

In the opinion of Bond Counsel, under existing federal law and assuming compliance with applicable requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issue date of the Bonds, interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals. However, while interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by corporations is taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by certain S corporations may be subject to tax, and interest on the Bonds received by foreign corporations with United States branches may be subject to a foreign branch profits tax. Receipt of interest on the Bonds may have other federal tax consequences for certain taxpayers. See "TAX MATTERS."

\$64,795,000
CITY OF TACOMA, WASHINGTON
Regional Water Supply System Revenue Refunding Bonds, 2013

DATED: Date of Delivery

DUE: December 1, as shown on the inside cover

The City of Tacoma, Washington (the "City"), Regional Water Supply System Revenue Refunding Bonds, 2013 (the "Bonds"), will be issued only as fully registered bonds under a book-entry system, initially registered in the name of Cede & Co., as nominee for The Depository Trust Company ("DTC"), New York, New York, which will act as securities depository for the Bonds. Individual purchases of the Bonds may be made in denominations of \$5,000 or any integral multiple thereof within a single maturity. Purchasers of the Bonds will not receive certificates representing their interest in the Bonds.

Both principal of and interest on the Bonds shall be payable in lawful money of the United States of America. Interest on the Bonds, payable each June 1 and December 1, commencing December 1, 2013, and principal of the Bonds are payable by the Bond Registrar (currently The Bank of New York Mellon, New York, New York) to DTC, which is obligated to remit such principal and interest to its broker-dealer Participants for subsequent disbursement to beneficial owners of the Bonds. See Appendix C—"BOOK-ENTRY SYSTEM."

Maturity Dates, Principal Amounts, Interest Rates, Yields and CUSIP Numbers on Inside Cover

The Bonds are subject to redemption by the City prior to their stated maturities as described herein under "DESCRIPTION OF THE BONDS—Optional Redemption."

The Bonds are being issued to refund all of the outstanding Regional Water Supply System Revenue Bonds, 2002, and to pay costs of issuance. See "THE SECOND SUPPLY PROJECT" and "PURPOSE AND APPLICATION OF BOND PROCEEDS."

The Bonds are payable solely from a special fund of the City known as the Regional Water Supply System Bond Fund, into which the City has pledged to pay out of the Revenue Fund (subject to prior payment of Operating Expenses) certain fixed amounts sufficient to pay the principal of and interest on the outstanding \$75,925,000 principal amount of Regional Water Supply System Revenue Bonds, 2002, all of which will be refunded with the Bonds, the \$3,595,000 principal amount of Regional Water Supply System Revenue Bonds, 2010A, the \$44,245,000 principal amount of Regional Water Supply System Revenue Bonds, 2010B (Taxable Build America Bonds – Direct Payment), the Bonds and any Future Parity Bonds. The Revenues of the Regional System include amounts due to the City under the Second Supply Project Agreement from the Participants, including the City's Water System. If another Participant defaults, Tacoma Water is obligated to increase its Participant Share, including paying debt service on the Bonds. The City expects to issue \$78,940,000* of Water System Revenue and Refunding Bonds, 2013 on or about May 7, 2013. The Bonds are not general obligations of the City, and neither the full faith and credit nor the taxing power of the City or of the State of Washington, nor any revenues of the City derived from sources other than the Regional Water Supply System, are pledged to the payment thereof. See "SECURITY FOR THE BONDS."

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

The Bonds are offered for delivery when, as, and if issued, subject to the approval of legality by Foster Pepper PLLC, Bond Counsel, Seattle, Washington. It is expected that the Bonds will be available for delivery at the facilities of The Depository Trust Company in New York, New York, by Fast Automated Securities Transfer (FAST) on or about April 16, 2013.

MATURITY SCHEDULES, INTEREST RATES, YIELDS AND CUSIP NUMBERS

\$64,795,000

REGIONAL WATER SUPPLY SYSTEM REVENUE REFUNDING BONDS, 2013

Due December 1	Amount	Interest Rate	Yield	CUSIP No. *
2013	\$ 960,000	5.00%	0.25%	87354TBH7
2014	1,070,000	5.00	0.38	87354TBJ3
2015	1,185,000	5.00	0.55	87354TBK0
2016	670,000	5.00	0.73	87354TBL8
2017	745,000	5.00	0.95	87354TBM6
2018	765,000	5.00	1.19	87354TBN4
2019	1,690,000	5.00	1.43	87354TBP9
2020	1,790,000	5.00	1.70	87354TBQ7
2021	1,890,000	5.00	1.90	87354TBR5
2022	1,985,000	5.00	2.11	87354TBS3
2023	2,110,000	5.00	2.25 **	87354TBT1
2024	4,575,000	5.00	2.36 **	87354TBU8
2025	4,820,000	5.00	2.48 **	87354TBV6
2026	5,035,000	5.00	2.59 **	87354TBW4
2027	5,300,000	5.00	2.69 **	87354TBX2
2028	5,560,000	5.00	2.78 **	87354TBY0
2029	5,875,000	5.00	2.84 **	87354TBZ7
2030	6,155,000	4.00	3.25 **	87354TCA1
2031	6,425,000	4.00	3.30 **	87354TCB9
2032	6,190,000	4.00	3.35 **	87354TCC7

* Copyright © 2013 CUSIP Global Services. The CUSIP numbers are included for convenience of the holders and potential holders of the Bonds. CUSIP is a registered trademark of the American Bankers Association. CUSIP Global Services (CGS) is managed on behalf of the American Bankers Association by Standard & Poor's. No assurance can be given that the CUSIP numbers for the Bonds will remain the same after the date of issuance and delivery of the Bonds.

** Priced to the June 1, 2023 par call date.

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

The information set forth herein has been obtained from sources that are believed to be current and reliable. The City, however, makes no representation regarding the accuracy or completeness of the information in Appendix C—“BOOK-ENTRY SYSTEM,” which has been obtained from DTC’s website. Estimates and opinions should not be interpreted as statements of fact. Summaries of documents do not purport to be complete statements of their provisions and such summaries are qualified by references to the entire contents of the summarized documents. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made by use of this Official Statement shall, under any circumstances, create any implication that there has been no change in the affairs of the City since the date hereof.

In connection with the offering of the Bonds, the purchaser may over allot or effect transactions which stabilize or maintain the market price of the Bonds at levels above those which might otherwise prevail in the open market. Such stabilizing, if commenced, may be discontinued or recommenced at any time.

The presentation of certain information, including tables of receipts from revenues, is intended to show recent historic information and is not intended to indicate future or continuing trends in the financial position or other affairs of the City or Tacoma Water. No representation is made that past experience, as it might be shown by such financial and other information, will necessarily continue to be repeated in the future.

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

This Official Statement contains forecasts, projections and estimates that are based upon expectations and assumptions that existed at the time such forecasts, projections and estimates were prepared. In light of the important factors that may materially affect economic conditions in the City, the inclusion in this Official Statement of such forecasts, projections and estimates should not be regarded as a representation by the City that such forecasts, projections and estimates will occur. Such forecasts, projections and estimates are not intended as representations of fact or as guarantees of results.

If and when included in this Official Statement, the words “plan,” “expect,” “forecast,” “estimate,” “budget,” “project,” “intends,” “anticipates” and similar words are intended to identify forward-looking statements, and any such statements inherently are subject to a variety of risks and uncertainties that could cause actual results to differ materially from those projected. These forward-looking statements speak only as of the date they were prepared.

The Bonds will not be registered under the Securities Act of 1933, as amended, in reliance upon an exception contained in such act.

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OFFICIAL STATEMENT

\$64,795,000

CITY OF TACOMA, WASHINGTON

Regional Water Supply System Revenue Refunding Bonds, 2013

INTRODUCTION

The City of Tacoma, Washington (the “City” or “Tacoma”), furnishes this Official Statement in connection with the offering of \$64,795,000 principal amount of its Regional Water Supply System Revenue Refunding Bonds, 2013 (the “Bonds”). This Official Statement, which includes the cover page, inside cover page and appendices, provides information concerning the City, the Bonds, the Regional Water Supply System (the “Regional System”), the Second Supply Project and the City’s Water System (the “Water System”). It also includes information concerning the City of Kent (“Kent”), Covington Water District (“Covington”) and Lakehaven Utility District (“Lakehaven”), all municipal corporations of the State of Washington (the “State”) and participants, together with the City’s Water System (collectively, the “Participants”), in the Second Supply Project pursuant to the Agreement for the Second Supply Project (the “Second Supply Project Agreement”) entered into by and among the Participants effective December 19, 2002, and the Repayment Agreement dated December 19, 2002, as amended, relating to the Bonds (the “Repayment Agreement”) entered into by and among the Participants. See “THE SECOND SUPPLY PROJECT.”

The City is a municipal corporation under the constitution and laws of the State. The Water Division, doing business as Tacoma Water (“Tacoma Water”), of the City’s Department of Public Utilities (the “Department”) operates the Water System and the Regional System. The Regional System is a separate utility system of the City. Tacoma Water is one of the largest publicly owned water utilities in the Pacific Northwest and had 96,333 customers in 2012. See “THE CITY OF TACOMA WATER SYSTEM.”

The Bonds are being issued pursuant to Ordinance No. 28137, passed by the City Council on March 19, 2013 (the “Bond Ordinance”), and under the authority of chapters 35.41, 39.46 and 39.53 of the Revised Code of Washington (“RCW”). Certain provisions of the Bond Ordinance are summarized in Appendix A.

The Regional System currently consists of the Second Supply Project, a water pipeline and delivery project described more fully in “THE SECOND SUPPLY PROJECT.” Tacoma, Kent, Covington and Lakehaven participate in the Second Supply Project under the terms of the Second Supply Project Agreement, which defines their rights and obligations with regard to the Second Supply Project. Tacoma has a 15/36 Participant Share and each of Kent, Covington and Lakehaven has a 7/36 Participant Share in the Second Supply Project. Generally, a Participant Share represents a Participant’s proportional right to receive and obligation to pay for water delivered by the Second Supply Project. If another Participant defaults, Tacoma Water is obligated to increase its Participant Share, including paying debt service on the Bonds.

The Bonds are being issued to refund certain outstanding bonds and to pay the costs of issuance of the Bonds, as more fully described under “PURPOSE AND APPLICATION OF BOND PROCEEDS.”

The Regional System has outstanding \$75,925,000 principal amount of Regional Water Supply System Revenue Bonds, 2002 (the “2002 Bonds”), all of which will be refunded with proceeds of the Bonds, \$3,595,000 principal amount of Regional Water Supply System Revenue Bonds, 2010A (the “2010A Bonds”) and \$44,245,000 principal amount of Regional Water Supply System Revenue Bonds, 2010B (Taxable Build America Bonds – Direct Payment) (the “2010B Bonds,” and together with the 2010A Bonds, the “2010 Bonds,” and collectively with the 2002 Bonds, the “Outstanding Parity Bonds”). The Bonds will be issued on parity with the Outstanding Parity

Bonds. The Bonds, the Outstanding Parity Bonds and any additional bonds issued on a parity of lien with the Bonds (“Future Parity Bonds”) are referred to collectively as the “Parity Bonds.”

Federal sequestration, which became effective on March 1, 2013, is expected to reduce Tacoma Water’s Federal subsidy for a portion of the interest on the 2010B Bonds and on the City’s 2009 Water System Bonds and 2010B Water System Bonds (hereinafter defined). There also could be indirect impacts to the economy of the area. The exact impact will depend on how various Federal agencies respond to mandated expenditure reductions and the duration of sequestration.

The Parity Bonds are special limited obligations of the City payable from and secured by Revenues of the Regional System, subject to the prior payment of Operating Expenses of the Regional System. Revenues of the Regional System include payments made by the Participants under the Project Agreement and the Repayment Agreement (“Participants’ Payments”), which are required to be deposited in the Revenue Fund. In addition, pursuant to the Bond Ordinance, certain funds and accounts, including the Debt Service Account, the Reserve Account and any Construction Account, are pledged to secure the payment of the principal of and interest on the Parity Bonds. See “SECURITY FOR THE BONDS.”

The City has covenanted to establish, maintain and collect rates and charges for water and other goods and services sold or supplied through the facilities of its Water System sufficient to pay the cost of operation and maintenance of the Water System and to provide Gross Revenues of the Water System sufficient, together with amounts on deposit in the Revenue Fund and available for such purpose (including Participants’ Payments), to pay all Regional Supply System Costs and all obligations against Gross Revenues of the Water System now or hereafter imposed by law or contract including principal of and interest on the Parity Bonds. In the ordinances authorizing the outstanding Tacoma Water System bonds, Tacoma Water has covenanted to collect Net Revenues of the Water System at least equal to 1.25 times annual debt service on the Water System parity bonds.

The Second Supply Project Agreement allows each Participant to pay all or part of its Participant Share of the Second Supply Project capital costs either in cash or over time. Lakehaven chose to pay its entire share of the capital cost of the Second Supply Project and Phase I of the Filtration Treatment Project in cash, and therefore did not participate in the issuance of the Outstanding Parity Bonds. The remaining three Participants chose to have the City issue the Outstanding Parity Bonds to finance their Participant Shares. Consequently, Tacoma Water, Covington and Kent’s water utilities are obligated to pay amounts sufficient to provide for the payment of the principal of and interest on the Bonds.

Under the Second Supply Project Agreement and the Repayment Agreement, Tacoma Water is responsible for payment of approximately 55% of the debt service on the 2002 Bonds, Kent is responsible for approximately 23% and Covington is responsible for approximately 22%. Since the Bonds refund the 2002 Bonds, Tacoma Water, Kent and Covington are each responsible for the same percentage of the debt service on the Bonds as they were for the 2002 Bonds. Kent and Covington will pay their share to the City, which will pay the Bond Registrar. If another Participant defaults, Tacoma Water is obligated to increase its Participant Share, including paying debt service on the Bonds. Those percentage shares are subject to change with the addition of a new participant, the payment default of a Participant, the issuance of Future Parity Bonds or the optional prepayment by an obligated Participant.

The payments by Tacoma Water, Kent and Covington constitute “Contract Resource Obligations” payable as operation and maintenance expenses from the gross revenues of their respective water utilities payable ahead of debt service on those Participant’s bonds. The Repayment Agreement governs debt service payments on the Bonds and does not otherwise affect each Participant’s rights and obligations under the Second Supply Project Agreement, and the Repayment Agreement takes precedence over the debt repayment provisions of the Second Supply Project Agreement. See “SECURITY FOR THE BONDS— Payment Obligations of the Participants.”

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

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

DESCRIPTION OF THE BONDS

General

The Bonds will be dated the date of their initial delivery and will be issued in the aggregate principal amount of \$64,795,000. The Bonds will bear interest at the rates and mature on the dates set forth on the inside cover page of this Official Statement. Interest on the Bonds shall be calculated on the basis of a 360-day year consisting of twelve 30-day months, and shall be payable each June 1 and December 1, commencing December 1, 2013.

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

Optional Redemption

The Bonds maturing in years 2013 through 2022, inclusive, are not subject to redemption prior to maturity. The Bonds maturing on and after December 1, 2023, are subject to redemption at the option of the City on and after June 1, 2023, in whole or in part at any time within one or more maturities selected by the City at a price of par plus accrued interest, if any, to the date of redemption.

