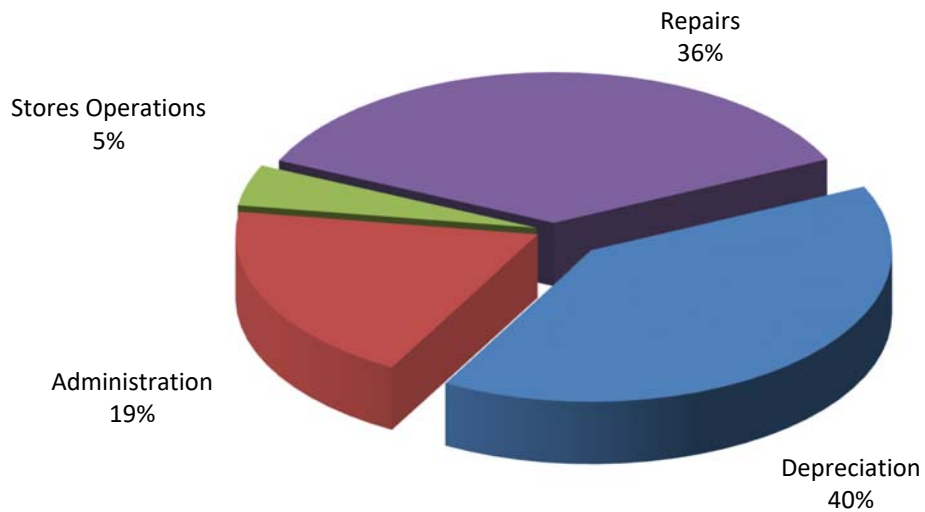
TOTAL OPERATING REVENUES
Year to Date - December 2016 (\$8,296,778)



TOTAL OPERATING EXPENSES
Year to Date - December 2017 (\$8,136,774)



TOTAL OPERATING EXPENSES
Year to Date - December 2016 (\$7,481,205)



FLEET MANAGER'S REPORT

Fleet Services completed a successful year providing vehicle and equipment maintenance and management services to our customers.

Fleet Finance

Fleet Services worked with customers during the year to assure they had the vehicles and equipment needed to perform their duties. Specification and purchasing procedures were completed for 65 pieces of equipment. Fleet Services arranged for public auction the sale of 50 pieces of equipment that were declared surplus by the assigned sections.

Fleet Services continued to return interest earned on fund investments for the year to our customers. A total of \$155,807 was credited to individual vehicle replacement funds through December 2017, with the allocation based on the amount each had paid into the fund.

After returning these funds to customers, the Fleet Fund ended the year with a \$18,652,494 cash and investment balance.

Fleet Maintenance

Fleet Services maintenance shop performed 1,607 preventive maintenance services and inspections and 3,655 corrective work orders on Public Utilities vehicles and equipment.

Fleet Services also performed state-mandated emissions testing on 151 vehicles with passing results.

Fleet Initiatives

TPU Fleet Services efforts to make improvements continued in 2017. Fleet Services with the coordination of the Power Rates, Planning & Analysis group, conducted an RFP for a utility-wide vehicle utilization and fleet study designed to garner an objective third party analysis of the Fleet Services operations as well as the size and utilization of the fleet. The final report will be presented to the Executive Team in March 2018. This effort included establishing a Fleet Advisory Committee group with representatives from Power, Water, Rail, Customer Service, MSO and Fleet to review and implement some of the recommendations from the study.

Fleet Services worked with Power Generation and Conservation groups to install new LED energy efficient lighting that provides a safer, better-lit and overall improved working environment. The estimated energy savings is 60%, which equates to more than \$6,000 annually. This project also qualified for a Bright Rebate of over \$17,500.

Fleet received rebates that totaled \$14,078.60 for purchasing plug-in hybrid and electric vehicles and \$3,712.22 for participating in Fleet purchasing incentive programs.

TPU Fleet Services obtained \$4,938.45 in fuel tax recovery through a Washington State program designed to reimburse for fuel road taxes paid for vehicles and equipment that were used for off road purposes. These instances include when the equipment is operated on unimproved roads, in PTO mode and for miscellaneous use such as chain saws, weed eaters, leaf blowers, etc.

Fleet Parts

Fleet Services parts warehouse issued \$853,510.68 in parts in support of the maintenance shop. Of this amount, 35 percent (\$295,729.36) was issued from stock and 65 percent (\$557,781.32) was ordered non-stock from vendors. The Fleet parts warehouse accomplished 10,603 issue transactions totaling 33,729 items.

Fleet Staff Development

Fleet Services employees received an average of 27.1 hours of technical, personal development, and safety-oriented training per person.

The Fleet Services Tool and Training Committee helped specify and obtain tools and shop equipment designed to increase productivity and safety.

Don Ashmore
Fleet Manager



The City of Tacoma does not discriminate on the basis of disability in any of its programs, activities, or services. To request this information in an alternative format or to request a reasonable accommodation, please contact the City Clerk's Office at (253) 591-5505. TTY or speech to speech users please dial 711 to connect to Washington Relay Services.

ANNUAL

SELF-INSURANCE CLAIM FUND

2017

**FINANCIAL
REPORT**



Public Utility Board

MONIQUE TRUDNOWSKI
Chair

WOODROW JONES
Vice-Chair

KAREN LARKIN
Secretary

BRYAN FLINT
Member

MARK PATTERSON
Member

LINDA MCCREA
Interim Director of Utilities/CEO

CHRIS ROBINSON
Power Superintendent/COO

ANDREW CHERULLO
Finance Director

DEPARTMENT OF PUBLIC UTILITIES

CITY OF TACOMA

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES

SELF-INSURANCE CLAIM FUND

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FINANCIAL DATA

MANAGEMENT DISCUSSION AND ANALYSIS

The following discussion and analysis of the financial performance of the Self-Insurance Fund provides an overview of the financial activities for the years ended December 31, 2017, 2016 and 2015. The information presented here should be read in conjunction with the financial statements as a whole, including the footnotes and other supplementary information that is provided.

Overview of the Financial Statements

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

The basic financial statements, presented on a comparative basis for the years ended December 31, 2017 and 2016, 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 the Fund'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 operations, investing and financing activities.

The notes to the financial statements, presented at the end of the basic 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 Fund's presentation of financial position, results of operations, and changes in cash flows.

Management has established and maintains a system of internal control that provides reasonable assurance as to the integrity and reliability of the financial statements, the protection of assets from unauthorized use or disposition and the prevention and detection of fraudulent financial reporting. The system of internal control provides for appropriate division of responsibility and is documented by written policies and procedures. The concept of reasonable assurance is based on the recognition that the cost of a system of internal control should not exceed the benefits derived.

Financial Statement Analysis

The Fund is reporting a net loss of \$1.7 million in 2017 compared to a net gain of \$658,000 recorded in 2016. Total revenues decreased by \$35,000 and total expenses increased by \$2.3 million for the year.

In 2016, the Fund reported a net gain of \$658,000 compared to a net gain of \$1.9 million in 2015. Total revenues increased \$26,000 and total expenses increased \$1.3 million for the year.

Selected Financial Information

(in thousands)

Category	2015	2016	2017
Premiums	\$1,240	\$1,240	\$1,207
Interest	<u>35</u>	<u>62</u>	<u>59</u>
Total Income	1,275	1,302	1,266
Total Expenses	<u>(641)</u>	<u>644</u>	<u>2,922</u>
Change in Net Position (Net Income)	\$1,916	\$658	(\$1,656)
Current Assets	\$6,856	\$7,633	\$7,029
Accounts Payable Claims	4,692	4,810	5,857
Other Liabilities	<u>16</u>	<u>17</u>	<u>22</u>
Total Liabilities (Current)	<u>4,708</u>	<u>4,827</u>	<u>5,879</u>
Total Net Position	\$2,148	\$2,806	\$1,150

Revenues

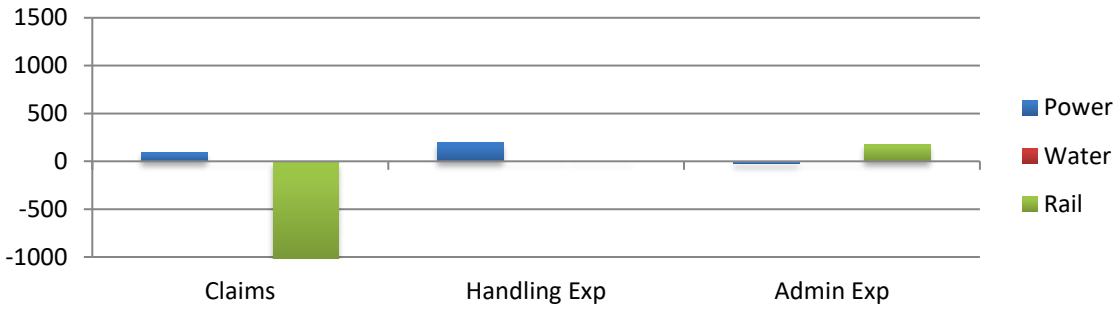
Self-Insurance fund revenues are contributions from the Power, Water and Rail funds and the interest earned. Total revenues were \$1.3 million for both 2017 and 2016, respectively.

Expenses

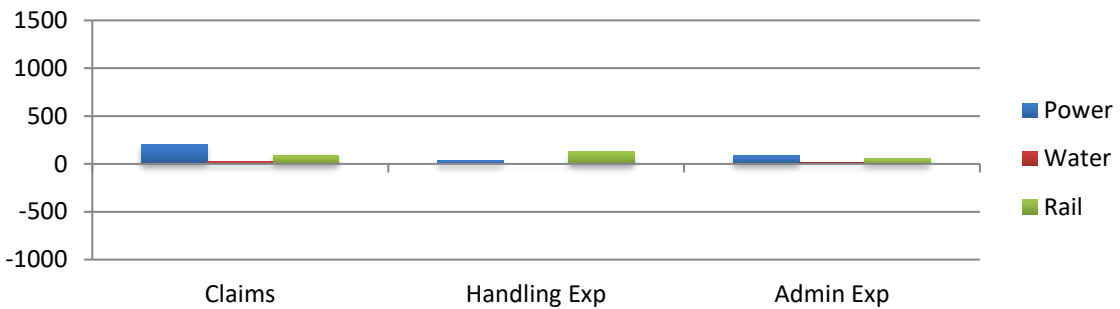
Self-Insurance fund expenses include claims and handling expenses paid during the year, adjustments to accrued claims and administrative expenses. Support Services claims and handling expenses are allocated to Power and Water only and based on each fund's percentage of combined claims and handling expense for the year. Administrative expenses are allocated to Power, Water and Rail funds based on each fund's percentage of total claims paid for the year.

Total expenses in 2017, 2016 and 2015 were \$2.9 million, \$644,000 and negative \$641,000 respectively. The increase or decrease in expenses from year to year is primarily due to adjustments in expected future developments accrued by the Fund. Negative claims expense is generally the result of adjustments to the liability where expected claims were accrued in one year and subsequently denied or revised the next year.

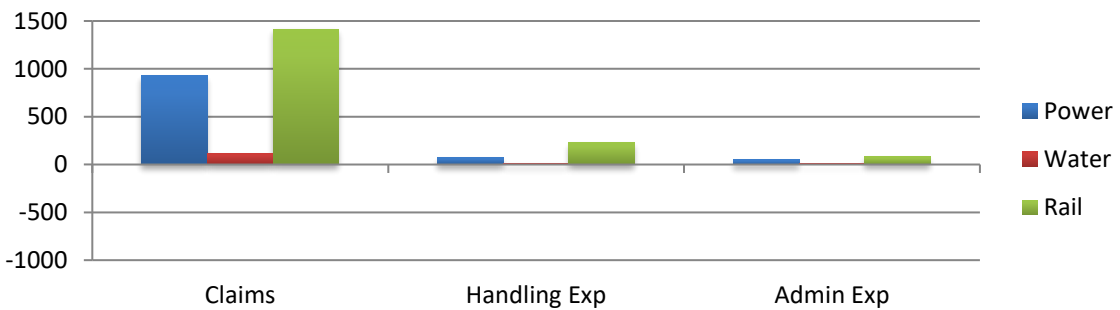
2015 Expenses (\$ in thousands)



2016 Expenses (\$ in thousands)



2017 Expenses (\$ in thousands)



Self-Insurance Claims

Claims paid by the Fund generally fall into four distinct categories. The following table illustrates the impact the various types of claims had on the Fund in 2017, 2016, and 2015.

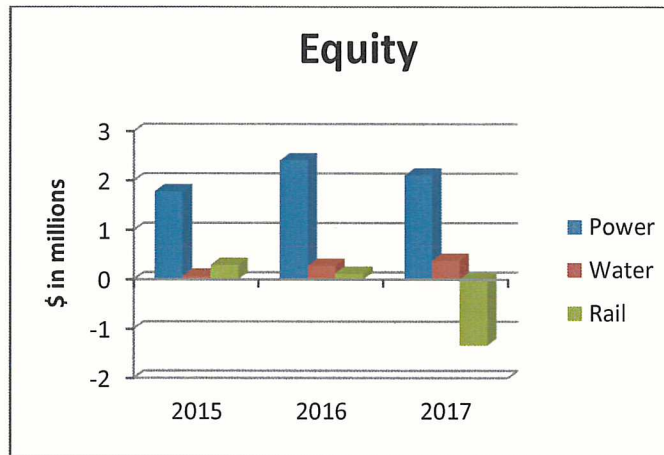
Category	2015	2016	2017
Non-Vehicular (Bodily Injury/Property Damage)	\$185,528	\$228,542	\$1,384,648
Vehicular (Bodily Injury/Property Damage)	92,485	13,600	32,574
Hazardous Waste (Environmental)	-	-	-
Contract/Harassment	-	-	-
Total Claims Paid	\$278,013	\$242,142	\$1,417,222

This table compares the balances that have been accrued as accounts payable claims at year-end 2017, 2016, and 2015 for these same four categories.

Category	2015	2016	2017
Non-Vehicular (Bodily Injury/Property Damage)	\$4,637,697	\$4,764,576	\$5,816,444
Vehicular (Bodily Injury/Property Damage)	54,532	45,307	40,748
Hazardous Waste (Environmental)	-	-	-
Contract/Harassment	-	140	-
Total Accrued Accounts Payable Claims	\$4,692,229	\$4,810,023	\$5,857,192

Equity

The Fund's equity at the end of 2017 is \$1.2 million compared to \$2.8 million in 2016 and \$2.1 million in 2015. The following graph provides a visual presentation as to how the Fund's equity is shared.



Summary

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the Self-Insurance Fund's finances and to show accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Division Manager of Utilities Accounting, 3628 South 35th Street, Tacoma, Washington, 98409.

Linda McCrea
Director of Utilities/CEO

Andrew Cherullo
Finance Director

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
SELF-INSURANCE CLAIM FUND

STATEMENTS OF NET POSITION - DECEMBER 31, 2017 AND DECEMBER 31, 2016

	<u>2017</u>	<u>2016</u>
ASSETS		
CURRENT		
Cash and Equity in Pooled Investments	<u>\$7,028,558</u>	<u>\$7,633,129</u>
TOTAL ASSETS	<u><u>\$7,028,558</u></u>	<u><u>\$7,633,129</u></u>
 NET POSITION AND LIABILITIES		
NET POSITION		
Restricted:		
Interfund Contributions	<u>\$1,150,408</u>	<u>\$2,806,451</u>
TOTAL NET POSITION	1,150,408	2,806,451
CURRENT LIABILITIES		
Accounts Payable Claims	5,857,192	4,810,023
Accounts Payable Claims Handling	12,048	4,433
Interdivision Payable	<u>8,910</u>	<u>12,222</u>
TOTAL LIABILITIES	<u>5,878,150</u>	<u>4,826,678</u>
TOTAL NET POSITION AND LIABILITIES	<u><u>\$7,028,558</u></u>	<u><u>\$7,633,129</u></u>

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

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
SELF-INSURANCE CLAIM FUND

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
DECEMBER 31, 2017 AND DECEMBER 31, 2016

	DECEMBER 2017	DECEMBER 2016
INCOME		
Premiums	\$128,333	\$103,333
Interest	(\$38,478)	(18,028)
	<hr/>	<hr/>
TOTAL INCOME	89,855	85,305
 EXPENSES		
Claims	537,716	(275,683)
Litigation Expense and Settlements	19,064	17,869
Incidental and Administrative Expense	12,668	12,222
	<hr/>	<hr/>
TOTAL EXPENSES	569,448	(245,592)
	<hr/>	<hr/>
CHANGE IN NET POSITION	(\$479,593)	\$330,897
	<hr/>	<hr/>
TOTAL NET POSITION - JANUARY 1		
TOTAL NET POSITION - DECEMBER 31		

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

YEAR-TO-DATE			
DECEMBER 2017	DECEMBER 2016	2017/2016 VARIANCE	PERCENT CHANGE
\$1,206,667	\$1,240,000	\$ (33,333)	-2.7%
59,596	61,576	(1,980)	-3.2%
1,266,263	1,301,576	(35,313)	-2.7%
2,464,390	350,057	2,114,333	604.0%
318,999	172,963	146,036	84.4%
138,917	120,574	18,343	15.2%
2,922,306	643,594	2,278,712	354.1%
(1,656,043)	657,982	(2,314,025)	-351.7%
2,806,451	2,148,469	657,982	
\$1,150,408	\$2,806,451	(\$1,656,043)	

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
SELF-INSURANCE CLAIM FUND

EQUITY DISTRIBUTION AS OF DECEMBER 31, 2017

	TACOMA POWER	TACOMA WATER	TACOMA RAIL	TOTAL
Balance January 1, 2017	\$2,407,775	\$278,502	\$120,174	\$2,806,451
Contributions (Premiums)	700,000	240,000	266,667	\$1,206,667
Claims (1)	(930,103)	(118,907)	(1,415,249)	(\$2,464,259)
Claims Handling Expense	(73,201)	(15,445)	(230,353)	(\$318,999)
Administrative Expenses (2)	(50,193)	(6,721)	(82,134)	(\$139,048)
Interest Income (3)	50,705	7,050	1,841	\$59,596
Balance December 31, 2017	<u>\$2,104,983</u>	<u>\$384,479</u>	<u>(\$1,339,054)</u>	<u>\$1,150,408</u>
GASB 10 Adjustments (4)	<u>(2,104,983)</u>	<u>(384,479)</u>	<u>1,339,054</u>	<u>(1,150,408)</u>
Adj Balance December 31, 2017	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

(1) Service divisions' claims of \$131 have been deducted from this area.

(2) Service divisions' claims and handling of \$131 have been added to Administrative expenses. These costs have been allocated to Power and Water divisions based on the ratio of claims activity to date. Service division does not provide support to Rail.

(3) Prior to 2017, interest income has been allocated to each division in the same ratio as its fund balance at January 1, plus contributions and expenses to date. Effective 2017, interest income has been allocated to each division based on the allocated cash balance as of the date of this statement.

(4) Tacoma Power, Water and Rail divisions have adjusted year-end balances to include their share of the equity in the Self Insurance Fund.

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
SELF-INSURANCE CLAIM FUND

STATEMENTS OF CASH FLOWS

	YEAR TO DATE	
	DECEMBER 31, 2017	DECEMBER 31, 2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Premiums Received	\$1,206,667	\$1,240,000
Claims Paid	(1,417,222)	(242,299)
Administrative and Other Expenses	(453,612)	(282,079)
Net Cash Provided by (Used in)		
Operating Activities	(664,167)	715,622
 CASH FLOWS FROM FINANCING ACTIVITIES		
Interest Received	59,596	61,576
Net Cash Provided by		
Financing Activities	59,596	61,576
 Net Increase in Cash and		
Equity in Pooled Investments	(604,571)	777,198
 Cash and Equity in Pooled		
Investments at January 1	7,633,129	6,855,931
 Cash and Equity in Pooled		
Investments at December 31	\$7,028,558	\$7,633,129

	YEAR TO DATE	
	DECEMBER 31, 2017	DECEMBER 31, 2016
Reconciliation of Operating Income to Net Cash Provided by Operating Activities:		
Net Income	(\$1,656,043)	\$657,982
Adjustments to Reconcile Operating Income to Net Cash Provided By Operating Activities:		
Interest Income	(59,596)	(61,576)
Adjustments to Reconcile Net Income to Net Cash Provided by (Used in) Operating Activities:		
Interdivision Payable	(3,312)	883
Accounts Payable Claims	1,047,167	117,794
Accounts Payable Claims Handling	7,617	539
Total Adjustments	991,876	57,640
Net Cash (Used in) Provided by Operating Activities	(\$664,167)	\$715,622

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
SELF-INSURANCE CLAIM FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Self-Insurance Claim Fund was established in 1979 by City of Tacoma Ordinance No. 21863. Its purpose is to account for all monetary transactions required to carry out a self-insurance program for Tacoma Power and Tacoma Water of the City of Tacoma, Department of Public Utilities. Its first year of full operation was 1981. In November 1985, under the terms of City of Tacoma Ordinance No. 23513, Tacoma Rail became a participant in the self-insurance program.

Insurance Coverage. In 1994 with insurance prices becoming more reasonable, all divisions again elected to purchase insurance for third party liability losses to which they may be exposed. Coverage levels are \$60.0 million for Tacoma Power and Tacoma Water with a \$1.5 million retention and \$100.0 million aggregate coverage with a \$50.0 million limit per occurrence for Tacoma Rail with \$1.0 million retention. The policies for Tacoma Power, Tacoma Water, Tacoma Rail and Public Officials coverage are "occurrence based" type policies. Additionally, all divisions now have Public Officials Liability Insurance; coverage is \$1.3 million for each wrongful act with \$2.6 million aggregate coverage with a \$200,000 retention level for each wrongful act. The Department has also purchased "All Risk" property damage insurance. Coverage applies to select properties, vehicles and equipment.

Basis of Financial Statements. The Self-Insurance Fund is an Internal Service Fund of the City of Tacoma operated by the Department of Public Utilities.

Cash and Equity in Pooled Investments. The Fund'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 Fund, 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 certificates of deposit with East West Bank and Opus Bank.

The Fund's equity in that portion of the City of Tacoma Investment Pool held in qualified public depositories at December 31, 2017 and 2016 is entirely covered by the Federal Deposit Insurance Corporation (FDIC) and the Washington State Public Deposit Protection Commission (WSPDPC).

SELF-INSURANCE CLAIM FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

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.

Incurred but Not Reported (IBNR). The Fund uses accrual basis of accounting for recognizing not only claims that have been asserted where probable loss is estimable but also cases where incidents have occurred but where claims have not been reported. For incurred but not reported incidents, a reasonable estimate has been made of the potential expense where it appears probable that a claim will be asserted.

NOTE 2 INVESTMENTS MEASURED AT FAIR VALUE

The City measures and records its investments within the fair value hierarchy established by generally accepted accounting principles.

The Hierarchy is based on the valuation inputs used to measure the fair value of the asset, where fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. These guidelines recognize a three-tiered fair value hierarchy, as follows:

- Level 1 - Level 1 inputs are quoted (adjusted) prices in active markets for identical assets or liabilities that the government can access at the measurement data. Observable markets include exchange markets, dealer markets, brokered markets and principal-to-principal markets.
- Level 2 - Level 2 inputs are other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs are sourced from pricing vendors using models that are market-based and corroborated by observable market data including: quoted prices; nominal yield spreads; benchmark yield curves; and other corroborated inputs.
- Level 3 - Level 3 inputs are unobservable inputs for the asset or liability and should only be used when relevant Level 1 or Level 2 inputs are unavailable.

The fair value evaluations are provided by Interactive Data. Interactive Data utilizes evaluated pricing models that vary by asset class and incorporate available trade, bid and other market information and for structured securities, cash flow and, when available, loan performance data. Because many fixed income securities do not trade on a daily basis, Interactive Data's evaluated pricing applications apply available information as applicable through processes such as benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing, to prepare evaluations. In addition, Interactive Data uses model processes, such as the Option Adjusted Spread model to assess interest rate impact and development payment scenarios. Their models and processes take into account market convention. For each asset class, a team of evaluators gathers information from market sources and integrates relevant credit information, perceived market movements and sector news into the evaluated pricing applications and models.

SELF-INSURANCE CLAIM FUND
NOTES TO FINANCIAL STATEMENTS
(continued)

Cash and cash equivalents include highly liquid investments including short-term investment funds. Cash and cash equivalents are valued at cost and, therefore, excluded from the fair value schedule.

Data regarding the City's investments, valued and categorized according to the above outlined levels, is below:

	As of 12/31/2017	Level 1	Level 2	Level 3
Debt Securities				
U.S. Treasury Securities	\$ 218,142,864	\$ -	\$ 218,142,864	\$ -
U.S. Agency Securities	517,345,818	-	517,345,818	-
Supranational Securities	19,966,040		19,966,040	
Municipal Bonds	40,760,727	-	40,760,727	-
Total	<u>\$ 796,215,449</u>	<u>\$ -</u>	<u>\$ 796,215,449</u>	<u>\$ -</u>

	As of 12/31/2016	Level 1	Level 2	Level 3
Debt Securities				
U.S. Treasury Securities	\$ 146,824,628		\$ 146,824,628	\$ -
U.S. Agency Securities	544,579,831	-	544,579,831	-
Municipal Bonds	61,450,051	-	61,450,051	-
Total	<u>\$ 752,854,510</u>	<u>\$ -</u>	<u>\$ 752,854,510</u>	<u>\$ -</u>

Self Insurance's share of the City Investments shown in the table above is 0.76% and 0.95% for 2017 and 2016.

NOTE 3 PENDING LEGAL ACTIONS AND CLAIMS FOR WHICH THE EXPOSURE TO LIABILITY MAY EXCEED \$300,000 PER OCCURRENCE.