Partial Redemption

If less than all of the Bonds of any maturity are to be redeemed, the Bonds or portions thereof to be redeemed are to be selected by the Bond Registrar or DTC, as applicable, by lot, or in accordance with their respective standard procedures. The Bond Ordinance provides that the portion of any Bonds of a denomination of more than \$5,000 to be redeemed will be in the principal amount of \$5,000 or any integral multiple thereof and that in selecting portions of such Bonds for redemption, the Bond Registrar will treat each such Bond as representing that number of such Bonds of \$5,000 denomination that is obtained by dividing the principal amount of such Bonds to be redeemed in part by \$5,000.

Notice of Redemption

Notice of any such redemption will be given by the Bond Registrar on behalf of the City by first-class mail at least 20 days and not more than 60 days prior to the date fixed for redemption to the Registered Owner of the Bonds to be redeemed at the address shown on the Bond Register. The notice requirements will be deemed to be complied with when notice is mailed as provided in the Bond Ordinance, whether or not notice is actually received by the owner of any Bond. Notwithstanding the foregoing, if the Bonds are held in book-entry only form, notice of redemption will be given in accordance with the operational arrangements in effect at DTC. Interest on the Bonds called for redemption will cease to accrue on the redemption date unless the Bond or Bonds so called are not paid in full upon presentation made pursuant to the call.

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

Purchase

The City has reserved the right at any time to purchase any of the Bonds at any price from amounts in the Revenue Fund available for such purchase.

Book-Entry System

When issued, the Bonds will be registered in the name of Cede & Co. (or such other name as may be requested by an authorized representative of DTC), as nominee of DTC. DTC will act as securities depository for the Bonds. Individual purchases will be made in book-entry form only through DTC, and purchasers will not receive physical certificates representing their interests in the Bonds purchased. For information about DTC and its book-entry system, see Appendix C—"BOOK-ENTRY SYSTEM."

Procedure in the Event of Discontinuation of Book-Entry Transfer System

If the City is unable to retain a qualified successor to DTC or the City determines that the beneficial owners should be able to obtain Bond certificates, the City shall execute, authenticate and deliver Bonds in fully registered form, in the denomination of \$5,000 or any integral multiple thereof within a single maturity. Thereafter, the principal of the Bonds shall be payable at maturity or prior redemption upon presentation and surrender thereof at the principal office of the Bond Registrar, currently The Bank of New York Mellon; interest on the Bonds will be payable by check or draft mailed (except that interest may be paid by wire transfer if requested in writing by owners owning at least \$1,000,000 par value of the Bonds) on the date interest is due to the persons in whose names such Bonds are registered, at the address appearing upon the registration books on the 15th day of the month preceding an interest payment date (the record date); and the Bonds will be transferable as provided in the Bond Ordinance.

Defeasance of the Bonds

In the event that money and/or Government Obligations, maturing at such time or times and bearing interest to be earned thereon in amounts (together with such money, if necessary) sufficient to redeem and retire part or all of the Bonds in accordance with their terms, are set aside in a special account of the City to effect such redemption and retirement, and such money and the principal of and interest on such obligations are irrevocably set aside and pledged for such purpose, then no further payments need be made into the Bond Fund for the payment of the principal of and interest on the Bonds so provided for, and such Bonds shall cease to be entitled to any lien, benefit or security of the Bond Ordinance except the right to receive the money so set aside and pledged, and such Bonds shall be deemed not to be outstanding.

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

PURPOSE AND APPLICATION OF BOND PROCEEDS

The Bonds are being issued to refund all of the 2002 Bonds and to pay the costs of issuance of the Bonds.

Refunding Plan

The 2002 Bonds to be refunded with the proceeds of the Bonds are identified below (“Refunded Bonds”).

Refunded Bonds						
Bond	Maturity Date	Par Amount	Interest Rate	Redemption Date	Redemption Price	CUSIP Numbers
<i>Regional Water Supply System Revenue Bonds, 2002</i>						
Serials	12/1/2013	\$ 875,000	4.125%	5/16/2013	100%	87354TAJ4
	12/1/2014	925,000	4.125	5/16/2013	100	87354TAK1
	12/1/2015	1,025,000	4.25	5/16/2013	100	87354TAL9
Term Bonds	12/1/2017	2,300,000	5.50	5/16/2013	100	87354TAM7
	12/1/2024	18,750,000	5.00	5/16/2013	100	87354TAN5
	12/1/2028	23,650,000	5.00	5/16/2013	100	87354TAP0
	12/1/2032	28,400,000	5.00	5/16/2013	100	87354TAQ8
Total		\$75,925,000				

A portion of the net proceeds from the sale of the Bonds will be deposited in the Refunding Account (the “Refunding Account”) and used to purchase Acquired Obligations (as defined below) to be held by U.S. Bank National Association, Seattle, Washington (the “Refunding Trustee”) under a refunding trust agreement (the “Refunding Trust Agreement”), dated the date of delivery of the Bonds, between the City and the Refunding Trustee. Funds will be irrevocably deposited in the Refunding Account and will be used to purchase direct, noncallable, obligations of the United States of America (the “Acquired Obligations”). The Acquired Obligations will mature at such times and pay interest in such amounts so that, with other available funds held by the Refunding Trustee under the Refunding Trust Agreement, sufficient money will be available to pay the interest on the Refunded Bonds coming due on and prior to their redemption date and to redeem and retire the Refunded Bonds on the redemption date set forth above. Since all payments of principal of and interest on the Refunded Bonds will thereafter be provided for from money and securities on deposit with the Refunding Trustee under the Refunding Trust Agreement, the liens, pledges and covenants securing the Refunded Bonds will terminate and be discharged and released.

Sources and Uses

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

Sources of Funds	
Par Amount of the Bonds	\$ 64,795,000
Original Issue Premium	10,558,096
Cash Contribution	<u>2,639,025</u>
Total	\$ 77,992,121
Uses of Funds	
Refunding Account	\$ 77,659,477
Issuance Expenses(1)	<u>332,644</u>
Total	\$ 77,992,121

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

SECURITY FOR THE BONDS

Revenue Obligations of Regional Water Supply System

The City has established a separate utility system known as the “Regional Water Supply System” (the “Regional System”) to construct and operate the Second Supply Project and has transferred facilities of the Second Supply Project from the Water System to the Regional System. See “THE SECOND SUPPLY PROJECT.” The Bonds, the

Outstanding Parity Bonds and any Future Parity Bonds are special limited obligations of the City payable from and secured by Revenues of the Regional System, subject to the prior payment of Operating Expenses. Revenues of the Regional System means the income, revenues, receipts and loan proceeds derived by the City through the ownership and operation of the Regional System, including Participants' Payments under the Second Supply Project Agreement. In addition, all money and investments in the Bond Fund (including the Debt Service Account and the Reserve Account) and any Construction Account (except for any Rebate Amount), together with the earnings thereon, are pledged to secure the payment of the principal of and interest on the Parity Bonds. Except as specifically provided in the Bond Ordinance, Revenues of the Regional System shall not include any income derived by the City through the ownership and operation of the Water System or any other separate utility system of the City. The terms "Operating Expenses" and "Participants' Payments" are defined in Appendix A—"SUMMARY OF THE BOND ORDINANCE—Definitions."

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

The Bonds are being issued on a parity of lien with the \$123,765,000 Outstanding Parity Bonds, of which \$75,925,000 will be refunded with proceeds of the Bonds. The City has obligated itself to set aside and pay into the Bond Fund certain fixed amounts out of the Revenue Fund, subject to prior payment of Operating Expenses, sufficient to pay the principal of, premium, if any, and interest on the Bonds, the Outstanding Parity Bonds and any Future Parity Bonds.

State law provides that the owner of a bond, such as the Bonds, the payment of which is pledged from a special fund, such as the Bond Fund, has a claim only against that fund and proportionate amounts of revenue pledged to that fund. Under State law, any bondowner may bring an action to compel a city to set aside and pay into the special fund the amount which a city is obligated to set aside and pay therein.

Payment Obligations of the Participants

Tacoma Water, Kent, Covington and Lakehaven have entered into the Second Supply Project Agreement to permit, design, finance, construct, operate and maintain the Second Supply Project and to receive delivery of water from the Second Supply Project ("Project Water"). In 2002, the Participants entered into the Second Supply Project Agreement, and a Repayment Agreement setting forth the terms under which Tacoma Water, Kent and Covington will pay to the City their proportionate shares of the amount necessary to pay the principal of and interest on the 2002 Bonds. In 2010, the Participants executed a Filtration Treatment Financing Plan and a Repayment Agreement setting forth the terms under which Tacoma Water, Kent and Covington will pay to the City their proportionate shares of the amount necessary to pay the principal of and interest on the 2010 Bonds. See "THE SECOND SUPPLY PROJECT—Project Participants." The Bonds are being issued to refund the 2002 Bonds, which were issued to finance a portion of the Second Supply Project.

Under the Second Supply Project Agreement and the 2002 Repayment Agreement, the City is responsible for payment of approximately 55% of the debt service on the Bonds, Kent is responsible for paying approximately 23% of the debt service on the Bonds and Covington is responsible for paying approximately 22% of the debt service on the Bonds. See "THE SECOND SUPPLY PROJECT." The Second Supply Project Agreement permits Participants to elect to pay cash obtained from the issuance of their own bonds, from the proceeds of loans from private or public sources, or by any other lawful means for their Participant Share of a Project Cost to be otherwise financed with the proceeds of bonds of the Regional System. Lakehaven elected to separately pay for its Participant Share of the costs of financing the Second Supply Project and Phase I of the Filtration Treatment Project. Consequently, Lakehaven has no obligation to make debt service payments on the Bonds or any Outstanding Parity Bonds. In addition, the Participants are obligated to pay their Participants' Share of other costs of the Project in the following shares: Tacoma, 15/36; Kent, 7/36; Covington, 7/36; and Lakehaven, 7/36.

In the Second Supply Project Agreement, each Participant has covenanted to establish, maintain and collect rates or charges for water and other services supplied by it which shall be adequate to provide revenues sufficient to enable each Participant to make the payments required to be made pursuant to the Second Supply Project Agreement, and to pay all other charges and obligations payable from or constituting a charge or lien upon such Participant's water

utility revenues. Each Participant is obligated to make the payments required under the Second Supply Project Agreement whether or not the Second Supply Project is completed, operable or operating and notwithstanding the suspension, interruption, interference, reduction or curtailment in the operation of the Second Supply Project for any reason, in whole or in part.

Under the Second Supply Project Agreement, the Participant Share of a Participant that has been in default for a period of 60 days or more on a payment obligation under the Second Supply Project Agreement (if that payment obligation includes amounts necessary for the City to make payment on any Outstanding Parity Bonds or the Bonds) will be offered for assignment to the non-defaulting Participants. Any non-defaulting Participant may accept all or any portion of the defaulting Participant's Participant Share and, upon that acceptance, will be obligated to cure a proportionate share of any existing payment default and will be responsible for paying all obligations associated with the increased Participant Share then assigned to it. In the event that other non-defaulting Participants decline any or all of the defaulting Participant's Participant Share, Tacoma Water will automatically increase its Participant Share in an amount equal to the defaulting Participant's Participant Share then remaining unassigned and will be responsible for the amount in default.

A Participant's share of debt service on Parity Bonds and a Participant's Participant Share of the Project are each subject to further change upon the occurrence of certain subsequent events. First, a Participant is entitled under the Second Supply Project Agreement to sell, assign or transfer in whole or in part its rights and obligations under the Second Supply Project Agreement with the prior written consent of all other Participants. Any new Participant must have a rating in one of the three highest categories by one Rating Agency. The City has covenanted in the Bond Ordinance that it will not amend the Second Supply Project Agreement in any manner that would increase or reduce a Participant's obligations to pay its share of debt service on Parity Bonds, except that it may allow for a new Participant or for an existing Participant (other than the City) to assign its interests in the Second Supply Project Agreement upon satisfaction of certain specified conditions. Such a sale or assignment could affect both an existing Participant's share of debt service on the Parity Bonds and its Participant's Participant Share and would, as well, add a new Participant to the Project. Second, as described above, the Participant Share of a Participant that has been in default for a period of 60 days or more on any debt service payment obligation is offered for assignment to the non-defaulting Participants. If other non-defaulting Participants decline any or all of the defaulting Participant's Participant Share, Tacoma Water's Participant Share will increase in an amount equal to the defaulting Participant's Participant Share then remaining unassigned. Third, since any Participant may make an election to pay cash in lieu of participating in the issuance of Future Parity Bonds, the percentage shares of debt service on all Parity Bonds (including the Bonds) allocable to a Participant may change. Fourth, Participants are permitted under the Repayment Agreement to prepay all or any portion of their shares of debt service if the Bonds are then subject to optional redemption. In that event, the percentage shares of future debt service for any Participant making an optional prepayment used to redeem Parity Bonds would be reduced, and for other Participants would be increased, as to the Parity Bonds remaining outstanding after that optional redemption.

The occurrence of an Uncontrollable Force (as defined in the Second Supply Project Agreement) will not relieve any Participant of its obligation to pay money when due. The Second Supply Project Agreement requires disputed invoices to be paid in full and provides a procedure for resolving invoice disputes and reconciling disputed payments.

For a description of Tacoma Water, see the information under the heading "THE CITY OF TACOMA WATER SYSTEM." For a description of the other Participants, see Appendix B—"PARTICIPANTS IN THE SECOND SUPPLY PROJECT."

City of Tacoma. The City has declared that its obligation to pay its share of costs of the Second Supply Project is a "Contract Resource Obligation" of its Water System. In its Water Bond Authorizing Ordinances described below, the City reserved the right to enter into contracts or other obligations for the acquisition, from facilities to be constructed, of water supply, transmission, treatment or other commodity or service relating to the Water System. Upon compliance with certain requirements of the Water Bond Authorizing Ordinances, the City may determine that such contract or obligation is a Contract Resource Obligation of its Water System and may provide that all payments under that Contract Resource Obligation (including payments prior to the time that water supply, transmission, treatment or other commodity or service is being provided, or during a suspension or after termination of supply or service) shall be operating expenses of the Water System. In the ordinance authorizing the issuance of the 2002 Bonds, the City determined that the obligations of the City under the Second Supply Project Agreement are a

Contract Resource Obligation of its Water System and that all payments to be made to the City under the Second Supply Project Agreement shall be an operating expense of its Water System. In the Bond Ordinance, the City covenants to pay into the Revenue Fund in each month, as an operating expense payable from Gross Revenues of the Water System, an amount which, together with Participants' Payments and other Revenues available for such purpose, is equal to the Regional Supply System Costs which are then unpaid together with the estimated Regional Supply System Costs for the next succeeding month.