Miscellaneous. Tacoma Public Utilities has received several miscellaneous claims that either do not allege significant amounts, or that the Legal Department has determined do not pose a risk of liability to the Utilities.

STATISTICAL DATA

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
SELF-INSURANCE CLAIM FUND

CLAIMS STATISTICS SUMMARY - DECEMBER 31, 2017

NUMBER OF CLAIMS PAID (JANUARY 1 - DECEMBER 31, 2017)

	<u>Tacoma Power</u>	<u>Tacoma Water</u>	<u>Tacoma Rail</u>	<u>Svc. Divs.</u>	<u>Total</u>
Over \$5,000	8	7	14	-	29
\$1,001 - 5,000	17	10	-	-	27
\$501 - 1,000	9	3	-	-	12
\$100 - 500	3	16	-	-	19
Less than \$100	<u>2</u>	<u>4</u>	<u>-</u>	<u>1</u>	<u>7</u>
	39	40	14	1	94
Total Dollar Amount of Claims Paid	208,938	\$119,828	\$1,088,431	\$25	\$1,417,222

NUMBER OF CLAIMS ACCRUED AT DECEMBER 31, 2017

Over \$50,000	13	-	1	-	14
\$10,000 - 50,000	14	6	6	-	26
Less than \$10,000	<u>271</u>	<u>93</u>	<u>4</u>	<u>4</u>	<u>372</u>
	298	99	11	4	412
Total Dollar Amount Accrued for Known Claims	\$3,367,761	\$262,311	\$377,500	\$1,156	\$4,008,728
Total Dollar Amount Accrued for Unknown Claims	<u>\$483,963</u>	<u>\$181,413</u>	<u>\$1,177,856</u>	<u>\$5,232</u>	<u>\$1,848,464</u>
Total Dollar Amount Accrued for All Claims	<u><u>\$3,851,724</u></u>	<u><u>\$443,724</u></u>	<u><u>\$1,555,356</u></u>	<u><u>\$6,388</u></u>	<u><u>\$5,857,192</u></u>

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
SELF-INSURANCE CLAIM FUND

CLAIMS STATISTICS DETAIL - DECEMBER 31, 2017

NUMBER OF CLAIMS PAID (JANUARY 1 - DECEMBER 31, 2017)

Range	Non-Vehicular Bodily Injury/Property Damage			
	Tacoma Power	Tacoma Water	Tacoma Rail	Svc. Divs.
Over \$5,000	6	7	14	-
\$1,001 - 5,000	17	8	-	-
\$501 - 1,000	8	3	-	-
\$100 - 500	2	16	-	-
Less than \$100	1	4	-	1
	34	38	14	1
Total Dollar Amount of Claims Paid	\$183,809	\$116,057	\$1,088,431	\$25
Average Dollar Amount of Claims Paid	\$5,406	\$3,054	\$77,745	\$25

NUMBER OF CLAIMS ACCRUED AT DECEMBER 31, 2017

Range	Non-Vehicular Bodily Injury/Property Damage			
	Tacoma Power	Tacoma Water	Tacoma Rail	Svc. Divs.
Over \$50,000	13	-	1	-
\$10,000 - 50,000	14	5	6	-
Less than \$10,000	255	83	4	4
	282	88	11	4
Total Dollar Amount Accrued for Known Claims .	\$3,345,876	\$243,448	\$377,500	\$1,156
Total Dollar Amount Accrued for Unknown Claims	\$483,963	\$181,413	\$1,177,856	\$5,232
Total Dollar Amount Accrued for All Claims ...	\$3,829,839	\$424,861	\$1,555,356	\$6,388

Vehicular Bodily Injury/Property Damage				Contract/Harassment			
Tacoma Power	Tacoma Water	Tacoma Rail	Svc. Divs.	Tacoma Power	Tacoma Water	Tacoma Rail	Svc. Divs.
2	-	-	-	-	-	-	-
-	2	-	-	-	-	-	-
1	-	-	-	-	-	-	-
1	-	-	-	-	-	-	-
1	-	-	-	-	-	-	-
5	2	-	-	-	-	-	-
\$25,129	\$3,771	-	-	-	-	-	-
\$5,026	\$1,886	-	-	-	-	-	-

Vehicular Bodily Injury/Property Damage				Contract/Harassment			
-	-	-	-	-	-	-	-
-	1	-	-	-	-	-	-
16	10	-	-	-	-	-	-
16	11	-	-	-	-	-	-
\$21,885	\$18,863	-	-	-	-	-	-
-	-	-	-	-	-	-	-
\$21,885	\$18,863	-	-	-	-	-	-

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
SELF-INSURANCE CLAIM FUND

TEN-YEAR FINANCIAL REVIEW

STATEMENTS OF NET POSITION	2008	2009	2010
ASSETS			
Current	\$4,788,153	\$4,564,534	\$4,483,283
TOTAL ASSETS	4,788,153	4,564,534	4,483,283
LIABILITIES			
Current	1,878,524	1,415,874	2,540,439
NET POSITION	2,909,629	3,148,660	1,942,844
TOTAL LIABILITIES AND NET POSITION	\$4,788,153	\$4,564,534	\$4,483,283
STATEMENTS OF INCOME			
INCOME			
Premiums	\$804,000	\$324,000	\$324,000
Interest	197,619	121,687	71,595
Litigation Settlement Refund	-	-	-
Total	1,001,619	445,687	395,595
EXPENSES			
Claims	361,226	(148,043)	1,347,562
Claims Handling Expense	426,651	197,319	103,138
Incidental & Admin. Expense	197,892	157,380	150,711
Total	985,769	206,656	1,601,411
NET INCOME (LOSS)	\$15,850	\$239,031	(\$1,205,816)

2011	2012	2013	2014	2015	2016	2017
<u>\$3,934,405</u>	<u>\$5,359,525</u>	<u>\$5,681,826</u>	<u>\$6,227,388</u>	<u>\$6,855,931</u>	<u>\$7,633,129</u>	<u>\$7,028,558</u>
3,934,405	5,359,525	5,681,826	6,227,388	6,855,931	7,633,129	7,028,558
2,193,523	3,441,738	4,902,069	5,994,441	4,707,462	4,826,678	5,878,150
<u>1,740,882</u>	<u>1,917,787</u>	<u>779,757</u>	<u>232,947</u>	<u>2,148,469</u>	<u>2,806,451</u>	<u>1,150,408</u>
\$3,934,405	\$5,359,525	\$5,681,826	\$6,227,388	\$6,855,931	\$7,633,129	\$7,028,558
\$744,000	\$2,470,377	\$1,040,004	\$1,040,004	\$1,240,000	\$1,240,000	\$1,206,667
123,337	78,820	23,559	52,827	35,169	61,576	59,596
<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
867,337	2,549,197	1,063,563	1,092,831	1,275,169	1,301,576	1,266,263
680,886	1,678,679	1,817,285	1,375,087	(968,980)	350,057	2,464,390
270,349	560,911	248,952	134,293	196,895	172,963	318,999
<u>118,064</u>	<u>132,702</u>	<u>135,356</u>	<u>130,261</u>	<u>131,732</u>	<u>120,574</u>	<u>138,917</u>
1,069,299	2,372,292	2,201,593	1,639,641	(640,353)	643,594	2,922,306
(\$201,962)	\$176,905	(\$1,138,030)	(\$546,810)	\$1,915,522	\$657,982	(\$1,656,043)



The City of Tacoma does not discriminate on the basis of disability in any of its programs, activities, or services. To request this information in an alternative format or to request a reasonable accommodation, please contact the City Clerk's Office at (253) 591-5505. TTY or speech to speech users please dial 711 to connect to Washington Relay Services.

ANNUAL

TACOMA RAIL

2017

**FINANCIAL
REPORT**



Public Utility Board

MONIQUE TRUDNOWSKI
Chair

WOODROW JONES
Vice-Chair

KAREN LARKIN
Secretary

BRYAN FLINT
Member

MARK PATTERSON
Member

LINDA MCCREA
Interim Director of Utilities/CEO

DALE KING
Rail Superintendent

ANDREW CHERULLO
Finance Director

DEPARTMENT OF PUBLIC UTILITIES

CITY OF TACOMA

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES

TACOMA RAIL

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FINANCIAL DATA

Report of Independent Auditors

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

Report on the Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Department of Public Utilities, Rail Division (the Division), which comprise the statements of net position as of December 31, 2017 and 2016, and the related statements of revenues, 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, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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 City of Tacoma, Department of Public Utilities, Rail Division as of December 31, 2017 and 2016, and the results of its operations and 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, schedule of proportionate share of net pension liability, and schedule of employer contributions, as listed in the table of contents, 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 opinions on the financial statements taken as a whole. The statistical data on pages 34 through 44 and the superintendent's report on pages 45 through 46 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 do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated April 18, 2018, on our consideration of City of Tacoma, Department of Public Utilities, Rail Division's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Division's internal control over financial reporting and compliance.



Tacoma, Washington
April 18, 2018

MANAGEMENT DISCUSSION AND 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, 2017, 2016 and 2015. 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, 2017 and 2016, 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 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 2017 indicate a decrease in both intermodal platform traffic and non-intermodal traffic. Ocean shipping lines continued consolidating their routes and realigned their vessel-sharing agreements. The new shipping alliance started calling the Port of Seattle in May of 2017 causing the decrease in intermodal traffic. This also caused some of the related non-intermodal traffic, like transloaders, to follow. Miscellaneous switching charges increased due to new charges in 2017 associated with intraterminal intermodal switching movements. Locomotive servicing revenues remain strong due to both the Union Pacific and BNSF's reliance of the service.

Overview of the Financial Statements

Tacoma Rail is reporting a change in net position of (\$0.9) million in 2017, compared to \$2.0 million in 2016, a decrease of \$2.9 million. The decrease in net position is predominately due to a decrease of \$0.1 million in operating revenues, an increase of \$0.9 million in operating expenses, a decrease in non-operating revenues of \$1.0 million, and a decrease of \$0.9 million in contributions.

In 2016, Tacoma Rail realized a change in net position of \$2.0 million, compared to \$2.8 million in 2015, a decrease of \$0.8 million. The decrease in net position was due to an increase of \$1.7 million in operating revenues, an increase of \$2.8 million in operating expenses, and an increase in non-operating revenue of \$0.4 million.

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

OPERATING RESULTS					
(in thousands)					
<u>Description</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>17/16 Increase (Decrease)</u>	<u>16/15 Increase (Decrease)</u>
Operating Revenues	\$ 30,717	\$ 30,827	\$ 29,165	\$ (110)	\$ 1,662
Operating Expenses	29,529	28,608	25,806	921	2,802
Operating Income	1,188	2,219	3,359	(1,031)	(1,140)
Net Non-Operating Revenues	458	1,425	1,061	(967)	364
Contributions	36	939	846	(903)	93
Transfers Out	(2,549)	(2,591)	(2,455)	42	(136)
Change in Net Position	<u>\$ (867)</u>	<u>\$ 1,992</u>	<u>\$ 2,811</u>	<u>\$ (2,859)</u>	<u>\$ (819)</u>

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)

<u>Description</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>17/16</u>	<u>16/15</u>
				<u>Increase</u> <u>(Decrease)</u>	<u>Increase</u> <u>(Decrease)</u>
Capital Assets (Net)	\$ 26,706	\$ 28,217	\$ 24,748	\$ (1,511)	\$ 3,469
Current and Other Assets	13,964	14,026	14,909	(62)	(883)
Total Assets	\$ 40,670	\$ 42,243	\$ 39,657	\$ (1,573)	\$ 2,586
Net Investment in Capital Assets	\$ 20,662	\$ 22,003	\$ 18,246	\$ (1,341)	\$ 3,757
Restricted Net Position	-	65	65	(65)	-
Unrestricted Net Position	7,505	6,966	8,731	539	(1,765)
Total Net Position	28,167	29,034	27,042	(867)	1,992
Long-Term Debt, net of current maturities	5,223	5,397	5,556	(174)	(159)
Current and Long Term Liabilities	7,280	7,812	7,059	(532)	753
Total Liabilities	12,503	13,209	12,615	(706)	594
Total Net Position & Liabilities	\$ 40,670	\$ 42,243	\$ 39,657	\$ (1,573)	\$ 2,586

Revenues

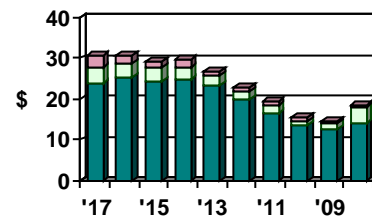
2017 Compared to 2016

In 2017, Tacoma Rail operating revenues of \$30.7 million were \$0.1 million lower than the \$30.8 million in 2016. Overall switching revenues decreased \$0.8 million (2.8%), from 2016. The following table summarizes the switching revenues by activity type for the last two years.