City of Kent. The obligation of Kent to make payments of debt service on the Bonds constitutes a "Contract Resource Obligation" payable as an operation and maintenance expense of its water utility. Kent's ordinances authorizing its outstanding water system revenue bonds provide that Kent may incur an obligation, designated as a "Contract Resource Obligation," to make payments for water supply, transmission or other commodity or service relating to its water utility. Kent may provide that all payments under a Contract Resource Obligation (including payments prior to the time that water supply, transmission, treatment or other commodity or service is being provided, or during a suspension or after termination of supply or service) shall be an operation and maintenance expense of Kent's water utility (and therefore enjoy a lien on the gross revenues of the water utility prior to the lien of its outstanding bonds). Kent has determined that the Second Supply Project Agreement is a Contract Resource Obligation of its water utility, which means that all payments to be made by Kent under the Second Supply Project Agreement shall be operating expenses of its water utility. For financial reporting purposes, Kent treats its payments to Tacoma Water as debt and not as operation and maintenance expenses.

Covington Water District. The obligation of Covington to make payments of debt service on the Bonds constitutes a "Contract Resource Obligation." Covington has determined that all payments under this Contract Resource Obligation (including payments prior to the time that water supply or transmission or other commodity or service is being provided, or during a suspension or after termination of supply or service) shall constitute a charge upon gross revenue of its water system and utility local improvement district assessments equal to the charge thereon of operation and maintenance costs, and prior and superior to any other charges whatsoever. For financial reporting purposes, Covington treats its payments to Tacoma Water as debt and not as operation and maintenance expenses.

Separate Utility System

The City has established the Regional System as a separate utility system to construct and operate the Second Supply Project and has transferred facilities of the Second Supply Project from the Water System to the Regional System. See "THE SECOND SUPPLY PROJECT."

Pursuant to the City's ordinances authorizing its outstanding 2003 Water System Bonds, 2005 Water System Bonds, 2009 Water System Bonds, 2010A Water System Bonds, 2010B Water System Bonds and 2013 Water System Bonds (collectively, the "Water Bond Authorizing Ordinances"), the City is authorized to create separate systems for water supply, transmission, treatment or other commodity or service. The revenue of any such separate utility system is not included in the Gross Revenues of the Water System. Instead, the revenue of a separate utility system may be pledged to the payment of revenue obligations issued to purchase, construct, condemn or otherwise acquire or expand that separate system. The City also may pledge, as an operating expense of its Water System, the Gross Revenues of the Water System to the payment of revenue obligations of a separate utility system to the extent such payments qualify as Contract Resource Obligations under the Water Bond Authorizing Ordinances.

The Water System has outstanding \$25,285,000 principal amount of Water System Revenue and Refunding Bonds, 2003 (the "2003 Water System Bonds"), all of which will be refunded with a portion of the 2013 Water System Bonds (defined herein), \$35,485,000 principal amount of Water System Revenue and Refunding Bonds, 2005 (the "2005 Water System Bonds"), \$76,775,000 principal amount of Water System Revenue Bonds, 2009 (Taxable Build America Bonds – Direct Payment) (the "2009 Water System Bonds"), \$28,585,000 principal amount of Water System Revenue Refunding Bonds, 2010A (the "2010A Water System Bonds"), and \$74,985,000 principal amount of Water System Revenue Bonds, 2010B (Taxable Build America Bonds – Direct Payment) (the "2010B Water System Bonds"). The City expects to issue approximately \$78,940,000* aggregate principal amount of Water System Revenue and Refunding Bonds, 2013 (the "2013 Water System Bonds") on or about May 7, 2013.

* Preliminary, subject to change.

Rate Covenants

The City has covenanted in the Bond Ordinance to establish, maintain and collect contract charges or other amounts for water and other goods and services sold or supplied through the facilities of the Regional System that will provide the City with Revenues sufficient for the payment of Regional Supply System Costs. “Regional Supply System Costs” is defined in Appendix A and includes principal of and interest on the Parity Bonds.

The City has further covenanted to establish, maintain and collect rates and charges for water and other goods and services sold or supplied through the facilities of its Water System sufficient to pay the cost of operation and maintenance of the Water System and to provide Gross Revenues of the Water System sufficient, together with amounts on deposit in the Revenue Fund and available for such purpose (including Participants’ Payments), to pay all Regional Supply System Costs and all obligations against Gross Revenues of the Water System now or hereafter imposed by law or contract.

Kent, Covington and Lakehaven have covenanted in the Second Supply Project Agreement to collect water rates and charges sufficient to pay their Participant Shares. See “THE SECOND SUPPLY PROJECT—Second Supply Project Agreement and Repayment Agreement.”

Reserve Account

The City has covenanted in the Bond Ordinance that on the date of delivery of the Bonds it will pay into the Reserve Account out of proceeds of the Bonds or other available funds and/or acquire Qualified Insurance or a Qualified Letter of Credit so that the amount in the Reserve Account at least equals the Reserve Account Requirement. The Reserve Account Requirement for the Bonds is defined in the Bond Ordinance to mean an amount equal to Average Annual Debt Service on the outstanding Bonds calculated on the date of Closing, but in no case shall the amount in the Reserve Account allocable to the Bonds exceed 10% of the proceeds of the Bonds. The Reserve Account will secure the payment of the Bonds, the Outstanding Parity Bonds and any Future Parity Bonds, if applicable. The Reserve Account Requirement for the Outstanding Parity Bonds is an amount equal to the Average Annual Debt Service on the Outstanding Parity Bonds calculated as of their closing date. The Reserve Account Requirement with respect to Future Parity Bonds will be either an amount equal to Average Annual Debt Service on such issuance of Future Parity Bonds, but in no case shall the amount in the Reserve Account allocable to such issuance of Future Parity Bonds exceed 10% of the proceeds of such bonds, or the ordinance authorizing such issuance of Future Parity Bonds may provide for the creation of a separate reserve account, in which case the Reserve Account Requirement, if any, for such issuance of Future Parity Bonds may be set in such ordinance and the Reserve Account shall not secure such series of Future Parity Bonds.

The City used 2002 Bond proceeds to fund the Reserve Account Requirement for the 2002 Bonds and used 2010A Bond proceeds and 2010B Bond proceeds to fund the Reserve Account Requirement for such bonds. As of April 16, 2013, the balance in the Reserve Account will be \$8,423,980 (consisting of \$3,778,888 from the 2010 Bonds and \$4,645,092 from the 2002 Bonds), which satisfies the Reserve Account Requirement for the Bonds and the Outstanding Parity Bonds. The current Reserve Account Requirement for the Bonds is \$5,296,492 (Average Annual Debt Service on the Bonds). The City may, at any time, substitute Qualified Insurance or a Qualified Letter of Credit for the money and investments in the Reserve Account. See Appendix A for the definitions of “Qualified Insurance” and “Qualified Letter of Credit.” The City will value the Reserve Account and any securities therein on each December 31, and may transfer any excess to the Revenue Fund.

In the event that there shall be a deficiency in the Debt Service Account, the City shall promptly make up such deficiency from the Reserve Account. The City covenants that any deficiency created in the Reserve Account by reason of any withdrawal therefrom for payment into the Debt Service Account shall be made up from money in the Revenue Fund first available after providing for the required payments into the Debt Service Account and after providing for payments under any reimbursement agreement entered into by the City in connection with Qualified Insurance or a Qualified Letter of Credit. See Appendix A—“SUMMARY OF THE BOND ORDINANCE—Payment of and Security for Parity Bonds.”

Additional Obligations

The City has, in the Bond Ordinance, reserved the right to issue Future Parity Bonds, to enter into Parity Payment Agreements (as defined in the Bond Ordinance and described below), and to issue junior lien obligations secured by a subordinate lien on Revenues of the Regional System.

Future Parity Bonds. Pursuant to the Bond Ordinance, the City has reserved the right to issue Future Parity Bonds for any lawful purpose of the City relating to the Regional System, including but not limited to, acquiring, constructing and installing additions, betterments and improvements to and extensions of, acquiring necessary equipment for, or making necessary renewals, replacements or repairs and capital improvements to the Regional System and refunding any outstanding indebtedness upon satisfaction of certain conditions set forth in the Bond Ordinance. Among other things, the Bond Ordinance requires that at the time of the issuance of such Future Parity Bonds there be no deficiency in the Bond Fund and the Second Supply Project Agreement be in full force and effect.

Except for refunding Parity Bonds meeting the conditions described below, there shall be on file prior to the issuance of any Future Parity Bonds either:

- (1) a certificate of the Finance Director (or equivalent official) of each Participant (including the City in the case of the Water System) that will be responsible for paying debt service on the Future Parity Bonds stating that “Revenues” or “Gross Revenues” (as defined in the Participant’s System bond ordinance or resolution), as determined from the financial statements of the Participant’s System, in any 12 consecutive months out of the most recent 24 months were sufficient to pay the Participant’s operation and maintenance expenses of the Participant’s System and the Participant’s portion of the debt service on the Future Parity Bonds then proposed to be issued based on the highest debt service in the next three calendar years following the year through which interest is capitalized or the Project being financed is placed in service, whichever is later, and “Net Revenues” (as defined in the Participant’s bond ordinance or resolution) for such 12-month period were sufficient to pay debt service on the Participant’s senior lien water revenue bonds and meet the Participant’s rate coverage required by such ordinance or resolution; or
- (2) for each Participant (including the City) that will be responsible for paying debt service on the Future Parity Bonds, a certificate of an Engineer or a Certified Public Accountant that the “Adjusted Revenues” (as determined in the Bond Ordinance) for each calendar year during the life of the Future Parity Bonds proposed to be issued will be sufficient to pay the operation and maintenance expenses of the Participant’s System and the Participant’s obligations under the Repayment Agreement to pay a proportionate share of the amount necessary to pay the debt service on the outstanding Parity Bonds and the Parity Bonds then proposed to be issued based on the highest debt service in the next three calendar years following the year through which interest is capitalized or the Project being financed is placed in service, whichever is later, and “Adjusted Net Revenues” (as determined in the Bond Ordinance) will be sufficient to pay debt service on the Participant’s senior lien water revenue bonds and meet the Participant’s rate coverage required by the ordinances or resolutions authorizing such senior lien bonds. In providing that certificate, the Engineer or Certified Public Accountant may take into account certain adjustments to Net Revenue as permitted by the Bond Ordinance.

If the Future Parity Bonds proposed to be issued are for the sole purpose of refunding outstanding Parity Bonds, no such coverage certification shall be required if the issuance of such refunding Future Parity Bonds results in a present value monetary saving to the City and such refunding Future Parity Bonds will not require an increase of greater than \$5,000 in debt service payments to be paid in any Fiscal Year or calendar year thereafter than would have been required to be paid in the same Fiscal Year or calendar year for Annual Debt Service on the Parity Bonds being refunded. See Appendix A—“SUMMARY OF THE BOND ORDINANCE—Future Parity Bonds.”

Under the Second Supply Project Agreement, each Participant has the option to pay cash for or to have the City issue Future Parity Bonds to finance its Participant Share of the capital costs of the Second Supply Project. Upon each issuance of Future Parity Bonds, the Participants’ shares of debt service will be recalculated to reflect their respective aggregate shares of debt service on all outstanding Parity Bonds. Consequently, the Participants’ shares of debt service on all Parity Bonds after the issuance of Future Parity Bonds could be different than their shares of debt service on the Bonds. See “SECURITY FOR THE BONDS—Payment Obligations of the Participants.”

Parity Payment Agreements. The Bond Ordinance permits the City to enter into a Payment Agreement for the purpose of managing or reducing the City's exposure to fluctuations or levels of interest rates, currencies or commodities or other interest rate, investment, asset or liability management purposes. Upon satisfaction of the requirements for the issuance of Future Parity Bonds and of additional requirements contained in the Bond Ordinance, a Payment Agreement may constitute a charge and lien on the Revenues of the Regional System equal in rank with the charge and lien of the Parity Bonds. The City has not entered into any such Parity Payment Agreements and has no plans to do so at this time. See Appendix A—"SUMMARY OF THE BOND ORDINANCE—Parity Payment Agreements."

Junior Lien Obligations. Nothing in the Bond Ordinance prohibits the issuance of obligations of the Regional System with a lien on Revenues junior to the lien of the Parity Bonds. See Appendix A—"SUMMARY OF THE BOND ORDINANCE—Junior Lien Obligations."

Flow of Funds

Amounts in the Revenue Fund shall be applied in each month as follows: first, to the payment of Operating Expenses for such month; and second, to the Bond Fund to pay interest, to pay principal and Mandatory Amortization Installments, and to replenish the Reserve Account and, in the event the City has entered into any Parity Payment Agreement, to make any regularly scheduled City Payments adjusted by any regularly scheduled Receipts (provided, however, that termination payments with respect to any Parity Payment Agreement shall not rank on a parity of lien with the Parity Bonds), and, in the event the City has entered into a reimbursement agreement with respect to Qualified Insurance or a Qualified Letter of Credit or other credit facility, to make all payments required to be made on a parity of lien with the Parity Bonds pursuant to such reimbursement agreement; provided that if there is not sufficient money to make all payments under more than one such reimbursement agreement, the payments shall be made on a pro rata basis. After such required payments are made, amounts in the Revenue Fund may be used to pay junior lien obligations of the Regional System, to finance capital improvements or for any other lawful purpose of the Regional System. See Appendix A—"SUMMARY OF THE BOND ORDINANCE—Revenue Fund; Flow of Funds of the Regional System."

Additional Covenants

The Bond Ordinance also contains covenants regarding operation and maintenance of the Regional System, the Second Supply Project Agreement, sale, transfer or disposition of the Regional System, books and accounts, and maintenance of insurance. See Appendix A—"SUMMARY OF THE BOND ORDINANCE—Covenants with Bondowners."

No Acceleration

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

DEBT SERVICE REQUIREMENTS AND ADDITIONAL BORROWING

The following table shows estimated debt service requirements on the Outstanding Parity Bonds, excluding the Refunded Bonds, and the Bonds. The City understands that a portion of the 35% Federal subsidy it should receive for the 2010B Bonds (and the 2009 Water System Bonds and the 2010B Water System Bonds) will be reduced as a result of the Federal sequestration so long as Congress does not take action. The Internal Revenue Service has announced that the reduction will be 8.7% for payments made through September 2013 (at which time it is subject to change).

Summary of Debt and Debt Service Requirements – RWSS Bonds

Year	Outstanding Parity Bonds(1)	The Bonds		Total Parity Bond Debt Service (2)
		Principal	Interest	
2013	\$ 2,854,286	\$ 960,000	\$ 1,907,531	\$ 5,721,817
2014	2,854,086	1,070,000	3,004,050	6,928,136
2015	2,853,786	1,185,000	2,950,550	6,989,336
2016	2,853,386	670,000	2,891,300	6,414,686
2017	2,850,136	745,000	2,857,800	6,452,936
2018	2,851,736	765,000	2,820,550	6,437,286
2019	2,853,036	1,690,000	2,782,300	7,325,336
2020	2,854,036	1,790,000	2,697,800	7,341,836
2021	2,849,736	1,890,000	2,608,300	7,348,036
2022	2,852,136	1,985,000	2,513,800	7,350,936
2023	2,853,936	2,110,000	2,414,550	7,378,486
2024	2,850,136	4,575,000	2,309,050	9,734,186
2025	2,850,936	4,820,000	2,080,300	9,751,236
2026	2,846,064	5,035,000	1,839,300	9,720,364
2027	2,840,385	5,300,000	1,587,550	9,727,935
2028	2,828,901	5,560,000	1,322,550	9,711,451
2029	2,821,880	5,875,000	1,044,550	9,741,430
2030	2,814,054	6,155,000	750,800	9,719,854
2031	2,805,421	6,425,000	504,600	9,735,021
2032	2,794,846	6,190,000	247,600	9,232,446
2033	6,793,427	--	--	6,793,427
2034	6,700,763	--	--	6,700,763
2035	6,614,105	--	--	6,614,105
2036	6,517,611	--	--	6,517,611
2037	6,416,280	--	--	6,416,280
2038	6,314,831	--	--	6,314,831
2039	6,207,702	--	--	6,207,702
2040	6,099,613	--	--	6,099,613
TOTAL (2)	\$ 108,497,258	\$ 64,795,000	\$ 41,134,831	\$ 214,427,089

(1) Before 35% federal direct payments of interest on the 2010B Bonds.

(2) Totals may not foot due to rounding.

Additional Borrowing

The City does not plan to issue Future Parity Bonds for the Regional System for several years. The City expects to issue approximately \$78,940,000* aggregate principal amount 2013 Water System Bonds on or about May 7, 2013. The City periodically reviews its outstanding bonds for refunding opportunities and may issue Future Parity Bonds or bonds for the Water System for refunding purposes if market conditions warrant.

* Preliminary, subject to change.

THE CITY

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

The City Council appoints a City Manager who is the chief executive officer of the City and who serves at the pleasure of the City Council. The City Manager is responsible to the City Council for the administration of all departments of the City with the exception of the Department of Public Utilities.

The City Manager appoints a Finance Director who supervises the financial and purchasing functions of the City, including the City’s accounting system. The Finance Director is responsible for preparing the Comprehensive Annual Financial Report (“CAFR”) in accordance with generally accepted accounting principles and the instructions of the State Auditor’s Office. The Finance Director is responsible for the payment of principal and interest on all bonds issued by the City, including the Bonds.

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

THE DEPARTMENT OF PUBLIC UTILITIES—TACOMA WATER

Overview

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

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

The Water Division consists of two separate systems: the Regional System and Tacoma Water.

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

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

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

Management

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

William A. Gaines, Director of Utilities, assumed his position in October 2007, after serving as Superintendent/Chief Operating Officer of Tacoma Power for a year. Mr. Gaines, an experienced executive with approximately 32 years in the utility industry, came to Tacoma from Seattle City Light, where he served as Power Supply and Environmental Affairs Officer and as Power Management Executive. He spent much of his career as an executive officer at Puget Sound Energy, where he served as Vice President for Engineering and Contracting and as Vice President for Energy Supply. Mr. Gaines is active in regional industry groups including the Public Power Council, Pacific Northwest Utilities Conference Committee and Western Systems Power Pool, and sits on the Board of the Tacoma/Pierce County Chamber of Commerce and the Pierce County Economic Development Board. Mr. Gaines received a B.S. degree in electrical engineering from Washington State University and an M.B.A. from the University of Puget Sound. He also attended the executive development program at Stanford University.

Linda McCrea, P.E., Superintendent, Water Division, joined the City in 1980, became the Water Distribution Manager in 1993, became Deputy Water Superintendent in 2006 and was appointed Superintendent in January 2010. She has a B.S. in civil engineering from the University of Washington.

Heather Pennington, P.E., Deputy Water Superintendent, Asset and Information Manager, joined Tacoma Water in 1994, and became Tacoma Water's interim Distribution Manager in 2006, Distribution Engineering Manager in 2007, Resource Planning Manager in July 2009 and Resource Planning (now Asset and Information Management) Deputy Water Superintendent in 2011. She holds an M.B.A. from Pacific Lutheran University and a B.S. in environmental engineering from Northwestern University.

Chris McMeen, P.E., Deputy Water Superintendent, Water Quality Manager, joined the City in 2002. He has over 25 years experience in the drinking water industry, including work as an engineering consultant, drinking water regulator, utility engineer and manager. He has a B.S. and M.S. in civil engineering from the University of Washington.

Sean Senescall, Rates and Financial Planning Manager, joined the City in 2010 as the Rates and Financial Planning Assistant Division Manager, and became the Rates and Financial Planning Manager in 2013. He has 7 years of experience in government finance and rate development. He attended the U.S. Air Force Academy and has a B.S. in economics from the University of Washington.

Glen George, P.E., Water Supply Manager, joined the City in 1992 as a Civil Engineer and became the Water Supply Manager in March 2010. He has a B.S. in civil engineering from the University of Washington.

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

Tony Lindgren, P.E., Water Distribution Engineering Manager, joined the City in 2002 and became the Resource Planning (now Asset and Information Management) Assistant Division Manager in 2010, and the Distribution Engineering Manager in January 2011. He has a B.S. in civil engineering from Washington State University.

Budgetary Policies

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

Auditing

Accounting systems and budgetary controls are prescribed by the Office of the State Auditor in accordance with RCW 43.09.200 and RCW 43.09.230. State statutes require audits for cities to be conducted by the Office of the

State Auditor. The City complies with the systems and controls prescribed by the Office of the State Auditor and establishes procedures and records which reasonably assure safeguarding of assets and the reliability of financial reporting.

The State Auditor is required to examine the affairs of cities at least once every two years. The City is audited annually. The examination must include, among other things, the financial condition and resources of the City, whether the laws and constitution of the State are being complied with, and the methods and accuracy of the accounts and reports of the City. Reports of the auditor's examinations are required to be filed in the Office of the State Auditor and in the finance department of the City.

The City has contracted with Moss Adams LLP to perform the annual audit of the financial statements of Tacoma Water for the 2012 fiscal year. The audited financial statements of Tacoma Water for fiscal years 2011 and 2012 prepared by Tacoma Water and audited by Moss Adams LLP are contained in Appendix D. Moss Adams LLP, the City's independent auditor, has not been engaged to perform and has not performed, since the date of its report included herein, any procedures on the financial statements addressed in that report. Moss Adams LLP also has not performed any procedures related to this Official Statement.

Retirement System

Substantially all employees of Tacoma Water are covered by a contributory retirement plan administered by the City's Employee Retirement System ("TERS"). TERS is a local single employer defined benefit pension retirement plan covering City employees other than law enforcement officers, fire fighters, and railroad employees, who are covered by retirement plans operated by other entities. The Board of Administration of TERS administers the plan, and benefit provisions are established in accordance with chapter 41.28 RCW and Chapter 1.30 of the Tacoma City Code. The Board of Administration of TERS consists of nine members, including the Mayor, City Administrator, Finance Director, designee of the Director of Utilities, three employees and one retiree. As of December 31, 2012, there were 2,107 retirees and beneficiaries receiving benefits, 426 vested terminated employees entitled to future benefits, and 2,861 active members in TERS.

Tacoma Water is current in all payments to TERS. Further details about TERS are provided in Note 10 in Appendix D—"CITY OF TACOMA WATER SYSTEM 2011 AND 2012 FINANCIAL STATEMENTS."

Contributions City-wide totaled \$42.4 million in 2011 (\$22.5 million employer contributions and \$19.9 million employee contributions) and totaled \$40.2 million in 2010 (\$21.3 million employer contributions and \$18.9 million employee contributions). The contribution rate for Tacoma Water's covered payroll is currently set at 20% of gross wages for 2013 (10.80% paid by Tacoma Water and 9.20% paid by employees). Tacoma Water contributed \$1,908,977 in 2011 and \$1,954,051 in 2012 into TERS.

The most recent actuarial valuation of TERS was completed as of January 1, 2012 by Milliman (the "Milliman Report"). Assumptions include investment earnings of 7.75%, wage growth of 4.25% and price inflation of 3.25%. TERS's 2011 market value investment return of 1.3% was less than the 7.75% investment earning assumption. According to the Milliman Report, due primarily to the continued recognition of a large asset loss in 2008, as of January 1, 2012 the Funding Ratio declined from 94.9% to 90.1% and the projected amortization period for the Unfunded Actuarial Accrued Liability ("UAAL") has increased from 12.8 years to 35.0 years. This is based on the Actuarial Value of Assets ("AVA") which smooth gains and losses over four years. As of January 1, 2012, the large 2008 loss was fully recognized in the AVA. Since the 2011 investment return of 1.3% was lower than the 7.75% assumption, measures based on the Market Value of Assets ("MVA") also declined. Specifically, based on MVA, the Funding Ratio declined from 95.4% to 91.3% and the projected amortization period of the UAAL increased from 11.4 years to 27.7 years. The asset losses were partially offset by salary increases that were less than assumed.

TERS Valuations
(Millions of \$)

Actuarial Valuation Date	Actuarial Value of Assets	Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	Percentage of Covered Payroll
01/01/2007	\$1,021.3	\$ 895.8	\$(125.5)	114.0%	\$175.0	(71.7)%
01/01/2009	1,097.3	1,002.3	(95.0)	109.5	197.4	(48.1)
01/01/2011	1,074.8	1,132.9	58.1	94.9	219.6	26.5
01/01/2012	1,068.3	1,185.5	117.2	90.1	219.4	53.4

The Milliman Report provides the following information regarding long-term funding projections: The baseline projection demonstrates that if experience in all future years matches the actuarial assumptions, including 7.75% investment returns, the Funding Ratio is projected to reach 100% by 2040. However, a downside scenario projection showing that adverse investment experience similar to what TERS experienced in 2006 – 2008 could require contribution rates to increase as high as 29.37% of pay to amortize the UAAL over 30 years. Future experience is expected to be both better and worse than the actuarial assumptions at different times and is likely to result in changes to TERS's funding status.

Although TERS is funded over a long period of time, the measurement of TERS's funding status can vary widely from year-to-year due to asset returns. The following table summarizes TERS's asset returns in recent years and compares the market value gains and losses to the AAL at the following valuation date. Returns greater than the 7.75% actuarial assumption are gains; returns less than the 7.75% actuarial assumption are losses. The AVA recognizes these market value gains and losses in four equal increments starting at the end of the year in which they occur. Gains in good years are needed to offset losses in bad years. The \$451 million market value loss in 2008, equal to 45% of TERS's AAL, and was fully recognized in the actuarial assets as of January 1, 2012.

TERS Asset Returns

Year	Market Value % Return*	Market Value Gain/ (Loss) compared to expected	End of Year Actuarial Accrued Liability (AAL)	Gain / (Loss) as a % of next AAL
2002	(8.9)%	\$ (112,800,000)	\$ 686,800,000	(16.4)%
2003	29.4	131,400,000	**	17.4
2004	15.5	60,100,000	754,300,000	8.0
2005	8.7	8,500,000	**	0.9
2006	48.6	102,800,000	895,800,000	11.5
2007	3.9	(42,200,000)	**	(4.2)
2008	(32.0)	(451,000,000)	1,002,300,000	(45.0)
2009	27.3	147,700,000	**	13.0
2010	14.1	60,200,000	1,132,900,000	5.3
2011	1.3	(69,900,000)	1,185,500,000	(5.9)

* The market value returns shown above are net of investment expenses, but not administrative expenses. They are based on the TERS's annual financial statements, but may have some variance from calculations performed by other parties due to different methodology. The preliminary estimate of the market value in 2012 is 14.1%.

** Until 2011, valuations were performed every other year.

In August 2012, the Board of Administration of TERS changed the rate of return assumption from 7.75% to 7.5%. This changed assumption will be reflected in the valuation report for 2012 expected in May 2013.

In addition to TERS, City employees participate in the Federal social security program. The City withholds the employee contribution from City employee's wages.

Other Post-Employment Benefits

The City allows retirees to participate in medical, dental and vision programs from the time retirement begins until they qualify for Federal funded programs. The City uses pay as you go funding, and upon retirement the retiree is responsible for paying a blended premium, which prior to retirement was paid by the City. The benefit is an implicit subsidy to the retiree. As of December 31, 2012, the City's net OPEB obligation was \$46,469,368, of which \$2,055,309 was related to the Water System. Further details about OPEB are provided in Note 11 in Appendix D—"CITY OF TACOMA WATER SYSTEM 2011 AND 2012 FINANCIAL STATEMENTS."

Taxation

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

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

Program of Insurance

Tacoma Water currently maintains insurance policies and a self insurance program. The insurance policies presently in effect include coverage on the Department's buildings and fleet vehicles as well as general liability and public officials liability. The current insurance policies have deductibles or self insured retention of \$250,000 for buildings and vehicles, and \$1,500,000 for general comprehensive liability. The public officials policy has a deductible of \$200,000 for employee practices liability. The general comprehensive liability policies provide \$40 million of coverage. The City has a policy to cover extraordinary worker's compensation claims with a statutory limit and \$1 million retention. Earthquake coverage has a 5% or \$250,000, whichever is greater, per building self-insured retention.

Tacoma Water participates in the Department's self insurance claim fund (the "Self Insurance Fund") for payment of third party claims. As of December 31, 2012, assets in the Self Insurance Fund totaled \$5.4 million, which exceeds accrued and incurred but not reported liabilities. Tacoma Water's premium payments in both 2011 and 2010 totaled \$120,000. Tacoma Water's premium payment in 2012 was \$496,377 due to one large injury settlement. Contributions are routinely reviewed to determine their adequacy. The Self Insurance Fund is dedicated and requires a two thirds vote of the City Council before it can be used for anything except insurance or casualty losses. The City and the other Second Supply Project Participants separately insure or self insure the Second Supply Project and potential liabilities arising from or related to the Second Supply Project.

Performance and fidelity bonds covering all employees are provided in amounts up to \$1 million (subject to a \$25,000 deductible per occurrence).

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

Financial Policies

Tacoma Water has formally adopted certain policies that serve as a guide to financial management and rate setting. These are included in the "Water Rate and Financial Policy" document and are reviewed and approved by the Board and City Council when changes are recommended by staff. These policies include rates based on cost of service within a customer class, restrictions on the term of debt, and maintenance of a minimum of 60 days of operating cash. The policies provide that water rates must be designed to adequately fund acquisition of new resources and conservation. The Board and City Council approved the amended Water Rate Policy in February 2013, to formalize debt service coverage minimums (at least 1.25 times on all Water System debt including junior lien debt, and with

taxes included as operating expenses) and an increase in the portion of rate revenues recoverable from the fixed component of the rate to 65%.

Tacoma Water operates under the guidance of its strategic plan, which was completed in 2012 to provide strategic focus for the utility for at least three to five years. This plan identifies eight initiatives, and progress towards the implementation of these initiatives will be closely monitored in the coming years. Financial forecasting scenarios were developed as a part of and incorporated into the strategic plan. These scenarios are meant to gauge the sensitivity of water rates to various contingencies. The plan also addresses financing and rate requirements necessary to support the implementation of the operations and capital programs. It served as the basis for developing Tacoma Water's 2013-2014 budget approved by the Board and City Council.

State law and City policies permit City utilities to borrow on a short-term basis from the General Fund. Tacoma Water has never borrowed from the General Fund and has no plans to do so.