<u>Activity Types</u>	<u>Rail Cars</u>				<u>Switching Revenues</u> <u>(in thousands)</u>			
	<u>2017</u>	<u>2016</u>	<u>Var</u>	<u>%Chg</u>	<u>2017</u>	<u>2016</u>	<u>Var</u>	<u>%Chg</u>
Intermodal Line Hauls	61,300	76,714	(15,414)	-20.1%	\$ 10,544	\$ 12,718	(2,174)	-17.1%
Commercial Line Hauls	27,762	29,583	(1,821)	-6.2%	12,875	12,643	232	1.8%
Capital Div. Line Hauls	686	762	(76)	-10.0%	286	323	(37)	-11.5%
Miscellaneous Switches	17,382	3,863	13,519	350.0%	2,944	1,734	1,210	69.8%
Total Line Hauls	107,130	110,922	(3,792)	-3.4%	\$ 26,649	\$ 27,418	\$ (769)	-2.8%

Demurrage and other operating revenues increased \$0.7 million. Demurrage revenue increased by \$53,000 and locomotive servicing revenue and other revenue increased \$0.6 million. This was due to both the Union Pacific and BNSF's increased demand for locomotive servicing.

OPERATING REVENUES
(in millions)



■ Line Hauls ■ Demurrage ■ Misc Switches

2016 Compared to 2015

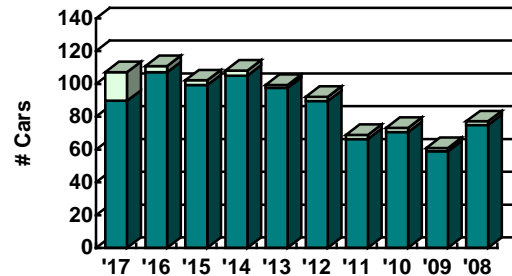
In 2016, Tacoma Rail operating revenues of \$30.8 million were \$1.7 million higher than the \$29.2 million in 2015. Overall switching revenues increased \$1.7 million (6.7%), from 2015.

Switching Activities

Switching activities decreased in 2017 by 3,792 cars (3.4%) to 107,130, from 110,922 in 2016. The most significant decrease in switching activity can be seen in intermodal line-hauls which were down by 15,414 cars (20.1%) due to a decrease in intermodal line haul rail traffic. The average number of cars switched over the last ten years is 90,009.

During 2016, total switching activities increased by 8,749 cars (8.6%) from 2015. The increase in intermodal line haul rail traffic was the dominant factor. Intermodal line-hauls were up by 8,261 cars (12.1%) in 2016.

SWITCHING ACTIVITIES
(in thousands)



■ Line ■ Miscellaneous

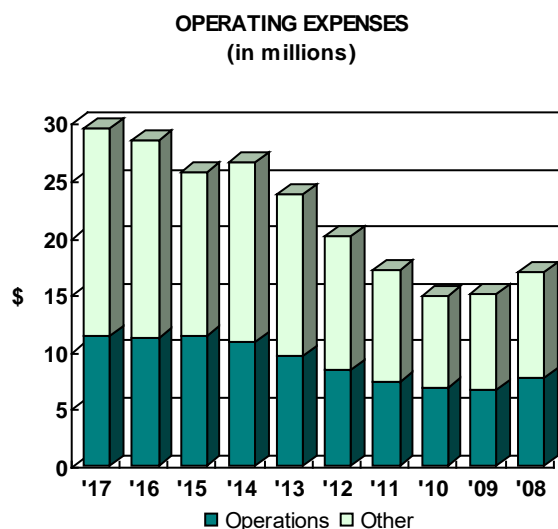
The table below shows the changes in switching volumes for the last three years.

<u>Description</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>17/16</u>	<u>16/15</u>
				<u>Increase</u> <u>(Decrease)</u>	<u>Increase</u> <u>(Decrease)</u>
Line Hauls	89,748	107,059	99,277	(17,311)	7,782
Miscellaneous Switches	17,382	3,863	2,896	13,519	967
Total Cars Switched	107,130	110,922	102,173	(3,792)	8,749

Expenses

2017 Compared to 2016

In 2017, Tacoma Rail operating expenses of \$29.5 million were \$0.9 million higher than the \$28.6 million in 2016. Salaries and wages increased \$0.4 million due to cost of living adjustments, additional personnel and increased overtime. Supplies and expenses increased \$0.4 million primarily due to a decrease in intermodal volume incentives. Depreciation also increased \$0.1 million due to an increase in depreciable assets compared to the same period.



2016 Compared to 2015

In 2016, Tacoma Rail operating expenses of \$28.6 million were \$2.8 million higher than the \$25.8 million in 2015. This was primarily due to a decrease of \$0.2 million in salaries and wages and increase of \$2.7 million in supplies and expenses. The increase is primarily due to the Incurred But Not Reported (IBNR) claims increasing \$1.2 million predominately from a credit adjustment in 2015 and volume incentive increase of \$0.7 million.

Capital Assets

Total Capital Assets decreased \$1.5 million during 2017. This decrease was primarily related to \$1.0 million in retirements and a decrease in the amount of new activity in Construction Work in Progress. During 2017, the Taylor Way Wye Track, Transfer Yard Connection and West End Configuration projects were completed, which resulted in decreased activity in Construction Work in Progress. In 2017, Construction Work in Progress additions were \$0.8 million versus \$4.9 million in 2016.

During 2016, total Capital Assets increased \$3.5 million. This increase was reflected primarily in machinery equipment which increased by \$2.1 million due to the 2014 Locomotive Repower/Replacement project completed in 2016. Road property plant increased \$0.9 million for track upgrades and rehabilitation projects such as East Lead Low Side, Edwards Crossover, Alexander Wye Crossing, Taylor Way and the SR-509 Track Rebuild.

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)

<u>Description</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>17/16</u>	<u>16/15</u>
				<u>Increase</u> <u>(Decrease)</u>	<u>Increase</u> <u>(Decrease)</u>
Land	\$ 160	\$ 167	\$ 160	\$ (7)	\$ 7
Road Property Plant	16,165	14,928	14,951	1,237	(23)
Building	1,932	2,040	1,614	(108)	426
Machinery Equipment	8,176	8,702	7,051	(526)	1,651
Office and Fixture	95	126	156	(31)	(30)
Construction Work In Progress	178	2,254	816	(2,076)	1,438
Total Net Capital Assets	<u>\$ 26,706</u>	<u>\$ 28,217</u>	<u>\$ 24,748</u>	<u>\$ (1,511)</u>	<u>\$ 3,469</u>

Additional information on Tacoma Rail's capital assets can be found in Note 4 to the Financial Statements.

Debt Administration

In 2017, no new Washington State loans from the Department of Transportation were obtained. Draws were taken in 2017 on Transfer Yard Connection (Phase 3), West Lead High Side Rebuild and Taylor Wye Rehabilitation in the amounts of \$33,821, \$369,519 and \$311,457 respectively.

In 2016, no new Washington State loans from the Department of Transportation were obtained for Tacoma Rail. Draws were taken in 2016 on Edwards Crossover Rehabilitation, East Lead Low Side Rebuild, and Transfer Yard Connection (Phase 3) in the amounts of \$119,550, \$404,465 and \$115,029 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 5 to the Financial Statements.

LONG-TERM DEBT
(In thousands)

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>17/16</u>	<u>16/15</u>
				<u>Increase</u> <u>(Decrease)</u>	<u>Increase</u> <u>(Decrease)</u>
Long-Term Debt Balance, December 31	\$ 6,044	\$ 6,213	\$ 6,502	\$ (169)	\$ (289)

Debt Service Coverage

Tacoma Rail is required by its bond covenants to maintain a 1.25 times debt service coverage. As of 2017, Tacoma Rail has no bonds, only interest free loans. In 2016, principal and interest were covered 19.68 times compared to 21.75 times in 2015.

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 independently 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.



Linda McCrea
Interim Director of Utilities/CEO



Andrew Cherullo
Finance Director

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL

STATEMENTS OF NET POSITION

ASSETS	DECEMBER 31,	
	2017	2016
CAPITAL ASSETS		
Road and Equipment Property	\$46,585,758	\$44,809,760
Less Accumulated Depreciation	(20,058,523)	(18,847,293)
Total	26,527,235	25,962,467
Construction Work in Progress	178,476	2,254,277
Net Capital Assets	26,705,711	28,216,744
 SPECIAL FUNDS		
Debt Service Funds	-	64,974
Total Special Funds	-	64,974
 CURRENT ASSETS		
Cash & Equity in Pooled Investments	8,729,263	7,986,328
Customer Accounts Receivable	3,222,019	3,133,279
(Net of Allowance for Doubtful Accounts of \$157,883 in 2017 and \$93,597 in 2016)		
Interfund Receivable	157,958	9,827
Prepayments	688,313	1,807,210
Materials and Supplies Inventory	1,166,772	1,024,333
Total Current Assets	13,964,325	13,960,977
 TOTAL ASSETS	\$40,670,036	\$42,242,695

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

	DECEMBER 31,	
NET POSITION AND LIABILITIES	2017	2016
NET POSITION		
Net Investment in Capital Assets.....	\$20,661,984	\$22,003,325
Restricted for:		
Debt Service	-	64,974
Unrestricted	7,505,391	6,965,599
TOTAL NET POSITION	28,167,375	29,033,898
LONG-TERM DEBT, NET OF CURRENT MATURITIES		
State Loans.....	5,223,477	5,397,028
Total Long-Term Debt	5,223,477	5,397,028
CURRENT LIABILITIES		
Accounts Payable	753,674	885,690
Customer Deposits	-	10,500
Wages Payable and Compensated Absences	315,741	279,822
Unemployment and Other Tax Payables	289,858	290,010
Volume Incentive Payable	-	1,249,999
Current Portion of Long-Term Debt	820,250	816,390
Interest Payable	-	866
Interfund Payable	60,733	260,518
Total Current Liabilities	2,240,256	3,793,795
LONG-TERM LIABILITIES		
On the Job Injury Reserve	829,761	773,407
Long-Term Portion of Compensated Absences	1,011,762	1,003,644
Other Post Employment Benefits	1,625,881	1,001,889
Incurred but not Reported Claims	1,571,524	1,239,034
Total Long-Term Liabilities	5,038,928	4,017,974
TOTAL LIABILITIES	12,502,661	13,208,797
TOTAL NET POSITION AND LIABILITIES	\$40,670,036	\$42,242,695

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	YEAR ENDED DECEMBER 31,	
	2017	2016
OPERATING REVENUES		
Switching Revenues	\$26,648,873	\$27,417,653
Demurrage and Other Operating Revenues	4,068,008	3,409,347
Total Operating Revenues	30,716,881	30,827,000
OPERATING EXPENSES		
Maintenance of Way and Structures	2,202,950	2,963,532
Mechanical	5,227,384	4,712,661
Operations	11,429,489	11,304,238
Administration	8,592,893	7,715,637
Taxes - State	432,081	439,317
Depreciation	1,644,373	1,472,955
Total Operating Expenses	29,529,170	28,608,340
Net Operating Income	1,187,711	2,218,660
NON-OPERATING REVENUES (EXPENSES)		
Interest Income	68,420	86,126
Loss from Disposition of Property	(649,715)	-
Miscellaneous	1,039,772	1,347,695
Interest Expense	(6)	(8,542)
Total Non-Operating Revenues	458,471	1,425,279
Contributions - Grants	-	801,949
Contributions - Others	36,254	137,686
Total Contributions	36,254	939,635
Transfers		
City of Tacoma Gross Earnings Tax	(2,548,959)	(2,591,337)
Total Transfers	(2,548,959)	(2,591,337)
CHANGE IN NET POSITION	(866,523)	1,992,237
TOTAL NET POSITION - BEGINNING OF YEAR	29,033,898	27,041,661
TOTAL NET POSITION - END OF YEAR	\$28,167,375	\$29,033,898

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

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL

STATEMENTS OF CASH FLOWS

	YEAR TO DATE	
	DECEMBER 31, 2017	DECEMBER 31, 2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash from Customers	\$30,469,510	\$30,541,060
Cash Paid to Suppliers	(11,134,999)	(10,258,991)
Cash Paid to Employees	(15,866,186)	(15,509,184)
Taxes Paid	(432,233)	(422,771)
Net Cash Provided by Operating Activities	3,036,092	4,350,114
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Transfers to Other Funds	(2,548,959)	(2,591,337)
Net Cash Used in Non-Capital Financing Activities	(2,548,959)	(2,591,337)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital Expenditures, Net	(133,340)	(4,941,312)
Principal Payments on Long-Term Debt	(884,488)	(932,991)
Interest Paid	(872)	(11,890)
Proceeds from Capital Contributions	36,254	939,635
Proceeds from Long-Term Debt	714,797	644,415
Proceeds from Other Non-Operating Revenues	390,057	1,347,696
Net Cash Provided by/(Used in) Capital and Related Financing Activities	122,408	(2,954,447)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest on Investments	68,420	86,126
Net Cash Provided by/(Used in) Investing Activities	68,420	86,126
Net Increase (Decrease) in Cash and Equity in Pooled Investments	677,961	(1,109,544)
Cash & Equity in Pooled Investments at January 1	8,051,302	9,160,846
Cash & Equity in Pooled Investments at December 31	\$8,729,263	\$8,051,302

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

	YEAR TO DATE DECEMBER 31, 2017	YEAR TO DATE DECEMBER 31, 2016
Reconciliation of Operating Income to		
Net Cash Provided by Operating Activities:		
Operating Income	\$1,187,711	\$2,218,660
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:		
Depreciation	1,644,373	1,472,955
Cash provided from changes in operating assets and liabilities:		
Accounts Receivable	(88,740)	(293,763)
Interfund Receivable	(148,131)	43,224
Materials and Supplies Inventory	(142,439)	(86,872)
Prepayments	1,118,897	110,523
Accounts Payable	(132,016)	348,863
Customer Deposits	(10,500)	(35,400)
Unemployment and other Tax Payables	(152)	16,546
Wages Payable and Compensated Absences.....	35,919	36,109
Volume Incentive Payable	(1,249,999)	41,665
Interfund Payable	(199,785)	75,072
Long-Term Portion of Compensated Absences	8,118	(14,412)
On the Job Injury Reserve	56,354	52,378
Other Post Employment Benefits	623,992	306,260
Incurred but not Reported Claims	332,490	58,306
Total Adjustments	1,848,381	2,131,454
Net Cash Provided by Operating Activities	<u>\$3,036,092</u>	<u>\$4,350,114</u>
Reconciliation of Cash and Equity in Pooled Investments to Balance Sheet:		
Cash and Equity in Pooled Investments in Special Funds	-	\$64,974
Cash and Equity in Pooled Investments in Operating Funds	8,729,263	7,986,328
Cash and Equity in Pooled Investments at December 31	<u>\$8,729,263</u>	<u>\$8,051,302</u>

**CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL**

**NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016**

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 Power 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 2018.