Labor Relations

Tacoma Water has approximately 248 employees, many of whom are represented by Local 483-International Brotherhood of Electrical Workers ("IBEW"), one of the 12 labor organizations that represent City employees. Other units representing Tacoma Water employees include Local 117-Teamsters, Local 17-Professional and Technical Engineers, and Local 120-AFSCME. Negotiations with unions are conducted by a team chaired by a Human Resources Labor Relations staff member selected by the Human Resources Director, who reports directly to the City Manager. Management of Tacoma Water strives to promote sound labor relations policies that are beneficial both to its operations and to its employees. This cooperative effort has precluded a significant work stoppage among utility employees for the last several decades, although there was an 11 day work stoppage by clerical members of IBEW, Local 483, in 1992.

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

Investments

The City's Investment Committee is composed of the Mayor, the Finance Director and the City Treasurer. Among the investments permitted by State law and the Investment Committee's policy are banker's acceptances of the top 50 world banks as published by American Banker; U.S. Treasury bills, certificates, notes and bonds; certain U.S. Government agency securities; commercial paper with the highest rating by at least two nationally recognized rating agencies; repurchase agreements with the market value of collateral exceeding the dollar amount of the repurchase agreement by 2% over the term of the agreement; reverse repurchase agreements; the State Local Investment Pool (described below); and municipal securities.

The City is authorized under State Law, primarily RCW 43.84.080, RCW 39.59.020 and by the City of Tacoma Investment Policy (Tacoma City Charter Section 7.4) to make security lending transactions. Securities lent are collateralized with cash or securities having 102% of market value.

As of December 31, 2012, the City's cash and investments, on a fair value basis, totaled \$954 million, not including City pension funds, of which a portion was Tacoma Water funds. The portfolio was distributed in various types of investment instruments in the following percentages:

City Investments
(As of December 31, 2012)

Bank Interest-Bearing Accounts	6.23%
LGIP	7.65
Municipal Securities	27.33
Federal Agricultural Mortgage Corp (Farmer Mac)	1.51
Federal Home Loan Mortgage Assn (Freddie Mac)	17.66
Federal Farm Credit Bank (Farm Credit)	6.00
Federal Home Loan Bank (Home Loan)	7.56
Federal National Mortgage Assn (Fannie Mae)	23.58
Tennessee Valley Authority (TVA)	1.45
U.S. Treasuries	0.11
Secured Repurchase Agreements	0.92
Total	<u>100.00%</u>

Source: City of Tacoma.

State Local Investment Pool. The State Treasurer's Office administers the Washington State Local Government Investment Pool (the "LGIP"), which invests over \$9 billion on behalf of more than 450 cities, counties and special taxing districts. In its management of LGIP, the State Treasurer is required to adhere, at all times, to the principles appropriate for the prudent investment of public funds. These principles are, in order of priority, (i) the safety of principal; (ii) the assurance of sufficient liquidity to meet cash flow demands; and (iii) the attainment of the highest possible yield within the constraints of the first two goals. Historically, the LGIP has had sufficient liquidity to meet all cash flow demands.

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

Authorized Investments for Bond Proceeds. In addition to the eligible investments discussed above, bond proceeds may also be invested in mutual funds with portfolios consisting of U.S. government and guaranteed agency securities with average maturities of less than four years; municipal securities rated in one of the four highest categories; and money market funds consisting of the same, so long as municipal securities held in the fund(s) are in one of the two highest rating categories of a nationally recognized rating agency. Bond proceeds may also be invested in shares of money market funds with portfolios of securities otherwise authorized by law for investment by local governments (RCW 39.59.030).

THE SECOND SUPPLY PROJECT

Description of the Second Supply Project

To meet its own future water supply requirements as well as to increase regional supply, in 1968 Tacoma Water began developing the Second Supply Project, which includes a second supply pipeline from Tacoma Water's Green River resource (the "Second Supply Pipeline"). The Second Supply Project is the major source of Tacoma Water's water supply. For a description of Tacoma Water, see "THE CITY OF TACOMA WATER SYSTEM."

The Second Supply Project consists of the following components: (i) water from the exercise of Tacoma Water's Second Diversion Water Right (up to 100 cubic feet per second ("cfs")); (ii) the Second Supply Pipeline; (iii) improvements made at the headworks diversion dam and intake; (iv) Second Supply Project fisheries and environmental enhancements; (v) the right to store water as a result of the Howard Hanson Dam Additional Storage Project; and (vi) Treatment Facilities (disinfection, pH adjustment, fluoridation, and ozone). The Second Supply Pipeline is approximately 34 miles long and varies from 48 to 90 inches in diameter. Its route follows a more northerly route than Tacoma Water's Pipeline No. 1, traversing south King County and thereby making water available to the urbanized areas north and east of Tacoma. In addition to increasing water supply, the Second Supply Project increases flexibility and reliability of water delivery in both Tacoma Water's and the other Participants' service areas. The Second Supply Project became operational in October 2005. All components of the Second Supply Project are complete, with the exception of the Howard Hanson Dam additional water storage project, which is expected to be completed in 2017.

Tacoma Water owns the Second Supply Project. It also is the holder of the Second Diversion Water Right and the operator of the Second Supply Project. The Second Supply Project is a separate utility system of the City.

Tacoma, Kent, Covington, and Lakehaven (the "Participants") participate in the Second Supply Project under the terms of the Second Supply Project Agreement, which defines their rights and obligations with regard to the Second Supply Project. Tacoma has a 15/36 Participant Share and each of Kent, Covington, and Lakehaven has a 7/36 Participant Share in the Second Supply Project. Generally, a Participant Share represents a Participant's proportional right to receive and obligation to pay for water delivered by the Second Supply Project. See "SECURITY FOR THE BONDS – Payment Obligations of the Participants."

Under the Second Supply Project Agreement and the associated Repayment Agreement, Tacoma Water is responsible for paying debt service on \$32,925,000 of the principal amount of the 2010 Bonds and is expected to be responsible for \$35,840,000 of the principal amount on the Bonds. Kent is responsible for paying debt service on \$11,400,000 of the principal amount of the 2010 Bonds and is expected to be responsible for \$14,790,000 of the principal amount on the Bonds. Covington is responsible for paying debt service on \$3,515,000 of the principal amount of the 2010 Bonds and is expected to be responsible for \$14,165,000 of the principal amount on the Bonds. Covington has received State Revolving Fund loans for the Filtration Treatment Project and is expected to contribute \$8,080,000 of loan proceeds to finance a portion of its share of the project. In order to reduce the amount that Tacoma would need to borrow to pay its share of additional costs of the Filtration Treatment Project, Tacoma has agreed to use a portion of Covington's share of unspent 2010 Bond proceeds for Tacoma's share of the project, and in return, pay a portion of the principal of and interest on the 2010 Bonds that are currently the responsibility of Covington. Kent and Covington will pay their share of debt service to Tacoma, which will pay the bond registrar for the RWSS Bonds. Those percentage shares are subject to change with the addition of a new participant, the payment default of a Participant, the issuance of additional RWSS Bonds or the optional prepayment by an obligated Participant. The payments by Tacoma Water, Kent and Covington constitute "Contract Resource Obligations" payable as operation and maintenance expenses from the gross revenues of their respective water utilities. The Repayment Agreement governs debt service payments on the RWSS Bonds and does not otherwise affect each Participant's rights and obligations under the Second Supply Project Agreement. The Repayment Agreement takes precedence over the debt repayment provisions of the Project Agreement.

Filtration Treatment Project

The Second Supply Project Agreement envisioned that future state or Federal regulations may require additional or different Treatment Facilities in order for Project Water to remain in compliance with water quality regulations. The

Second Supply Project Agreement defines the costs associated with additional or different Treatment Facilities to be Project Costs, apportioned to each of the Participants on the basis of their Participant Share. Further, the Second Supply Project Agreements call for the Project Committee (as described under “Second Supply Project Agreement and Repayment Agreement—*Project Committee*”) to make a determination of what Treatment Facilities should be added to the Second Supply Project.

Representatives from Kent, Covington and Lakehaven participated in the treatment plant decision process conducted by Tacoma Water. The Covington and Lakehaven Boards and the Kent City Council approved the installation of a filtration treatment system for the Second Supply Project in order to address public health, supply reliability and regulatory compliance issues associated with the Second Supply Project water supply.

The Green River is one of the few remaining major unfiltered surface water supplies in the country. In 2006, the U.S. Environmental Protection Agency promulgated the Long Term 2 Enhanced Surface Water Treatment Rule (“LT2”), establishing new requirements for all water utilities serving water from lakes or rivers to provide treatment for inactivation or removal of *Cryptosporidium*. *Cryptosporidium* is a naturally-occurring micro-organism that can be found in open surface water sources such as the Green River, and has been responsible for waterborne disease outbreaks in some public water systems. While years of monthly testing from the Green River indicates that the presence of this organism is extremely rare, the LT2 regulation required Tacoma Water to install additional treatment for *Cryptosporidium* by 2014. The Participants worked with a consulting team to analyze potential strategies for LT2 compliance. Following substantial analysis, significant public outreach and communication, the filtration option was selected as the best solution for the long-term benefit of the utility customers. In 2010, the Tacoma Public Utility Board, the Tacoma City Council, the Covington and Lakehaven Boards and the Kent City Council each adopted a resolution approving the installation of the Filtration Project. The Second Supply Project Agreement defines the costs associated with additional or different treatments facilities to be Project Costs, apportioned to each of the Participants on the basis of their Participant Share.

Following Board and City Council approval, design was authorized in 2010, and continued through 2011 and early 2012. The Filtration Project is being delivered using an alternative delivery methodology allowed under State law (Chapter 39.10 RCW) called General Contractor/Construction Manager (GC/CM). This project delivery approach enables substantial risk control through the selection of a qualified general contractor, and close collaboration between Tacoma Water, the Design Engineer, and the Contractor. To date, with over 85% of the work under contract, overall project costs are at approximately 80% of the upper bound budget approved by the Board. Underground work on facility foundations, where there are typically significant risks for major civil projects, is completed.

The 2010A Bonds and 2010B Bonds were issued to finance the costs of Phase I of the Filtration Treatment Project except for Lakehaven’s share (for which Lakehaven paid cash). Phase I work covers those portions of the Filtration Treatment Project completed between July 2010 and anticipated to be completed by approximately August 2013. This work includes completed design, permitting, and early stages of construction, including major earthwork and the early stages of major concrete placement. Phase II work will complete the concrete, major piping, and treatment process construction steps, leading toward an operational filtration plant by the end of 2014.

The total estimated cost for the Filtration Project is \$195 million. Tacoma Water is responsible for an estimated \$84.7 million of this total for its first diversion operations (the Tacoma Water system). The Second Supply System is responsible for an estimated \$110.3 million of Filtration Project costs. Tacoma Water is responsible for \$45.9 million of this portion.

Second Supply Project Agreement and Repayment Agreement

The term of the Second Supply Project Agreement extends through the Operating Life of the Second Supply Project, including all renewals and replacements thereof and additions thereto. Consistent with the Second Supply Project Agreement, the Participants expect that the Second Supply Project will have an operating life of no less than 100 years. The Second Supply Project Agreement provides that all obligations incurred during its term will survive its termination or expiration, and such obligations will survive until satisfied.

Rights and Obligations. The Second Supply Project Agreement confers rights and imposes obligations on all four Participants, including Tacoma Water, and on Tacoma Water as operator of the Second Supply Project (the “Project

Operator”). Each Participant has contractual rights under the Second Supply Project Agreement (i) to use an undivided share of the Second Supply Project equal to its project capacity share and to use available excess project capacity; (ii) to schedule for delivery and receive its Participant Share of Second Diversion Water at its points of delivery; (iii) to schedule for delivery and receive additional water at its points of delivery; and (iv) to its Participant share of storage. Each Participant has a contractual obligation (i) to receive Second Diversion Water and additional water scheduled for delivery by and delivered to it; and (ii) to pay its Participant Share of Project Costs.

As Project Operator, Tacoma Water is responsible for the day-to-day operation of the Second Supply Project and is obligated, consistent with the approved Project Annual Budget then in effect, to operate and maintain the Second Supply Project in a manner that is consistent with Prudent Utility Practice. Tacoma Water also is responsible as Project Operator for, among other things, (i) monitoring the delivery of Project Water to each Participant and (ii) calibrating and testing for accuracy the Master Meter and all Delivery Meters.

Water deliveries are scheduled on a weekly basis by an assigned Tacoma Water engineer. Tacoma Water tracks availability of run-of-the-river water for the Second Supply System and also tracks and coordinates delivery of stored water at Howard Hanson Dam. Tacoma Water maintains financial and water accounting records for the Second Supply System, providing reports to the Participants in accordance with the Second Supply Project Agreement. Daily flow records and other daily data are available to the Participants through a secure website. A monthly meeting is held by the Project Committee to discuss any issues or concerns related to the Second Supply Project. An operations subcommittee also meets bi-monthly to deal with operations issues.

Project Committee. Decisions are made by a Project Committee, consisting of one representative of each Participant. For the Project Committee to take action, a quorum of not less than three Participants is required, with Tacoma’s presence mandatory. For approval of certain matters, including approval of capital expenditures contained in an annual budget and approval or revision of any Financing Plan, an affirmative vote of 29/36ths of the Project Committee votes and three of the Participants is required. Further, in order to vote on a Financing Plan, the representative of each Participant must present to the Project Committee a resolution by its governing body indicating the nature of the vote to be cast by the representative. A Financing Plan sets forth the purpose, amount, repayment schedule and timing of any proposed Project Bond issuances. The Participants previously executed a Financing Plan for the 2002 Bonds, which includes the refunding of such 2002 Bonds.

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

Project Annual Budget and Capital Budget. Under the Second Supply Project Agreement, the Second Supply Project operates under an annual budget, which must include both the amounts necessary to operate and maintain the Second Supply Project and any proposed capital expenditures for any renewals, replacements, additions or improvements to the Second Supply Project.

The Second Supply System’s first capital project annual budget, not including initial project construction, was approved for the year 2008. Tacoma Water is required to submit to the Project Committee by no later than each July 1 a proposed Project Annual Budget for the next calendar year. By no later than October 15 the Project Committee must approve the Project Annual Budget as submitted by Tacoma Water or approve a Project Annual Budget as revised by the Project Committee. If the Project Committee has not approved a Project Annual Budget by January 1, Tacoma Water may operate the Second Supply Project and expend funds in accordance with the Project Annual Budget from the immediately preceding calendar year.

The City has established a Second Supply Project operating reserve account equal to two months of its annual operating budget.

Annual Operating Plans. Detailed provisions of the Second Supply Project Agreement govern, among other things, (i) the scheduling, withdrawal and use of Second Diversion Water from Storage, (ii) the metering of Project Water,

(iii) the introduction into the Second Supply Project of Additional Water, (iv) the Storage of Second Diversion Water upon completion of Phase I of the Howard Hanson Additional Storage Project, (v) the uses of Project Capacity and Excess Project Capacity, and (vi) the effects of Uncontrollable Force affecting the water systems of the Participants on the obligations of the Participants under the Second Supply Project Agreement.

Payment of Project Costs. The Second Supply Project Agreement governs the City's billing of Participants, no more frequently than once in each calendar month, for costs set forth in the Project Annual Budget then in effect. The Second Supply Project Agreement requires disputed invoices to be paid in full, and provides a procedure for resolving invoice disputes and reconciling disputed payments. Payments will be considered past due and will accrue a late payment charge if not received on or before the Due Date. Tacoma Water may elect to suspend deliveries of scheduled Project Water to any Participant for which an invoice or portion thereof remains unpaid for a period of 30 days after the Due Date, such suspension to apply until the Participant has paid in full all amounts due and owing.

Payment of Bonds: Defaults in Payment. All bonds issued for the Regional System to finance the Second Supply Project ("Project Bonds") are required to be issued in accordance with a Financing Plan submitted by Tacoma Water and approved by the Project Committee. In lieu of paying its respective Participant Share of amounts necessary for the City to repay Project Bonds, a Participant may elect to fund all or any part of its Participant Share of a Project Cost by the payment of cash. Lakehaven elected to pay cash for its Participant Share of the Project Costs financed by the other Participants with the proceeds of the 2002 Bonds, 2010A Bonds and 2010B Bonds. The Repayment Agreement governs the payments by Kent and Covington of their shares of amounts necessary for the Regional System to pay principal of and interest on the Bonds. The Bond Ordinance governs the payments by Tacoma Water of the principal of and interest on the Bonds.

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

Project Participants

Four Washington municipalities are the Participants in the Second Supply Project in the following fractional shares: Tacoma - 15/36; Kent - 7/36; Covington - 7/36; and Lakehaven - 7/36 ("Participant Shares"). Each Participant is entitled to use its Participant Share of Project Capacity and Second Diversion Water and is obligated to pay its Participant Share of Project Costs pursuant to the Second Supply Project Agreement. Under that agreement, Participants may elect to pay their Participant Share of certain Project Costs by participating in the City's issuance of "Project Bonds" or may elect to pay cash to the City for their Participant Share of those Project Costs. See "THE SECOND SUPPLY PROJECT—Second Supply Project Agreement and Repayment Agreement." For purposes of the Second Supply Project Agreement, the Outstanding Parity Bonds were all Project Bonds. Lakehaven elected to separately pay its Participant Share of the Second Supply Project and Filtration Treatment Project Costs otherwise financed with the proceeds of the Outstanding Parity Bonds. Therefore, only Tacoma Water, Kent and Covington are obligated to pay debt service on the Bonds. See "SECURITY FOR THE BONDS—Payment Obligations of the Participants."

Tacoma Water. Tacoma Water is described under the heading "THE CITY OF TACOMA WATER SYSTEM."

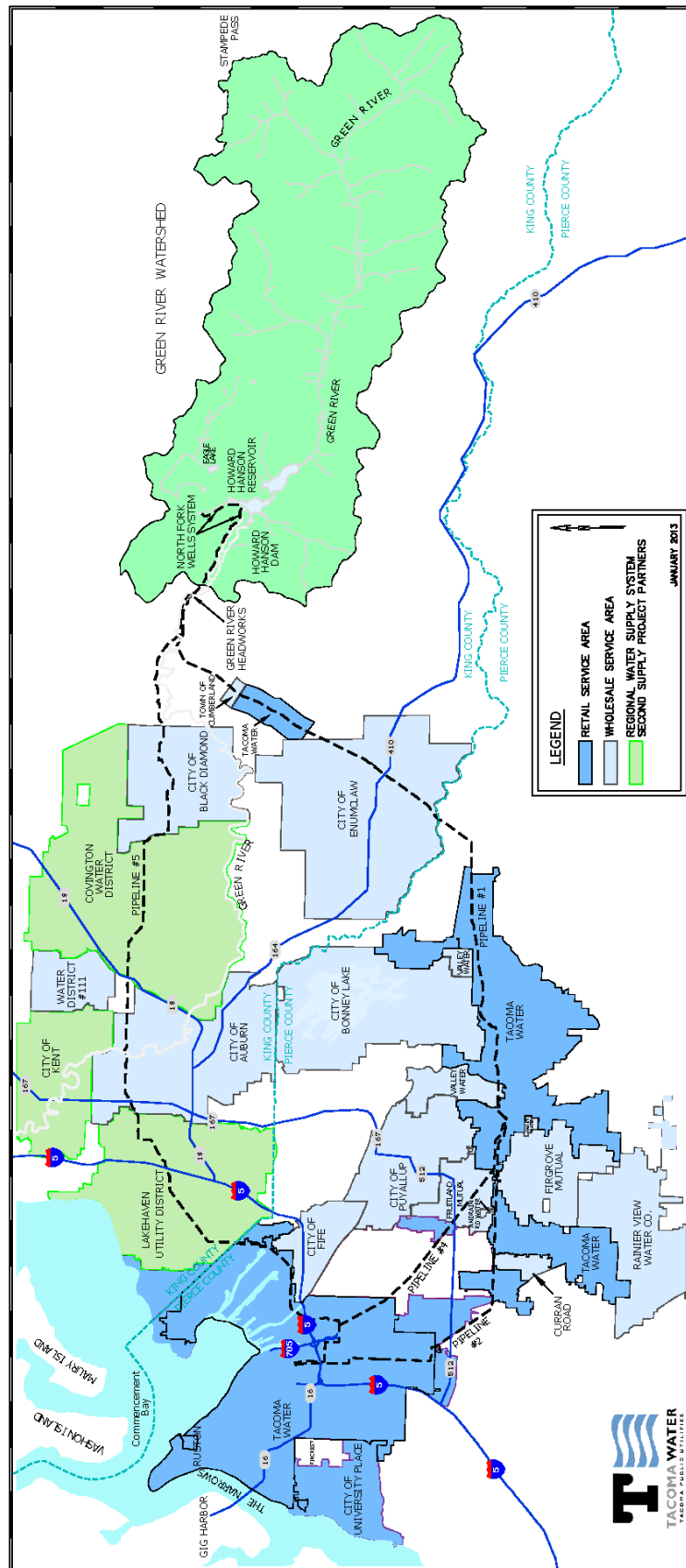
City of Kent. Kent is a code city of the State, incorporated in 1890. It is organized under a mayor-council form of government and has an estimated 2012 population of 119,100. Kent's water utility is managed by Kent's Director of Public Works who is accountable to the city council, which sets rates and charges and authorizes borrowings for the utility. Kent's water utility service area encompasses the city and certain unincorporated areas of King County. See Appendix B—"PARTICIPANTS IN THE SECOND SUPPLY PROJECT—The City of Kent."

Covington Water District. Covington is a special purpose district established in 1960. Covington is governed by a five-member board of commissioners and managed by a general manager. Covington is located in the southeastern portion of King County. Its service area encompasses approximately 55 square miles, with boundaries that include the City of Covington, approximately 60% of the City of Maple Valley, approximately 10% of the City of Black

Diamond, and unincorporated areas of King County (which is approximately 34% of its customer base). See Appendix B—“PARTICIPANTS IN THE SECOND SUPPLY PROJECT—Covington Water District.”

Lakehaven Utility District. Lakehaven (formerly Federal Way Water and Sewer District) is a special purpose district established in 1956. It is governed by a five-member board of commissioners and managed by a general manager. Lakehaven is located between the cities of Seattle and Tacoma in King and Pierce Counties. Lakehaven’s northern boundary is one mile south of Kent, the southern boundary overlaps slightly the Pierce County line, the western boundary follows the Puget Sound shoreline and the eastern boundary overlaps slightly the western city limits of Auburn. Lakehaven provides service to most of the City of Federal Way and to small portions of the cities of Auburn, Pacific, Tacoma, Des Moines and Milton. In addition, Lakehaven serves an unincorporated area of King County approximately 18 square miles north of Federal Way and west of Auburn. Lakehaven contributed cash to pay its share of the costs of the Second Supply Project and is not responsible for a share of debt service on the Bonds. See Appendix B—“PARTICIPANTS IN THE SECOND SUPPLY PROJECT—Lakehaven Utility District.”

The following map shows the service areas of the Participants:



Environmental Issues

The City's Habitat Conservation Plan for its Green River operations has been approved by the National Marine Fisheries Service and the U.S. Fish and Wildlife Service, resulting in the July 2001 issuance of an Incidental Take Permit to Tacoma from each agency pursuant to the Endangered Species Act. These Incidental Take Permits are for a term of 50 years, which provides critical long-term certainty for Tacoma's water supply operations on the Green River. A programmatic environmental impact statement ("EIS") for the Second Green River Diversion and Transmission Project was prepared in 1980, and a project-specific EIS was prepared in 1987 and updated in 1994. See also "THE CITY OF TACOMA WATER SYSTEM—Endangered Species Act Compliance."

To gain support from the many interested parties potentially affected by the Second Supply Project, Tacoma Water has used a consensus approach to solving various environmental issues including obtaining the 404 permit and extension associated with completion of the Second Supply Project. All mitigation projects associated with the construction of the Second Supply Pipeline have been completed and required post-construction maintenance and monitoring are either on-going or have been completed.

Agreement with Muckleshoot Tribe

An agreement was signed in August 1995 with the Muckleshoot Indian Tribe (the "Muckleshoots") that recognizes the importance of the Green River to the Muckleshoots' fisheries and cultural history. The settlement package had a cost of approximately \$30,000,000, of which \$25,213,000 has been paid to date, and includes five basic elements: (1) building a fish restoration facility and paying for annual operation and maintenance of that facility or, at the Muckleshoots' election, making an equivalent cash payment; (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 Muckleshoots; and (5) providing for limited access into the Green River watershed. With respect to item (1) above, the Muckleshoots have elected to accept an equivalent cash payment, relieving Tacoma Water of the annual operation and maintenance obligation. The Muckleshoots have until 2015 to determine if they would like to utilize the cash payment they have received for a fish restoration facility. The settlement resolves past damage claims by the Muckleshoots for Tacoma Water's historical operations on the river, gains the Muckleshoots' support for the Second Supply Project and provides a basis for a long-term cooperative working relationship on the Green River.

Water Use

The average daily water of the Second Supply System used by the Participants for the years 2008 through 2012 appear below. The Participants have other sources of water.

Second Supply System Average Daily Total Water Use (MGD)					
	2008	2009	2010	2011	2012
Tacoma Water	25.85	23.84	15.57	15.53	19.57
City of Kent	0.10	0.74	0.54	0.47	0.64
Lakehaven Utility District	4.69	2.14	2.89	5.25	6.09
Covington Water District	1.22	1.16	1.90	1.96	2.60
Total Use	31.86	27.87	20.90	23.21	28.89

MGD = million gallons per day.

Operating Results

Tacoma Water and the other Participants pay all costs of the Regional System on the same lien as operating costs of their respective utilities, prior to the payment of debt service and capital expenses. The other Regional System Participants are billed and pay monthly their share of capital and operating and maintenance expenses. Payments for debt service on the RWSS Bonds are paid by the other Participants monthly for the 2002 Bonds and the Bonds and

semi-annually for the 2010 Bonds in advance when the debt service payments are due. Tacoma Water receives the payments from the other Participants and pays all operating costs and debt service of the Regional System.

The Regional System annual revenues are established to approximately equal annual operating costs and debt service. Variations from year to year primarily reflect the timing of payments received by Tacoma Water and payments made for capital projects. If another Participant defaults, Tacoma Water is obligated to increase its Participant's share, including paying debt service on the Bonds. See "THE CITY OF TACOMA WATER SYSTEM – Historical Operating Results."

The following table shows selected historical revenues and expenses for the Regional Water Supply System for the years 2008 through 2012.

Regional Water Supply System Historical Operating Results (Year ending December 31)					
	2008	2009	2010	2011	2012
Operating Revenues					
Tacoma Water	\$ 3,738,462	\$ 3,737,135	\$ 4,500,707	\$ 4,026,921	\$ 4,709,244
Kent	1,630,416	1,211,628	1,890,066	1,677,415	1,869,737
Covington	1,601,782	1,177,764	1,879,914	1,671,137	1,859,353
Lakehaven	<u>660,194</u>	<u>328,090</u>	<u>882,662</u>	<u>916,591</u>	<u>5,977,937</u>
Total Operating Revenue	\$ 7,630,854	\$ 6,454,617	\$ 9,153,349	\$ 8,292,064	\$ 14,416,271
Operating Expenses					
Operating & Maintenance	\$ 2,300,026	\$ 2,629,850	\$ 2,458,379	\$ 2,485,977	\$ 2,510,085
Depreciation	<u>4,803,549</u>	<u>4,792,037</u>	<u>4,426,113</u>	<u>4,482,820</u>	<u>4,495,971</u>
Total Operating Expenses	\$ 7,103,575	\$ 7,421,887	\$ 6,884,492	\$ 6,968,797	\$ 7,006,056
Net Operating Income (Loss)	\$ 527,279	\$ (967,270)	\$ 2,268,857	\$ 1,323,267	\$ 7,410,215
Non-Operating Revenue (Expenses)					
Other Income	\$ 14,360	\$ 0	\$ 0	\$ 0	\$ 0
Interest Income	293,709	184,332	861,775	396,391	407,622
Interest Charges (Net)	<u>(3,411,937)</u>	<u>(3,918,240)</u>	<u>(4,833,300)</u>	<u>(6,440,678)</u>	<u>(4,968,459)</u>
Total Non-Operating Revenue (Expense)	\$ (3,103,868)	\$ (3,733,908)	\$ (3,971,525)	\$ (6,044,287)	\$ (4,560,837)
Net Income (Loss) Before Capital Contributions	\$ (2,576,589)	\$ (4,701,178)	\$ (1,702,668)	\$ (4,721,020)	\$ 2,849,378
Debt Service Calculation Adjustments					
Add: Capital Contributions from Participants	\$ 1,131,930	\$ 0	\$ 0	\$ 0	\$ 0
Add: Interest Subsidies on 2010B Bonds	0	0	306,327	868,328	868,328
Add: Depreciation	4,803,549	4,792,037	4,426,113	4,482,820	4,495,971
Add: Interest Charges (Net)	3,411,937	3,918,240	4,833,300	6,440,678	4,968,459
Add: Use of Other Available Funds (1)	<u>0</u>	<u>1,096,214</u>	<u>0</u>	<u>0</u>	<u>0</u>
Net Regional Water Supply System Revenue Available for Debt Service	\$ 6,770,827	\$ 5,105,313	\$ 7,863,072	\$ 7,070,806	\$ 13,182,136
Debt Service on Outstanding Bonds	\$ 4,995,313	\$ 5,105,313	\$ 5,593,852	\$ 7,243,016	\$ 7,259,682

- (1) The City maintains and collects rates that, together with amounts on deposit in the Revenue Fund, are sufficient to pay the cost of operation and maintenance of the Water System and debt service and other costs. See Appendix A—"SUMMARY OF THE BOND ORDINANCE – Covenants with Bondowners." The City currently bills the Second Supply System partners based on actual expenses so occasionally there are timing differences. When this occurs within the Regional Water Supply System funds other Regional Water Supply System funds are used to adjust for these differences, as occurred in 2009.

Capital Improvement Program

The following table shows the 2013-2016 capital improvement program for the Regional System.