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 certificates of deposit with East West Bank and Opus Bank.

The Division's equity in that portion of City Tacoma Investment Pool held in qualified public depositories at December 31, 2017 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 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.

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 Generally Accepted Accounting Principles, 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.

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. Sick leave pay is recorded as an expense in the year earned.

The accrued liability is computed at 100% vacation and PTO while sick leave is accrued at 10%, which is considered the amount vested or 25% if the employee meets retirement criteria. Based on historical information, 10% of compensated absences are considered short term.

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 deferred outflows and liabilities and deferred inflows 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 INVESTMENTS MEASURED AT FAIR VALUE

The City measures and records its investments within the fair value hierarchy established by generally accepted accounting principles.

The hierarchy is based on the valuation inputs used to measure the fair value of the asset, where fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. These guidelines recognize a three-tiered fair value hierarchy, as follows:

- Level 1 – Level 1 inputs are quoted (unadjusted) prices in active markets for identical assets or liabilities that the government can access at the measurement date. Observable markets include exchange markets, dealer markets, brokered markets and principal-to-principal markets.
- Level 2 – Level 2 inputs are other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs are sourced from pricing vendors using models that are market-based and corroborated by observable market data including: quoted prices; nominal yield spreads; benchmark yield curves; and other corroborated inputs.
- Level 3 – Level 3 inputs are unobservable inputs for the asset or liability and should only be used when relevant Level 1 or Level 2 inputs are unavailable.

The fair value evaluations are provided by Interactive Data. Interactive Data utilizes evaluated pricing models that vary by asset class and incorporate available trade, bid and other market information and for structured securities, cash flow and, when available, loan performance data. Because many fixed income securities do not trade on a daily basis, Interactive Data's evaluated pricing applications apply available information as applicable through processes such as benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing, to prepare evaluations. In addition, Interactive Data uses model processes, such as the Option Adjusted Spread model to assess interest rate impact and development payment scenarios. Their models and processes take into account market convention. For each asset class, a team of evaluators gathers information from market sources and integrates relevant credit information, perceived market movements and sector news into the evaluated pricing applications and models.

TACOMA RAIL NOTES TO FINANCIAL STATEMENTS (continued)

Cash and cash equivalents include highly liquid investments including short-term investment funds. Cash and cash equivalents are valued at cost and, therefore, excluded from the fair value schedule.

Data regarding the City's investments, valued and categorized according to the above outlined levels, is below:

	As of			
Debt Securities	12/31/2017	Level 1	Level 2	Level 3
U.S. Treasury Securities	\$ 218,142,864	\$ -	\$ 218,142,864	\$ -
U.S. Agency Securities	517,345,818	-	517,345,818	-
Supranational Securities	19,966,040	-	19,966,040	-
Municipal Bonds	40,760,727	-	40,760,727	-
	<u>\$ 796,215,449</u>	<u>\$ -</u>	<u>\$ 796,215,449</u>	<u>\$ -</u>

	As of			
Debt Securities	12/31/2016	Level 1	Level 2	Level 3
U.S. Treasury Securities	\$ 146,824,628	\$ -	\$ 146,824,628	\$ -
U.S. Agency Securities	544,579,831	-	544,579,831	-
Municipal Bonds	61,450,051	-	61,450,051	-
	<u>\$ 752,854,510</u>	<u>\$ -</u>	<u>\$ 752,854,510</u>	<u>\$ -</u>

Tacoma Rail's share of the City Investments shown in the table above is 0.94% and 1.16% as of December 31, 2017 and 2016.

NOTE 4 CAPITAL ASSETS

A summary of the balances and changes in capital assets for 2017 and 2016 follows:

	Balance			Transfers &	Balance
	December 31,			Adjustments	December 31,
	2016	Additions	Retirements		2017
Land	\$ 167,256	\$ -	\$ -	\$ (6,800)	\$ 160,456
Road Property Plant	26,685,617	2,818,803	(1,082,858)	-	28,421,562
Building	4,457,044	40,003	-	7,162	4,504,209
Machinery Equipment	12,814,201	-	-	(385)	12,813,816
Office and Fixture	685,642	-	-	73	685,715
Total Capital Assets In Service	44,809,760	2,858,806	(1,082,858)	50	46,585,758
Less Accumulated Depreciation	(18,847,293)	(1,644,373)	433,143	-	(20,058,523)
	<u>25,962,467</u>	<u>1,214,433</u>	<u>(649,715)</u>	<u>50</u>	<u>26,527,235</u>
Construction Work In Progress	2,254,277	798,362	-	(2,874,163)	178,476
Net Capital Assets	<u>\$ 28,216,744</u>	<u>\$ 2,012,795</u>	<u>\$ (649,715)</u>	<u>\$ (2,874,113)</u>	<u>\$ 26,705,711</u>

TACOMA RAIL NOTES TO FINANCIAL STATEMENTS (continued)

	Balance December 31, 2015	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2016
Land	\$ 160,456	\$ 6,800	\$ -	\$ -	\$ 167,256
Road Property Plant	25,818,064	867,553	-	-	26,685,617
Building	3,916,280	540,764	-	-	4,457,044
Machinery Equipment	10,726,901	2,087,300	-	-	12,814,201
Office and Fixture	685,255	387	-	-	685,642
Total Capital Assets In Service	41,306,956	3,502,804	-	-	44,809,760
Less Accumulated Depreciation	(17,374,337)	(1,472,956)	-	-	(18,847,293)
	23,932,619	2,029,848	-	-	25,962,467
Construction Work In Progress	815,769	4,941,312	-	(3,502,804)	2,254,277
Net Capital Assets	<u>\$ 24,748,388</u>	<u>\$ 6,971,160</u>	<u>\$ -</u>	<u>\$ (3,502,804)</u>	<u>\$ 28,216,744</u>

NOTE 5 LONG-TERM DEBT

Long-term debt activities for 2017 and 2016 were as follows:

	Balance December 31, 2016	Additions	Reductions	Balance December 31, 2017	Due Within One Year
Revenue Bonds	\$ 64,238	\$ -	\$ (64,238)	\$ -	\$ -
Department of Transportation State Loans	6,149,180	714,797	(820,250)	6,043,727	820,250
Total Long-Term Debt	<u>\$ 6,213,418</u>	<u>\$ 714,797</u>	<u>\$ (884,488)</u>	<u>\$ 6,043,727</u>	<u>\$ 820,250</u>

	Balance December 31, 2015	Additions	Reductions	Balance December 31, 2016	Due Within One Year
Revenue Bonds	\$ 312,763	\$ -	\$ (248,525)	\$ 64,238	\$ 64,238
Department of Transportation State Loans	6,189,230	644,416	(684,466)	6,149,180	752,152
Total Long-Term Debt	<u>\$ 6,501,993</u>	<u>\$ 644,416</u>	<u>\$ (932,991)</u>	<u>\$ 6,213,418</u>	<u>\$ 816,390</u>

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 \$64,238 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. This bond was paid in full on January 1, 2017.

TACOMA RAIL NOTES TO FINANCIAL STATEMENTS (continued)

JUNIOR LIEN DEBT

Washington State Department of Transportation Loans (WSDOT)	2017	2016
2009 WSDOT loan for locomotive idling improvement, with 0% interest, due in yearly installments of \$1,759 from 2010 through 2024.	12,313	14,072
2009 WSDOT loan for locomotive servicing facility upgrades, with 0% interest, due in yearly installments of \$16,630 from 2011 through 2025.	133,042	149,672
2011 WSDOT loan for locomotive repower, with 0% interest, due in yearly installments of \$45,000 from 2013 through 2022.	225,000	270,000
2012 WSDOT loan for Tacoma Rail Annie Tracks 1&2 Rail Relay, with 0% interest, due in yearly installments of \$61,200 from 2013 through 2022.	306,000	367,200
2012 WSDOT loan for Yard Tracks 2, 3 & 4, with 0% interest, due in yearly installments of \$34,859 from 2013 through 2022.	174,296	209,155
2013 WSDOT loan for East 11th Street Crossing, with 0% interest, due in yearly installments of \$34,732 from 2014 through 2023.	208,392	243,124
2013 WSDOT loan for Yard Tracks 5 & 6, with 0% interest, due in yearly installments of \$36,394 from 2014 through 2023.	218,362	254,756
2013 WSDOT loan for Yard Tracks 8 & 9, with 0% interest, due in yearly installments of \$61,863 from 2015 through 2024.	433,037	494,900
2013 WSDOT loan for Port Pass West, with 0% interest, due in yearly installments of \$25,000 from 2015 through 2024.	174,997	199,997
2013 WSDOT loan for N. Intermodal Yard lead track, with 0% interest, due in yearly installments of \$36,639 from 2016 through 2025.	293,109	329,748
2013 WSDOT loan for East Loop 17th St., with 0% interest, due in yearly installments of \$77,307 from 2016 through 2025.	618,456	695,763
2013 WSDOT loan for Taylor Way Track Rehabilitation, with 0% interest, due in yearly installments of \$110,506 from 2016 through 2025.	884,046	994,552
2013 WSDOT loan for West Loop, with 0% interest, due in yearly installments of \$51,577 from 2016 through 2025.	412,616	464,193
2014 WSDOT loan for SR509 Track Improvements, with 0% interest, due in yearly installments of \$91,000 from 2016 through 2025.	728,005	819,005
2015 WSDOT loan for Edwards Crossover Rehabilitation, with 0% interest, due in yearly installments of \$12,112 from 2017 through 2026.	109,007	121,119
2015 WSDOT loan for East Lead Low Side Rebuild, with 0% interest, due in yearly installments of \$40,574 from 2017 through 2026.	365,171	405,745

TACOMA RAIL NOTES TO FINANCIAL STATEMENTS (continued)

Junior Lien Debt continued	2017	2016
2015 WSDOT loan for Transfer Yard Connection (Phase 3), with 0% interest, due in yearly installments of \$15,000 from 2017 through 2026.	135,000	116,179
2015 WSDOT loan for West Lead High Side Rebuild, with 0% interest, due in yearly installments of \$36,952 from 2017 through 2026.	332,567	-
2015 WSDOT loan for Taylor Wye Rehabilitation, with 0% interest, due in yearly installments of \$31,146 from 2017 through 2026.	280,311	-
Subtotal Junior Lien Debt	6,043,727	6,149,180
Less Current Portion of Debt	(820,250)	(752,152)
Long-term Portion of Junior Lien Debt	<u>\$ 5,223,477</u>	<u>\$ 5,397,028</u>

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

	Principal	Interest
2018	\$ 820,250	\$ -
2019	\$ 820,250	\$ -
2020	\$ 820,250	\$ -
2021	\$ 820,250	\$ -
2022	\$ 820,250	\$ -
2023-2026	\$ 1,942,477	\$ -
	<u>\$ 6,043,727</u>	<u>\$ -</u>

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 junior lien debt is subject to certain financial and non-financial covenants.

NOTE 6 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 32% and 46% of total revenues, respectively, in 2017. Revenue in 2016 was 25% and 49%, respectively. Accounts receivable from UP and BNSF in 2017 represented 37% and 35% of total customer accounts receivable, respectively. Accounts receivable in 2016 was 29% and 49%, respectively.