Regional Water Supply System 2013-2016 Capital Improvement Program (\$000)

Uses of Funds	2013	2014	2015	2016
Filtration Project	\$43,726	\$34,042	\$ 888	\$ 0
Major Water Treatment Equipment	56	56	56	56
Watershed Betterments	110	80	95	95
HCP Required Fish Habitat Projects	256	229	158	0
Additional Improvements	634	590	180	180
Total Uses	\$44,782	\$34,997	\$1,377	\$331

The Regional System capital improvements are expected to be funded from proceeds of the 2010 Bonds, cash payments from the Participants and State loans. The City has no plans for the issuance of Future Parity Bonds for the Regional System in the next several years.

THE CITY OF TACOMA WATER SYSTEM

Sources of Supply

The primary current source of supply for the Water System is a headworks diversion on the Green River approximately 30 miles east of the City, which is capable of supplying up to approximately 167 MGD to Tacoma Water and its Second Supply Project Participants. Water withdrawn at the headworks is chlorinated, fluoridated, treated with ozone, and pH adjusted before being introduced into Pipeline No. 1 and the Second Supply pipeline. Pipeline No. 1 transports up to 72 MGD through or near the cities of Enumclaw, Buckley, Bonney Lake, Puyallup, and other urbanized areas before discharging it into McMillin Reservoir. The Second Supply Pipeline transports up to 95 MGD through the cities of Black Diamond, Auburn, Federal Way, and Tacoma before discharging into Pipeline No. 4. The Green River diversion and Pipeline No. 1 were originally constructed in 1913. Over the years, nearly all of the original Pipeline No. 1 has been replaced and improvements to the diversion dam have occurred as a component of the Second Supply Project. The Second Supply Pipeline itself began delivering water in October 2005. The City is constructing a filtration project on the Green River. See “THE SECOND SUPPLY PROJECT—Filtration Treatment Project.”

The watershed, located above the diversion, consists of approximately 230 square miles of timbered and mountainous terrain. The U.S. Army Corps of Engineers (the “Army Corps”) constructed Howard Hanson Dam and Reservoir in 1961, forming the Eagle Gorge Reservoir, about three miles upstream from Tacoma Water’s Headworks Diversion Dam. The primary authorized purpose of the dam is to provide flood control for the Green River valley during the winter. Secondary authorized purposes include augmentation of low summer flows downstream of the dam, irrigation and storing water for municipal water supply purposes by Tacoma Water and its Second Supply Project partners. In 2012, the Army Corps completed the last dam safety rehabilitation project on the Howard Hanson Dam to mitigate damages from the January 2009 storm event and insure reliability of the dam in the future. The Army Corps was responsible for all dam safety costs. Projects implemented by the Army Corps include vertical and horizontal short path seepage dewatering wells, rock armoring and additional log booms.

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

In addition to the North Fork Wells, Tacoma Water has a number of wells within its service area that can be used to meet peak summer water demands. During a typical year, approximately 96% of the Water System’s water supply is from the Green River and 4% is from these wells. The following table summarizes the water supplied by source

during 2012 to meet the peak and average water requirements for Tacoma Water only, it does not include capacity or production values for the Second Supply Participants (see the “THE SECOND SUPPLY PROJECT”).

**Tacoma Water
2012 Sources of Supply of the Water System
(MGD)**

Source	Peak Capacity	Peak Day Production(2)	Average Production(2)
Surface Water Sources:			
Green River	111.58(1)	80.40	50.25
Groundwater Sources:			
Wells	53.30	14.89	0.49
Total Sources	164.88	95.29	50.74

- (1) Tacoma’s Peak Green River capacity is limited by pipe/plant capacity (see “Water Rights” discussion below), which is 72 MGD for Pipeline No. 1 plus 15/36 of 95 MGD (39.58 MGD) for the Second Supply Pipeline.
(2) 2012 Tacoma water use (excludes Second Supply water use by Kent, Covington and Lakehaven).

Tacoma Water’s 2012 demand forecast indicates that the Water System has sufficient water supply to meet projected demands for at least the next 50 years.

Water Rights

Tacoma Water has water rights on the Green River in excess of its current needs, which include a water right claim for 73 MGD (the “First Diversion Water Right”) plus a water permit for the Second Diversion Water Right of up to 15/36 of 65 MGD and is the source of supply for the Second Supply System, as further described in “THE SECOND SUPPLY PROJECT.” Second Diversion Water is conditional based on Green River flow and is, therefore, only available approximately 60% of the time on an annual basis. However, Second Diversion Water may be stored behind Howard Hanson Dam in the spring, and as the water is being stored at a rate not to exceed the Second Diversion water right rate, it may be withdrawn at a later date, at any rate. Therefore, when needed in the peak season, water from the Green River source may be used at a rate that is limited only by pipe/plant capacity.

Water rights for the Water System’s 25 wells, most of which are located within its water service area, total 115 MGD, with an installed pumping capacity of 67.2 MGD.

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

Endangered Species Act Compliance

In 1999, the National Marine Fisheries Service (“NMFS”) listed Puget Sound Chinook salmon as a threatened species. Subsequently, the U.S. Fish & Wildlife Service (“USFWS”) listed Puget Sound bull trout and Puget Sound steelhead as threatened species in 1999 and 2007, respectively. Pursuant to regulations, NMFS and USFWS have extended to these threatened species certain protections under the Endangered Species Act (“ESA”). These protections include a prohibition on “take,” which includes not only harm to members of the species, but also adverse effects or destruction of habitat. This caused water utilities throughout the region to assess their potential liability under the ESA. Tacoma Water has approached these issues within a multi faceted response strategy. First, it developed a Habitat Conservation Plan under Section 10 of the ESA, which was approved by the NMFS and USFWS in 2001, to protect its source of supply operations on the Green River. Acceptance of the Habitat

Conservation Plan led to the issuance of 50-year Incidental Take Permits from NMFS and the USFWS for Tacoma Water's water supply operations on the Green River. Although the protection of the threatened Chinook salmon was the incentive for plan development, the Habitat Conservation Plan eventually was approved to provide coverage for 32 aquatic and terrestrial species. This significantly reduces the risk to Tacoma Water that future water supply operations may be disrupted due to ESA issues. Second, Tacoma Water has adopted a "take" avoidance strategy for its field operations on the water distribution system. Section 4(d) of the ESA allows certain categories of activities defined by federal rule to be conducted without "take" liability. In 2001, Tacoma Public Utilities obtained coverage under this provision for a wide variety of its utility maintenance activities by adopting and implementing the federally approved "Regional Road Maintenance Endangered Species Act Program Guidelines." Tacoma Water has modified its operation to obtain coverage under this program for many of its day to day operations.

Water Quality and Treatment

Watershed monitoring and protection programs are critical to ensuring high water quality. Well managed, unpopulated watersheds minimize potential adverse effects on the water supply. Tacoma Water has a well organized watershed control program with inspectors who patrol the watershed to protect against any unauthorized entry. Tacoma Water owns approximately 11% of the watershed area including much of the land adjacent to the Green River and the Eagle Gorge Reservoir, located approximately three miles upstream from the Green River Headworks behind Howard Hanson Dam. Most of the land that is not owned by Tacoma Water is either U.S. Forest Service property or is owned by timber companies or the State Department of Natural Resources. There are no permanent residents living within the watershed boundaries. Tacoma Water, the timber companies, and the State Department of Natural Resources work cooperatively to ensure that timber harvesting and other activities comply with watershed control best management practices, thereby minimizing any potential adverse impacts on water quality. Tacoma Water has in place agreements with all of the timber companies to document their commitment to use these best management practices.

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

Tacoma Water adds ozone, chlorine, fluoride and sodium hydroxide (to raise the pH of the water) at the Green River Headworks. As discussed under "THE SECOND SUPPLY PROJECT—Filtration Treatment Project," new regulations require additional treatment of the Green River supply, and filtration has been selected to meet this requirement, and construction is well underway.

The water from Tacoma Water's wells is chlorinated before being introduced into the distribution system. The water quality is monitored on a regular basis in accordance with the requirements of the WSDOH and the U.S. Environmental Protection Agency ("U.S. EPA"). One of Tacoma Water's 30 wells is equipped with an air stripping tower to remove organic compound contamination, which was discovered during the early 1980s. This treatment maintains water quality by keeping water-borne contaminants to levels that are below the detectable limits. Contaminant levels in this groundwater source have also decreased as a result of the cleanup of the pollution source and significantly more rigorous land use controls within the City to protect groundwater. Tacoma Water is constructing a 40 million gallon per day groundwater treatment system at its Hood Street Reservoir to bolster compliance with regulations related to corrosivity of water to household plumbing, and to provide fluoridation of the groundwater. This work will be completed in 2013.

Water System Security

Tacoma Water, along with many other major water utilities, is taking increased steps to protect its water supply facilities and to prevent contamination of the water supply. Tacoma Water covered the last of its open basins in 2012. The basins were replaced with smaller covered reservoirs that will provide improved water quality as well as improved system security. The water quality leaving these new reservoirs has improved so much that a gas-rechlorination system has been eliminated, thus providing a decreased level of risk. Tacoma Water also has taken actions to secure the source of supply on the Green River through increased surveillance of watershed activities and closing additional areas to access. Security has been tightened regarding chemical deliveries to Tacoma Water

facilities, additional monitoring of water quality has been initiated, and security provisions are reviewed on an ongoing basis to assure adaptive reaction to any changes in threat status. A system wide analysis was completed in early 2003 with the support of a U.S. EPA grant. In 2013, Tacoma Water will be conducting a comprehensive all hazards vulnerability assessment. The intent is to identify Tacoma Water's vulnerabilities and develop remediation and resilience strategies to assure the continued safety and security of the Water System's assets. The assessment will include all of Tacoma Water's assets, including pump stations, wells, reservoirs, pressure reducing stations, interconnections, mains and appurtenances within its service area including the treatment facility and the new Filtration Project and in-town groundwater treatment facilities under construction. A separate cyber vulnerability assessment will be prepared under separate contract and incorporated into the all hazard analysis. The cyber assessment will evaluate the resilience of the corporate network, Supervisory Control And Data Acquisition (SCADA) system, and supporting infrastructure (telecommunications, microwave towers).

Water System Operations

Water Quality Section. The Water Quality Section of Tacoma Water is responsible for managing, operating and maintaining the Green River Headworks and watershed; assuring security and natural resource management of Tacoma Water lands including the watershed; providing for fish and wildlife habitat management, and installing, operating and maintaining water treatment equipment within the Water System. Water Quality Section personnel respond to all matters relating to water quality from the source to the customer, and monitor for contaminants as required by State and Federal regulations, and as required to meet customer needs and expectations. The section must assure compliance with the Federal Safe Drinking Water Act, as implemented through WSDOH.

The Water Quality Section operates the Green River intake for both water supply and an adult salmon fish trap and sort facility. Major water quality and regulatory drivers have led to initiatives for significant investments in water treatment infrastructure. A new chemical treatment plant began operation in 2005, providing capacity for the Second Supply Project, and significantly improved safety and reliability for the addition of chlorine, fluoride, and sodium hydroxide. In 2007, ozone treatment was added to enhance system disinfection, eliminate seasonal poor taste and odor in the natural water, and reduce the levels of regulated chlorinated organic compounds that form after chlorine disinfection. The cost of this treatment was included in the Second Supply Project Agreement. The addition of filtration is a responsibility of the Water Quality Section, and its future operation (beginning in 2014) will also be incorporated into this section. Tacoma Water has positioned itself with experienced personnel capable of transitioning into filtration operation.

In addition to the watershed and treatment operations associated with the Green River supply, the Water Quality Section operates and maintains disinfection treatment equipment for the groundwater supplies at three reservoir locations, and at several smaller groundwater sites. Tacoma is constructing a 40 million gallon per day groundwater treatment system at its Hood Street Reservoir to bolster treatment of groundwater at this location to assure future regulatory compliance. This work will be completed in 2013.

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

Tacoma Water's water transmission and distribution system consists of 141 miles of transmission pipelines ranging in size from 28 to 96 inches in diameter, 29 booster pump stations, 141 million gallons of reservoir storage, and 1,209 miles of distribution pipeline ranging in size from two to 24 inches in diameter. The distribution system includes a number of pressure zones; most are supplied by reducing the pressure gradient from the McMillin Reservoir and the remainder requires additional pumping of water to serve higher areas.

The storage available in the Water System is capable of supplying approximately three days at the average daily usage rate. To maintain better water quality within the Water System and as a result of other system changes, such as the construction of the Second Supply Project, storage was reduced by approximately 143 million gallons ("MG") from the historic storage amount to the amount of storage available in 2012.

Tacoma Water also has approximately 22 interties with 11 wholesale purveyor systems. Some of these interties are used to supply wholesale water to the systems on a regular basis and others are available for peak or emergency demands of these systems. Several of these interties are capable of providing Tacoma Water with a limited amount of emergency water supply.

Water Distribution Operations Section. The Water Distribution Operations Section is responsible for the operation and maintenance of the distribution system, which includes all of the distribution mains, hydrants, valves, service connections, meters, and other distribution system features. Tacoma Water has made significant improvements during the last few years in its operations and maintenance programs.

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

Water Distribution Engineering Section. The Water Distribution Engineering Section engineering staff supports the operation and maintenance crews as well as engineering for distribution main projects for both private development and Tacoma Water's capital improvement program. This staff evaluates and approves permits for Water System extensions including developer installed systems. The section prepares the design of developer systems rather than simply approving a system designed by the developer's engineer, which is the more common approach taken by water utilities. Past benchmarking and cost analysis has shown that this approach not only assures a timely response and quality design for the developer but is less expensive than hiring a private engineering firm. The Water Distribution Engineering Section has implemented a major water main replacement program. Beginning in 1995, Tacoma Water formalized this program and has since ramped up project funding for its replacement priorities as well as replacement work conducted in conjunction with public road projects and work by other jurisdictions. Subsequent cycles of evaluation of the program continue to refine the criteria for main replacement based on an evolving asset management structure.

Asset and Information Management Section. The Asset and Information Management section oversees implementation of Tacoma Water's infrastructure and information management initiatives as detailed in the Strategic Plan as well as ensures that the Strategic Plan implementation uses a balanced scorecard throughout the organization. This staff manages Tacoma Water's asset management and performance management programs and provides hydraulic modeling, GIS, SAP and other technology support. Responsibilities also including system, strategic, and technology plan development for Tacoma Water.

Tacoma Water continues to prioritize its asset management program. The physical infrastructure that delivers water to customers is extensive and effective management is essential to get the most out of the investments and optimize operation, maintenance and capital expenditures. An economic model was developed and enhanced in 2012 to allow multiple assets to be brought together to analyze a capital project's benefit. This tool informed water main replacement decision making to support capital improvement program management. Tacoma Water also uses business case evaluations to evaluate and justify spending decisions. Comparing the lifecycle costs of alternatives, while considering the financial, social and environmental risks and benefits, provides Tacoma Water with optimal solutions. That process is used to make a variety of capital, operational and maintenance decisions, from vehicle replacements to work group relocations.

Rates and Financial Planning Section. The Rates and Financial Planning Section is responsible for managing financial risk through the development of financial policies, rates and charges, long-term financial plans, capital funding strategies, demand forecasts, and water supply agreements and strategies. This section is also responsible for managing the development of the utility's budget, and providing certain financial performance reporting to internal and external stakeholders. This section is expected to represent Tacoma Water in key financial matters, and make recommendations to the Superintendent and Director of Utilities with respect to agreements that have critical financial features.