NOTE 7 FLEET SERVICES FUND

The Department of Public Utilities has established a Fleet Services Fund to perform scheduled maintenance, repair and replacement of the Department vehicles and related equipment. 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 2017 and 2016 were \$526,433 and \$511,522, respectively.

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 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 \$266,667 in 2017 and \$100,000 in 2016. Assets in the Self-Insurance Fund total \$7.0 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.

Other 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 property insurance policy has a deductible of \$250,000 for buildings and property within buildings and \$10,000 per vehicle. General government obtains coverage on general government's buildings and property within buildings with a limit of \$500,000 and a retention of \$150,000 with exceptions. For the Department, 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 \$20 million of excess coverage with a \$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 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 2017 and 2016, Tacoma Rail contributed \$2,140,844 and \$2,092,517 respectively, per structures set forth by the United States Railroad Retirement Board shown as follows:

	EARNINGS BASE	
	2017	2016
Employer Tier I	\$ 127,200	\$ 118,500
Employer Tier II	94,500	88,200
Employer Medicare	No Limit	No Limit

	TAX RATE	
	2017	2016
Employer Tier I	6.20%	6.20%
Employer Tier II	13.10%	13.10%
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 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. GASB 45 requires that the portion of age-adjusted expected retiree health claims costs that exceed the premium charged to retirees be recognized as a liability for accounting purposes. 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 (3.50%).

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 under GASB 45. 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 2017 is 20 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 statements of net position. The City has a Net OPEB Obligation as of December 31, 2017 as the City has not set aside funds for OPEB.

EXCISE TAX FOR HIGH COST OR “CADILLAC” HEALTH PLANS IN 2020 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 Consolidated Appropriations Act (CAA), which was signed into law in December 2015, delays the tax for two years, until 2020.

GASB Statement No. 45, as well as GASB 74 and 75, 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. 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.

There is significant uncertainty with respect to the excise tax at this time. President Trump recently signed an executive order which gives instruction to the leaders of the new administration to unwind certain aspects of the ACA, especially those components deemed “burdensome.” It remains unclear how this would be implemented, especially due to the interconnected nature of the ACA. The City has continued to value the excise tax as it currently appears in the tax code, but will monitor this situation carefully going forward.

SUMMARY OF CHANGES – As of the January 1, 2017 valuation the total AAL was \$240,449,771, for the City, 12.5% higher than expected primarily due to changes in demographic experience, medical cost expectations and medical trend assumptions, and demographic and economic assumptions.

TACOMA RAIL NOTES TO FINANCIAL STATEMENTS (continued)

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

	January 1, 2015	January 1, 2017
Total membership:		
Active employees	3404	3492
Terminated vested employees	442	476
Retired employees & dependents	744	691
Total	<u>4,590</u>	<u>4,659</u>
Annual Benefit Payments	\$ 8,963,089	\$ 9,010,942
Discount rate	3.75%	3.50%
Present Value of Benefits (PVB)	\$ 262,184,195	\$ 289,047,229
Actuarial Accrued Liability (AAL)	\$ 208,814,312	\$ 240,449,771
Assets	\$ -	\$ -
Unfounded Actuarial Accrued Liability (UAAL)	<u>\$ 208,814,312</u>	<u>\$ 240,449,771</u>
Normal Cost	\$ 3,832,131	\$ 3,261,947
Annual Required Contribution (ARC)	\$ 16,966,964	\$ 19,529,549

The following table shows the total value of the benefits provided, the member paid premiums and the City paid benefits as of January 1, 2017.

Value of Subsidy at 3.50% Interest Rate	Total Value of Benefits	Member Paid Premiums	City Paid Benefits
Present Value of Benefits (PVB)	\$ 399,300,824	\$ 110,253,595	\$ 289,047,229
Actuarial Accrued Liability (AAL)	\$ 285,825,708	\$ 45,375,937	\$ 240,449,771
Normal Cost	\$ 7,595,595	\$ 4,443,955	\$ 3,151,640
Annual Benefit Payments	\$ 11,674,734	\$ 2,663,793	\$ 9,010,941

TACOMA RAIL NOTES TO FINANCIAL STATEMENTS (continued)

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, 2017.

	City	Division
Determination of Annual Required Contribution		
Normal Cost at Year-end	\$ 3,261,947	\$ 490,563
Amortization of UAAL	16,267,602	261,478
Annual Required Contribution (ARC)	<u>\$ 19,529,549</u>	<u>\$ 752,041</u>
Determination of Net OPEB obligation:		
Annual Required Contribution (ARC)	\$ 19,529,549	\$ 752,041
Interest on prior year Net OPEB Obligation	2,895,939	35,066
Adjustments of ARC	<u>(4,743,612)</u>	<u>(48,955)</u>
Annual OPEB Cost	\$ 17,681,876	\$ 738,152
Actual benefits paid	<u>(9,010,941)</u>	<u>(114,160)</u>
Increase in Net OPEB Obligation	\$ 8,670,935	\$ 623,992
NET OPEB Obligation - beginning of year	<u>82,741,128</u>	<u>1,001,889</u>
NET OPEB Obligation - end of year	<u>\$ 91,412,063</u>	<u>\$ 1,625,881</u>

The Division is presented as a liability in the long-term liabilities section 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 3.50% interest rate.

Year Ended	Annual OPEB Cost		Benefits Paid		Net OPEB Obligation	
	City	Division	City	Division	City	Division
12/31/2015	\$ 15,954,387	\$ 411,114	\$ 8,963,089	\$ 78,549	\$ 73,129,502	\$ 695,629
12/31/2016	18,151,028	407,340	8,539,402	101,080	82,741,128	1,001,889
12/31/2017	17,681,876	738,152	9,010,941	114,160	91,412,063	1,625,881

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 20 years.

TACOMA RAIL NOTES TO FINANCIAL STATEMENTS (continued)

Actuarial Methods and Significant Actuarial Assumptions:

Valuation Date:	January 1, 2017														
Census Date:	January 1, 2017														
Actuarial Cost Method:	Entry Age														
Amortization Date:	Combination of level percentage and level dollar amount, see note above.														
Remaining Amortization Period:	20 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:	3.50% for pay-as-you-go funding														
Medical Cost Trend:	<table><tr><td>2017</td><td>9.10%</td></tr><tr><td>2018</td><td>6.40%</td></tr><tr><td>2019</td><td>5.80%</td></tr><tr><td>2020</td><td>5.30%</td></tr><tr><td>2030</td><td>5.40%</td></tr><tr><td>2040</td><td>5.50%</td></tr><tr><td>2050</td><td>5.20%</td></tr></table>	2017	9.10%	2018	6.40%	2019	5.80%	2020	5.30%	2030	5.40%	2040	5.50%	2050	5.20%
2017	9.10%														
2018	6.40%														
2019	5.80%														
2020	5.30%														
2030	5.40%														
2040	5.50%														
2050	5.20%														
	The trend for year 2017 reflects the amount by which 2018 medical costs are expected to exceed 2017 medical costs. The medical cost rate is assumed to continue grading downward until achieving the ultimate rate of 4.40% in 2073 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):	3.50%														
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 11 COMMITMENTS AND CONTINGENCIES

LINDA WONNER, EXECUTRIX OF THE ESTATE OF ROBERT W. WONNER, SR. V. TACOMA –

On February 22, 2018, Linda Wonner filed a lawsuit on behalf of the Estate of Robert Wonner in U.S. District Court, alleging that her husband Robert Wonner was exposed to toxic agents during his 40 years of employment with Tacoma Rail resulting in his death on December 17, 2014. Ms. Wonner seeks damages of \$5 million. The City is currently in the discovery stage.

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, 2017.

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 2018. The agreement states that Public Works would fund Tacoma Rail for any operations on the Mountain Division.

STATISTICAL DATA (Unaudited)

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL

TEN-YEAR FINANCIAL REVIEW

STATEMENTS OF NET POSITION	2017	2016	2015	2014
ASSETS				
Railway Plant - Net	\$26,705,711	\$28,216,744	\$24,748,388	\$21,058,809
Other Property and Special Funds ..	-	64,974	64,861	65,104
Current and Accrued Assets	13,964,325	13,960,977	14,843,745	15,964,236
Other Assets	-	-	-	-
TOTAL ASSETS	40,670,036	42,242,695	39,656,994	37,088,149
LIABILITIES				
Long-Term Debt	5,223,477	5,397,028	5,556,302	4,482,801
Current and Accrued Liabilities ..	3,139,600	3,793,795	3,443,589	4,096,245
Long-Term Liabilities	4,139,584	4,017,974	3,615,442	4,278,913
Total Liabilities	12,502,661	13,208,797	12,615,333	12,857,959
NET POSITION	28,167,375	29,033,898	27,041,661	24,230,190
TOTAL LIABILITIES AND NET POSITION ..	\$40,670,036	\$42,242,695	\$39,656,994	\$37,088,149
STATEMENTS OF INCOME				
OPERATING REVENUES				
Switching Revenues	\$26,648,873	\$27,417,653	\$25,690,797	\$26,495,108
Other Operating Revenues	4,068,008	3,409,347	3,474,443	2,962,289
Total Operating Revenues	30,716,881	30,827,000	29,165,240	29,457,397
OPERATING EXPENSES				
Operation and Maintenance	27,452,716	26,696,068	24,168,168	25,063,534
Taxes	432,081	439,317	417,135	429,875
Depreciation	1,644,373	1,472,955	1,220,882	1,069,265
Total Operating Expenses	29,529,170	28,608,340	25,806,185	26,562,674
NET OPERATING INCOME (LOSS)	1,187,711	2,218,660	3,359,055	2,894,723
NON-OPERATING REVENUES (EXPENSE)				
Net Other Income	426,311	2,287,330	1,878,109	1,830,033
Interest Earned on Investments ...	68,420	86,126	51,379	72,535
Interest on Unfunded Debt	(6)	(8,542)	(21,678)	(34,122)
Total Non-Operating Revenues ...	494,725	2,364,914	1,907,810	1,868,446
TRANSFERS OUT				
City Gross Earnings Tax	2,548,959	2,591,337	2,410,016	2,440,631
Transfers to Other Funds	-	-	45,378	310,527
NET INCOME (LOSS)	(\$866,523)	\$1,992,237	\$2,811,471	\$2,012,011

In accordance with Governmental Accounting Standards Board Statement No. 65 both 2012 and 2011 were restated for comparative purposes. Years prior to 2011 are shown as originally reported.

2013	2012	2011	2010	2009	2008
\$18,015,675	\$16,258,926	\$13,958,818	\$9,446,780	\$9,813,322	\$9,422,038
65,110	397,381	399,607	400,792	406,268	414,059
12,961,818	11,397,915	8,867,794	8,686,413	8,474,144	8,912,688
<u>-</u>	<u>-</u>	<u>-</u>	<u>6,103</u>	<u>7,121</u>	<u>8,138</u>
31,042,603	28,054,222	23,226,219	18,540,088	18,700,855	18,756,923
2,764,959	2,166,751	2,001,568	2,101,571	2,641,116	2,878,279
3,232,279	3,920,067	1,762,532	1,602,400	1,569,847	1,768,188
<u>2,827,186</u>	<u>1,617,434</u>	<u>1,315,320</u>	<u>1,226,721</u>	<u>1,634,512</u>	<u>1,245,906</u>
8,824,424	7,704,252	5,079,420	4,930,692	5,845,475	5,892,373
22,218,179	20,349,970	18,146,799	13,609,396	12,855,380	12,864,550
\$31,042,603	\$28,054,222	\$23,226,219	\$18,540,088	\$18,700,855	\$18,756,923
\$24,570,867	\$20,793,364	\$17,250,227	\$14,580,858	\$13,365,092	\$14,690,148
<u>2,372,435</u>	<u>2,250,434</u>	<u>2,153,392</u>	<u>898,739</u>	<u>1,212,804</u>	<u>3,718,926</u>
26,943,302	23,043,798	19,403,619	15,479,597	14,577,896	18,409,074
22,348,268	18,962,149	16,117,560	13,942,626	14,235,461	16,126,814
437,282	404,105	339,525	261,854	214,935	270,106
<u>996,782</u>	<u>824,549</u>	<u>641,315</u>	<u>706,323</u>	<u>577,643</u>	<u>611,148</u>
23,782,332	20,190,803	17,098,400	14,910,803	15,028,039	17,008,068
3,160,970	2,852,995	2,305,219	568,794	(450,143)	1,401,006
1,004,957	1,282,274	3,836,348	1,524,627	1,678,847	860,497
21,155	81,907	132,196	74,327	139,662	264,272
<u>(45,941)</u>	<u>(62,090)</u>	<u>(80,959)</u>	<u>(102,293)</u>	<u>(133,177)</u>	<u>(174,994)</u>
980,171	1,302,091	3,887,585	1,496,661	1,685,332	949,775
2,240,525	1,931,338	1,632,180	1,311,439	1,244,359	1,525,080
<u>32,407</u>	<u>20,577</u>	<u>13,049</u>	<u>-</u>	<u>-</u>	<u>35,088</u>
<u>\$1,868,209</u>	<u>\$2,203,171</u>	<u>\$4,547,575</u>	<u>\$754,016</u>	<u>(\$9,170)</u>	<u>\$790,613</u>

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL

TEN-YEAR SWITCHING STATISTICS

	2017	2016	2015	2014
SWITCHING REVENUES				
Line Hauls	\$23,704,622	\$25,683,614	\$24,334,649	\$24,933,732
Local and Miscellaneous	<u>2,944,251</u>	<u>1,734,039</u>	<u>1,356,148</u>	<u>1,561,376</u>
TOTAL SWITCHING REVENUES	\$26,648,873	\$27,417,653	\$25,690,797	\$26,495,108
NUMBER OF CARS SWITCHED				
Line Hauls	89,748	107,059	99,277	105,079
Local and Miscellaneous	<u>17,382</u>	<u>3,863</u>	<u>2,896</u>	<u>3,058</u>
TOTAL NUMBER OF CARS SWITCHED..	107,130	110,922	102,173	108,137
SWITCHING STATISTICS (AVERAGE)				
Revenue/Line Haul Car	\$264.12	\$239.90	\$245.12	\$237.29
Revenue/Local & Miscellaneous Car	\$169.39	\$448.88	\$468.28	\$510.59

2013	2012	2011	2010	2009	2008
\$23,358,089	\$19,913,410	\$16,395,640	\$13,744,377	\$12,735,114	\$14,277,743
1,212,778	879,954	854,587	836,481	629,978	412,405
\$24,570,867	\$20,793,364	\$17,250,227	\$14,580,858	\$13,365,092	\$14,690,148
97,536	89,554	66,440	70,574	58,892	74,940
1,830	2,563	2,513	2,601	2,032	2,254
99,366	92,117	68,953	73,175	60,924	77,194
\$239.48	\$222.36	\$246.77	\$194.75	\$216.25	\$190.52
\$662.72	\$343.33	\$340.07	\$321.60	\$310.03	\$182.97

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL

COMPARISON OF CARS SWITCHED AND SWITCHING REVENUES

	December 2017	December 2016	YEAR ENDED DECEMBER 31,	
			December 31, 2017	December 31, 2016
SWITCHING REVENUES				
LINE HAULS--INTERMODAL	\$792,840	\$1,139,707	\$10,543,023	\$12,717,977
LINE HAULS--COMMERCIAL	1,137,010	1,004,350	12,875,290	12,643,110
LINE HAULS--CAPITAL DIVISION	25,042	15,040	286,309	322,527
MISCELLANEOUS SWITCHES	<u>264,463</u>	<u>154,917</u>	<u>2,944,251</u>	<u>1,734,039</u>
TOTAL SWITCHING REVENUES	<u>\$2,219,355</u>	<u>\$2,314,014</u>	<u>\$26,648,873</u>	<u>\$27,417,653</u>
 SWITCHING ACTIVITIES (CARS)				
LINE HAULS--INTERMODAL	4,716	7,017	61,300	76,714
LINE HAULS--COMMERCIAL	2,204	2,218	27,762	29,583
LINE HAULS--CAPITAL DIVISION	60	36	686	762
MISCELLANEOUS SWITCHES	<u>2,060</u>	<u>406</u>	<u>17,382</u>	<u>3,863</u>
TOTAL CARS SWITCHED	<u>9,040</u>	<u>9,677</u>	<u>107,130</u>	<u>110,922</u>

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL

FUNDS AVAILABLE FOR DEBT SERVICE

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>
Total Income	\$ 31,175,358	\$ 32,260,821	\$ 30,248,665	\$ 30,482,258	\$ 27,923,473
Less: Operating Exp ...	<u>27,884,797</u>	<u>27,135,385</u>	<u>24,585,303</u>	<u>25,493,409</u>	<u>22,785,550</u>
Income Available for Debt Service	<u>\$ 3,290,561</u>	<u>\$ 5,125,436</u>	<u>\$ 5,663,362</u>	<u>\$ 4,988,849</u>	<u>\$ 5,137,923</u>
Bond Redemption	\$ -	\$ 248,525	\$ 235,569	\$ 223,288	\$ 211,648
Bond Interest	-	11,891	24,847	37,127	48,768
Debt Service Payable ..	<u>\$ -</u>	<u>\$ 260,416</u>	<u>\$ 260,416</u>	<u>\$ 260,415</u>	<u>\$ 260,416</u>
Time Debt Service Covered	-	19.68	21.75	19.16	19.73

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA RAIL

TAXES AND EMPLOYEE WELFARE CONTRIBUTIONS
FOR THE YEAR 2017

FEDERAL

Railroad Retirement	\$2,140,844	
Railroad Unemployment Insurance	45,630	
Total		\$2,186,474

STATE OF WASHINGTON

Retail Sales & Use Tax	395,189	
Utility and Business Occupation Tax	432,081	
Total		827,270

CITY OF TACOMA

Gross Earnings Tax		<u>2,548,959</u>
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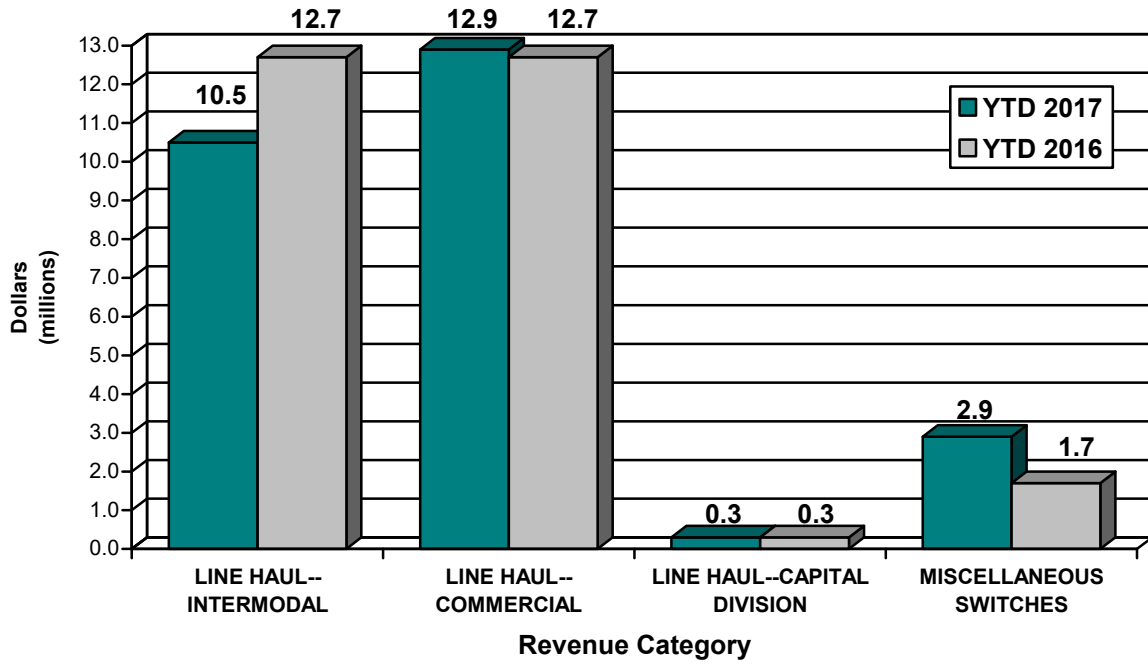
TOTAL TAXES		<u><u>\$5,562,703</u></u>
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Taxes as a % of Total Operating Revenues of \$30,716,881	18.11%
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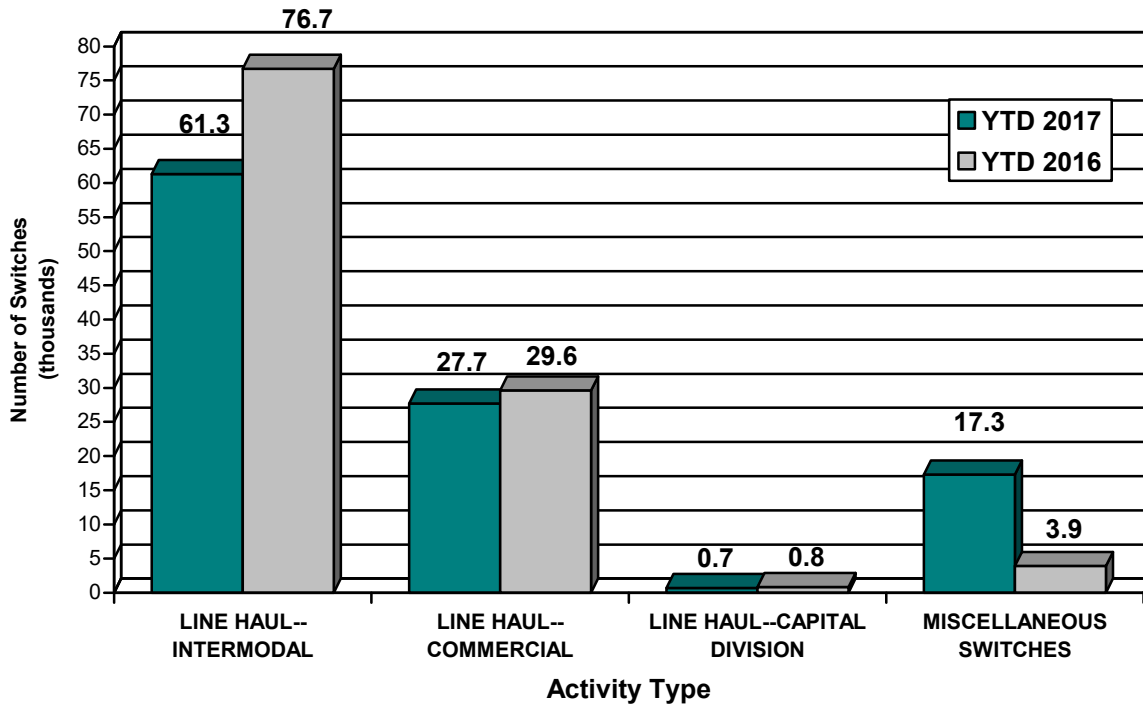
EMPLOYEE WELFARE CONTRIBUTIONS

Pierce County Medical Bureau	\$1,946,720	
Washington Dental Service	171,899	
Other Contributions	433,521	
TOTAL EMPLOYEE WELFARE CONTRIBUTIONS		<u><u>\$2,552,140</u></u>

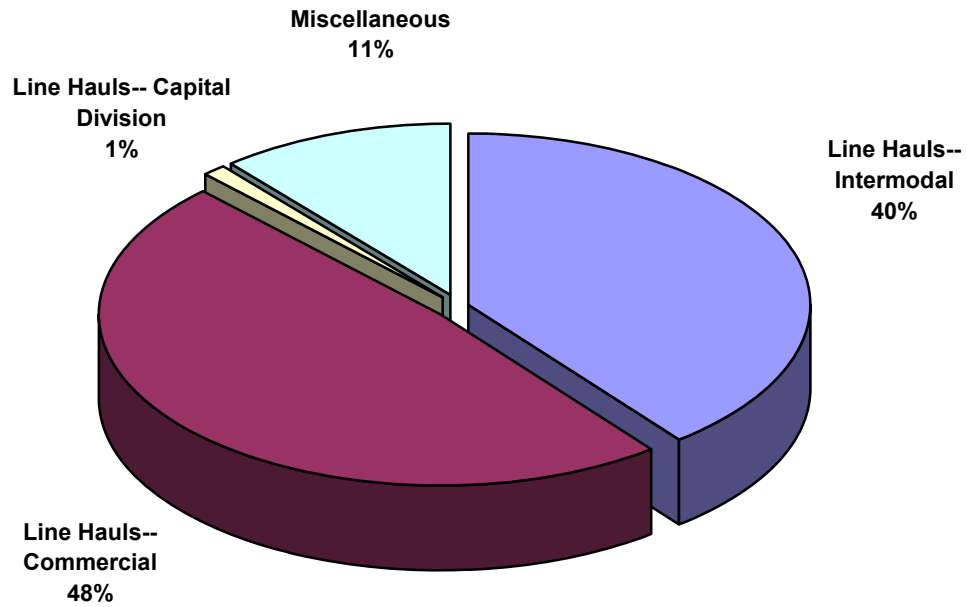
SWITCHING REVENUES
Year to Date - December 2017 & 2016



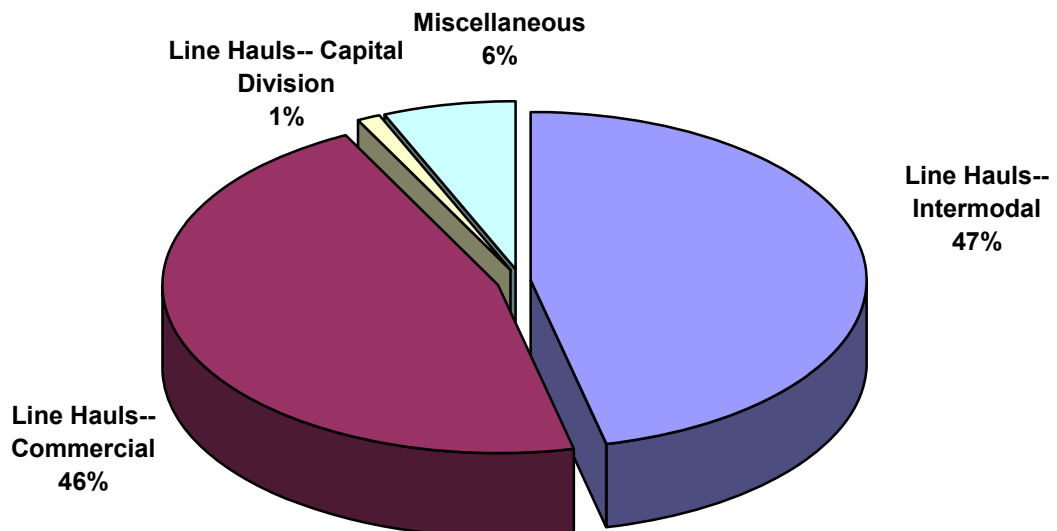
SWITCHING ACTIVITIES
Year to Date - December 2017 & 2016



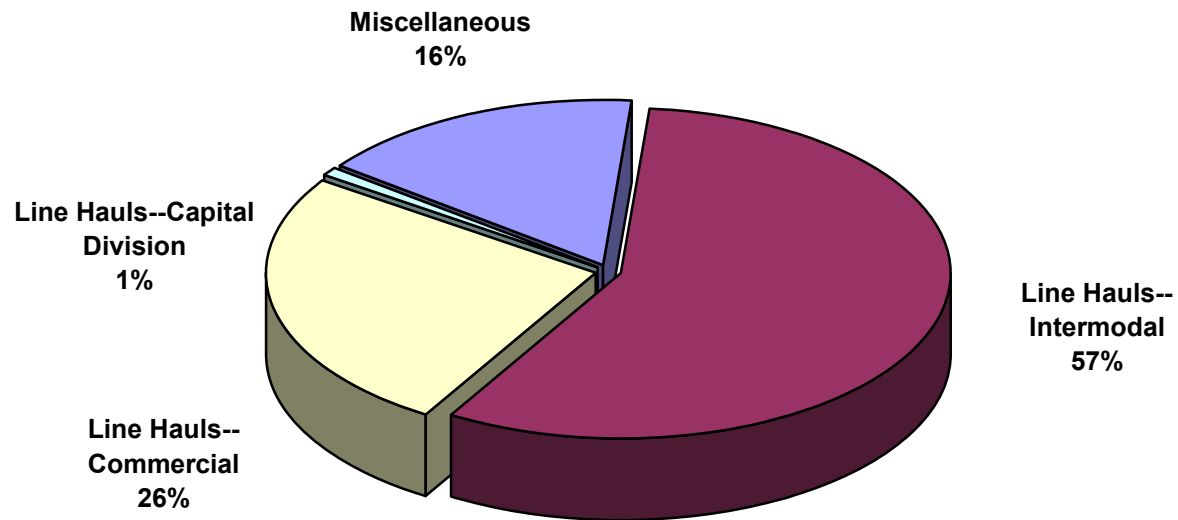
SWITCHING REVENUES
Year to Date - December 2017 (\$26,648,873)



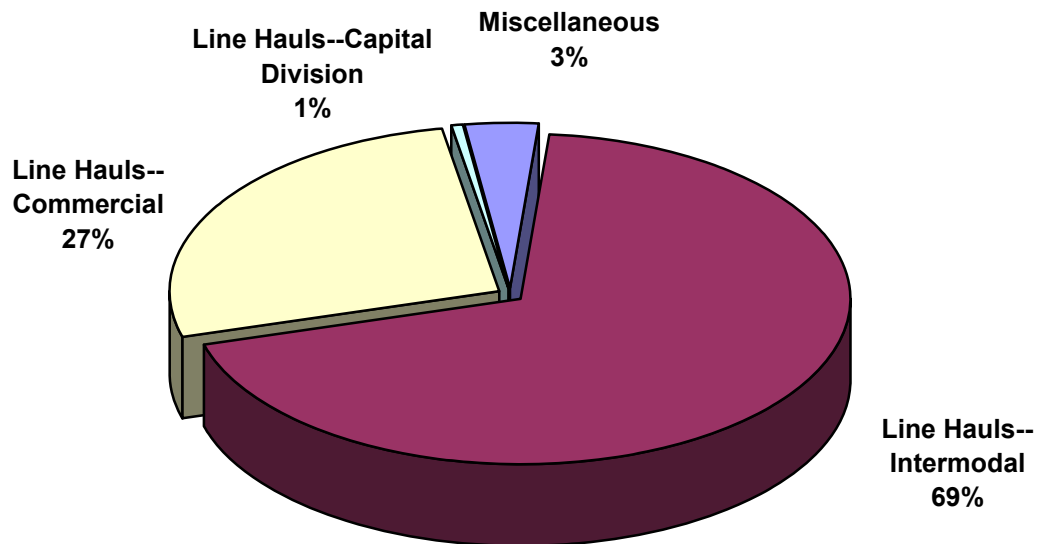
SWITCHING REVENUES
Year to Date - December 2016 (\$27,417,653)



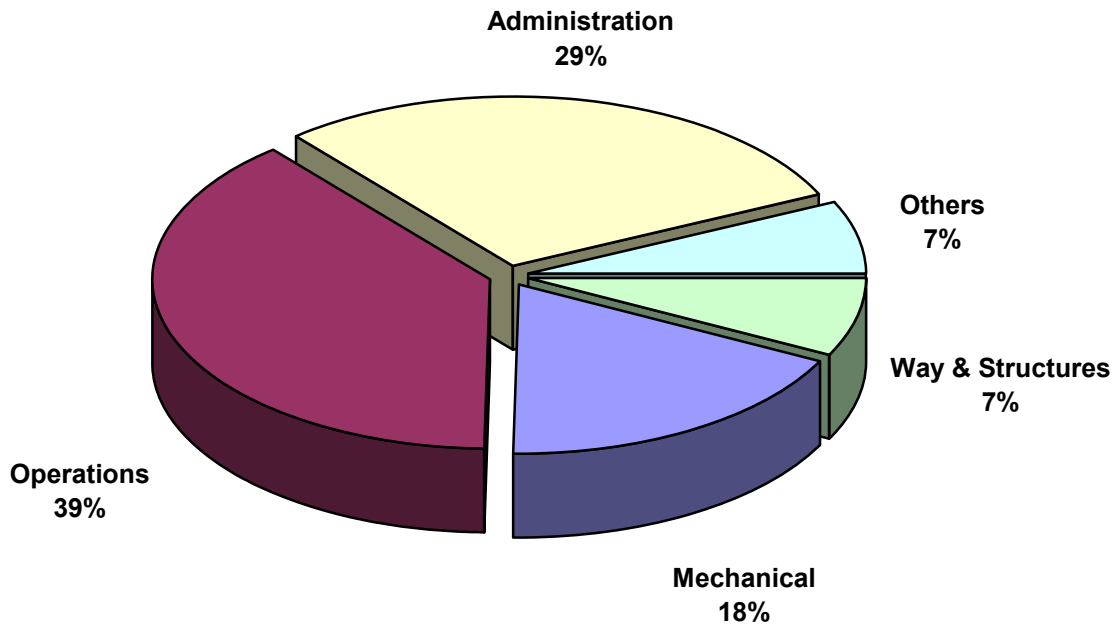
SWITCHING ACTIVITY
Year to Date - December 2017 (107,130 cars)



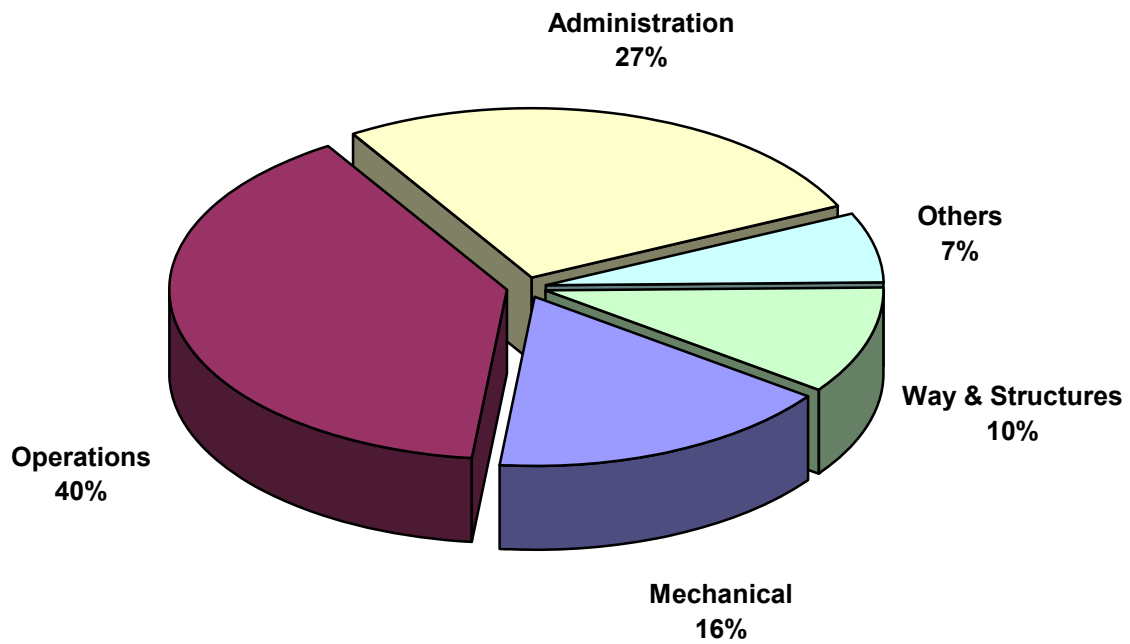
SWITCHING ACTIVITY
Year to Date - December 2016 (110,922 cars)



TOTAL OPERATING EXPENSES
Year to Date - December 2017 (\$29,529,170)



TOTAL OPERATING EXPENSES
Year to Date - December 2016 (\$28,608,340)



2017 SUPERINTENDENT'S REPORT TACOMA RAIL

Tacoma Rail continued to meet its primary goal of providing efficient, cost-effective rail service to the Port of Tacoma and Tacoma's industrial areas (Tidelands Division), to Lakeview (Capital Division) and to Frederickson (Mountain Division) in 2017.

TIDELANDS DIVISION

Line haul count was down by almost 40,000 units in 2017 over 2016. The traffic mix of fewer intermodal platforms and a small increase in commercial railcars led to a corresponding decrease in line haul revenue of approximately \$1.8 million. The Northwest Seaport Alliance (NWSA) saw a one percent increase in their international intermodal container business, however, ocean shipping lines consolidated their routes and realigned their vessel-sharing agreements. This new shipping alliance started calling the Port of Seattle in May of 2017. This caused Tacoma Rail's intermodal total volumes to decrease by 21% relative to the previous year. In November of 2017, Tacoma Rail reached a new agreement with the Union Pacific to assemble 10,000 foot intermodal trains on a daily basis. This was the first time in Tacoma Rail's history of building a train of this size. The new service successfully ran through the final two months of the year.

Unit trains were up versus the prior year, otherwise the commercial business was flat with an overall increase of 2% in 2017. New Washington State environmental rules mandating the development of oil spill contingency plans continued to increase the expenses involved in handling unit trains and into the foreseeable future.

	2017	2016	2015	2014	2013	2012
Intermodal platforms	171,443	214,156	187,827	184,451	179,673	162,297
Unit train railcars	21,641	17,410	13,800	13,838	8,759	
All others	27,519	30,844	31,142	32,509	30,904	31,454
Total line hauls	220,603	262,410	232,769	230,798	219,336	193,751

CAPITAL DIVISION

From 773 carloads in 2016, total traffic on the Capital Division declined 9% to 705 carloads. The Capital Division provides service to customers in South Tacoma and Lakewood through our freight franchise on the rail line owned by Sound Transit. Future expenses will increase on the Capital Division as Positive Train Control (PTC) becomes functional.

MOUNTAIN DIVISION

Tacoma Rail operates the Mountain Division for the City of Tacoma. Carloads handled grew from 1,368 in 2016 to 1,482 in 2017. The increase was led by Hardie Building Products and Pacific Steel & Recycling. Each of these customers had more than 35% growth in line haul traffic. Future expenses will also increase on the Mountain Division as PTC becomes functional. A new tariff was issued in 2017 to mitigate the expense and change the Mountain Division's relationship with the BNSF from a Handling Carrier to a Switching Carrier starting in 2018.

Dale W. King
Superintendent/COO



The City of Tacoma does not discriminate on the basis of disability in any of its programs, activities, or services. To request this information in an alternative format or to request a reasonable accommodation, please contact the City Clerk's Office at (253) 591-5505. TTY or speech to speech users please dial 711 to connect to Washington Relay Services.