State Department of Health/U.S. Environmental Protection Agency Requirements. Tacoma Water must comply with the requirements of the rules and regulations promulgated by the U.S. EPA pursuant to the Safe Drinking Water Act. WSDOH is delegated by U.S. EPA to administer these regulations in the State. In addition, WSDOH

has rules and regulations for the design and operation of water systems. WSDOH provides oversight of water systems including reviews, approvals, and monitoring of performance.

Tacoma Water has a Comprehensive Water Plan (the “Plan”), which was approved by WSDOH in 2008 and is required to be updated by January 23, 2014. The Plan includes projections of future water demand requirements for several scenarios and presents an Integrated Resource Development Strategy for meeting future water demands. The Plan sets forth Tacoma Water’s proposed program of supply development and system capital improvements. It also describes the financial plan for funding these improvements and includes required sections on emergency response and routine operations. Because the Plan as a whole is only periodically updated, Tacoma Water updates key components of the Plan more frequently. These updates include a renewed water demand forecast, an updated capital facilities plan, and the utility strategic plan.

Service Area

Tacoma Water’s current service area consists of the City and the urbanized areas of Pierce and south King Counties. The area extends from the northerly boundary of Lakewood Water District and Parkland Light and Water Company in the south, northward to the City of Federal Way in King County. The eastern boundary is the foothills of the Cascade Mountains. The western boundary is Puget Sound. Water service outside the City limits is provided under franchises granted by both Pierce County and King County, and the cities of Puyallup, Federal Way, Lakewood, Fircrest and University Place. Approximately 36% of Tacoma Water’s residential service is outside of the City limits.

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

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

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

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

Currently, wholesale service is a small part of Tacoma Water’s operations. Less than 3.5% of billed revenue is derived from that source, but it is expected to grow as additional water rights become more difficult to obtain by nearby growing communities that rely on limited ground water supplies.

The map under “THE SECOND SUPPLY PROJECT—Project Participants” shows Tacoma Water’s service area.

Customers, Water Sales, and Rates

Tacoma Water serves residential, commercial, industrial and wholesale customers, and charges cost of service rates by customer class. In 2012, revenues were attributed 65.5% to residential service, and 27% to commercial and industrial service, including the Simpson Tacoma Kraft Company (“Simpson”). The remaining approximately 7.5% was accounted for by service to municipal and other governmental customers and to wholesale customers.

Simpson is the largest customer of Tacoma Water and accounted for approximately 8.5% of total water sales revenue in 2011 and in 2012. In 2012, the ten largest customers combined accounted for 14.9% of total water sales revenue.

Special Contracts and Wholesale Agreements

The City and Simpson executed a 10-year retail contract for industrial water supply in 2006, which includes options to extend or renegotiate upon its expiration in 2015. The parties have started negotiations on such extension. The contract currently provides that the City will furnish 15.9 MGD to Simpson on a uniform basis, 24 hours a day. Pursuant to the contract, Simpson would not be required to take water if its paper mill operations shut down, but would be required to pay liquidated damages.

Tacoma Water has agreements with a number of regional water purveyors to provide wholesale service, and most recently executed an agreement with the City of Auburn to provide one MGD of wholesale supply. A number of regional utilities, including the City of Auburn, have expressed an interest in increasing wholesale purchases, and Tacoma Water is actively engaged with these utilities in exploring options for expanded wholesale service.

Agreement with Cascade Water Alliance

In 2005, Tacoma Water entered into an agreement with the Cascade Water Alliance (“Cascade”), a regional wholesale water supplier, that entitled Cascade to a permanent supply of four MGD of water (average daily demand) each year, and an additional guaranteed reserved supply of six MGD (average daily demand) through 2026, declining to one MGD (average daily demand) in 2030 (the “Additional Supply”), and discontinuing thereafter. Tacoma Water entered into an Amended and Restated Agreement for the Sale of Wholesale Water with Cascade effective December 31, 2012, that specifies a fixed payment stream from Cascade to Tacoma Water from 2012 through 2042. It also enables Cascade to transfer capacity that was previously purchased from Tacoma Water to the Cities of Auburn, Bonney Lake, Buckley, and Sumner (the “Four Cities”) over a period of five years, after which Tacoma Water will make such capacity available for direct purchase to the Four Cities until December 31, 2026. If such capacity transfer occurs, a wholesale water agreement will be negotiated between Tacoma Water and one or more of the Four Cities, and all water sales revenues will be received by Tacoma Water. Tacoma Water will receive a fixed payment stream, totaling \$119.7 million, from Cascade in amounts ranging from \$5,000,000 to \$6,863,929 between 2012 and 2029, inclusive, and ranging from \$1,000,000 to \$1,268,242 between 2030 and 2042, inclusive.

Water Rates

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

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

The 2013 and 2014 water rates were adopted by the City Council on February 26, 2013 and are scheduled to be implemented on April 1, 2013 and April 1, 2014. The changes resulted in an average annual increase in water charges of approximately 6% per year. Rate increases since 2005 are summarized in the following table.

**Tacoma Water
Rate Increases**

Year	Average Annual Increase
2005	8.0%
2006	8.0
2007	7.5
2008	7.5
2009	3.9
2010	2.9
2011	5.2
2012	5.2
2013	6.0
2014	6.0

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

**Tacoma Water
Current Water Rates and Charges
(as of April 1, 2013)**

Size of Meter (inches)	Customer Charge Per Month	
	Inside City Limits	Outside City Limits
5/8	\$ 17.78	\$ 21.34
3/4	26.67	32.00
1	44.45	53.34
1-1/2	88.90	106.68
2	142.24	170.69
3	266.70	320.04
4	444.50	533.40
6	889.00	1,066.80
8	1,422.40	1,706.88
10	2,044.70	2,453.64
12	3,000.38	3,600.45

Consumption Up to and Including:

Residential

Each 100 cubic feet of consumption

October through May.....

\$ 1.450 \$ 1.740

First 500 cubic feet of consumption June through

September

1.450 1.740

Each 100 cubic feet of consumption over 500 cubic

feet June through September.....

1.813 2.176

Commercial and Industrial

General

1.600 1.920

Large Volume (over 65,000 cubic feet annually)

1.425 1.710

Parks and Irrigation

For each 100 cubic feet.....

2.200 2.640

(1) ccf = 100 cubic feet

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

2013 Comparison of Average Monthly Water Bills

UTILITY	5/8" RESIDENTIAL (10 ccf/month)	2" COMMERCIAL (150 ccf/month)
Tacoma Water (1)	\$ 32.28	\$ 382.24
Major Regional Water Systems:		
City of Everett, WA	30.25	341.40
Portland, OR Water Bureau(2)	43.39	508.33
Seattle Public Utilities	58.50	698.75
San Francisco, CA	59.50	842.20
Neighboring Water Systems:		
City of Bellevue, WA	55.96	654.34.
City of Kent, WA	46.23	651.24
City of Puyallup, WA	29.27	329.49
Covington Water District, WA	55.85	595.98
Lakehaven Utility District, WA	25.60	307.86

(1) Tacoma rates effective as of April 1, 2013.

(2) Billed quarterly. Rates are greater if billed monthly or bimonthly.

Source: Individual Utilities. Off-peak season rate (inside city where applicable).

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

The following table shows annual funds recognized as revenues from SDCs from 2005 through 2012. In 2009, Tacoma Water deposited approximately \$35 million of SDCs into the Rate Stabilization Account, and consequently, these SDCs are not reflected in the table.

Tacoma Water Annual SDC Revenue

Year	SDC Recognized Revenue
2005	\$ 5,769,592
2006	12,688,488
2007	2,953,984
2008	1,754,475
2009	404,451
2010	5,772,945
2011	4,834,803
2012	1,810,178

Public Fire Protection Costs

In response to an October 2008 Washington State Supreme Court ruling that public fire protection costs are the responsibility of general government, Tacoma Water removed these costs from the water rates effective January 19, 2009. Public fire protection costs were invoiced to the cities and counties served by Tacoma. Representatives from

the larger entities (Pierce County and the cities of University Place and Federal Way) declined to pay these costs. Tacoma Water filed suit in Pierce County Superior Court to have its legal rights determined. The defendants moved the case to King County Superior Court, where a judge entered an order on summary judgment ruling that the hydrant costs in areas with franchise agreements must be incorporated back into the utility rates. The City appealed the decision to the Washington State Supreme Court, which affirmed the outcome on January 23, 2012. Tacoma Water is now collecting these costs through fixed monthly charges to the ratepayers in these jurisdictions, both prospectively and retrospectively, and has refunded any funds received from local governments for these services. Tacoma Water bills the City, and not customers directly, for service provided within the City.

Historical Operating Results

The following table shows Tacoma Water's customer accounts and water sales for the years 2008 through 2012.

Tacoma Water
Historical Number of Customers and Water Sales

	2008	2009	2010	2011	2012
Customer Accounts (Average)					
Residential	89,680	90,677	90,818	90,447	90,090
Commercial & Industrial Service	5,466	5,636	5,663	5,646	5,612
Simpson Tacoma Kraft ⁽¹⁾	1	1	1	1	1
Municipal	251	209	213	203	206
Other Public Buildings	442	441	425	420	406
Other Utilities	18	18	17	17	18
Total Customer Accounts	95,858	96,982	97,137	96,734	96,333
Water Sales (ccf)⁽²⁾					
Residential	11,018,505	11,566,425	10,360,619	10,314,437	10,408,609
Commercial & Industrial Service	3,963,159	3,806,353	3,608,517	3,339,309	3,341,364
Simpson Tacoma Kraft ⁽¹⁾	7,777,754	7,386,109	7,724,770	7,823,129	7,835,544
Municipal	97,056	102,179	88,948	105,286	94,432
Other Public Buildings	692,616	732,647	575,331	655,814	611,332
Other Utilities	851,377	1,127,243	871,563	836,657	910,332
Total Water Sales	24,400,467	24,720,956	23,229,748	23,074,632	23,201,613

(1) Simpson Tacoma Kraft is a pulp and paper mill with contracted annual usage of 15.9 MGD. See "THE CITY OF TACOMA WATER SYSTEM—Special Contracts and Wholesale Agreements."

(2) ccf = 100 cubic feet.

Source: Annual Tacoma Water financial reports.

The following table shows selected historical revenues and expenses for Tacoma Water for the years 2008 through 2012. The following table is based on consolidated audited financial statements that include Tacoma Water and the Second Supply System for the period between 2008 and 2012.

**Tacoma Water
Historical Operating Results**

	2008	2009	2010	2011	2012
Operating Revenues (1)					
Residential and Domestic	\$ 34,592,712	\$ 36,643,366	\$ 35,453,730	\$ 36,682,278	\$ 38,685,705
Commercial & Industrial	8,978,703	9,659,078	10,049,782	10,101,108	10,620,950
Special Rate—Simpson	4,371,527	4,153,327	3,798,922	4,774,237	5,031,760
Municipal (2)	349,722	380,267	364,357	400,322	383,385
Other Public Bldgs. & Grounds (3)	1,680,603	1,861,111	1,702,656	1,815,865	1,909,782
Unbilled (4)	417,145	187,966	(648,438)	478,594	416,986
Sales to Other Water Utilities	<u>1,251,815</u>	<u>1,776,686</u>	<u>1,530,116</u>	<u>1,625,163</u>	<u>2,090,430</u>
Total Water Sales	\$ 51,642,227	\$ 54,661,801	\$ 52,251,125	\$ 55,877,567	\$ 59,138,998
Other Operating Revenues (5)	<u>5,382,313</u>	<u>9,331,955</u>	<u>10,735,630</u>	<u>9,526,467</u>	<u>21,541,733</u>
Total Operating Revenue	\$ 57,024,540	\$ 63,993,756	\$ 62,986,755	\$ 65,404,034	\$ 80,680,731
Operating Expenses (1)					
Operating & Maintenance	\$ 33,387,663	\$ 34,055,463	\$ 34,453,742	\$ 32,821,611	\$ 32,602,452
Depreciation	13,016,544	13,845,799	14,474,964	14,389,681	15,262,686
Taxes (6)	<u>2,881,877</u>	<u>3,093,311</u>	<u>3,142,772</u>	<u>3,106,516</u>	<u>3,485,243</u>
Total	\$ 49,286,084	\$ 50,994,573	\$ 52,071,478	\$ 50,317,808	\$ 51,350,381
Net Operating Income (Loss)	\$ 7,738,456	\$ 12,999,183	\$ 10,915,277	\$ 15,086,226	\$ 29,330,350
Non-Operating Revenue (Expenses) (1)					
Other Income	\$ 61,265	\$ 497,331	\$ 33,795	\$ (12,371)	\$ 288,183
Interest Income	3,730,407	1,955,385	2,370,993	3,141,374	2,320,753
Gain from Disposition of Property	0	26,100	0	0	0
Interest Charges (Net)	<u>(8,406,264)</u>	<u>(9,076,156)</u>	<u>(15,175,660)</u>	<u>(15,018,374)</u>	<u>(14,696,096)</u>
Total Non-Operating Revenue (Expense)	\$ (4,614,592)	\$ (6,597,340)	\$ (12,770,872)	\$ (11,889,371)	\$ (12,087,160)
Net Income (Loss) Before Capital Contributions (1)	\$ 3,123,864	\$ 6,401,843	\$ (1,855,595)	\$ 3,196,855	\$ 17,243,190
Less: Regional System Net Income (Loss) Before Capital Contributions (7)	<u>(2,576,589)</u>	<u>(4,701,178)</u>	<u>(1,702,668)</u>	<u>(4,721,020)</u>	<u>2,849,378</u>
Net Tacoma Water Net Income (Loss) Before Capital Contributions	\$ 5,700,453	\$ 11,103,021	\$ (152,927)	\$ 7,917,875	\$ 14,393,812
Debt Service Calculation Adjustments (8)					
Less: Restricted Income	\$ (623,867)	\$ (273,694)	\$ (145,331)	\$ (341,378)	\$ (224,988)
Less: Gain from Disposition of Property	0	(26,100)	0	0	0
Add: Interest Subsidies on 2010B Bonds	0	244,683	2,048,805	2,972,443	2,972,439
Add: Depreciation	8,212,995	9,053,762	10,048,851	9,906,861	10,766,715
Add: Interest Charges (Net)	4,323,860	5,157,916	10,342,360	8,577,696	9,727,637
Add: SDC Revenues (9)	<u>1,754,475</u>	<u>404,451</u>	<u>5,772,945</u>	<u>4,834,803</u>	<u>1,810,178</u>
Net Tacoma Water Revenue Available for Debt Service	\$ 19,367,916	\$ 25,664,039	\$ 27,914,703	\$ 33,868,300	\$ 39,445,793
Debt Service on Outstanding Bonds (10)	\$ 10,438,208	\$ 10,432,133	\$ 16,198,876	\$ 18,689,644	\$ 18,751,491
Debt Service Coverage	1.86x	2.46x	1.72x	1.81x	2.10x

(1) Includes Regional System operating results. See "Regional Water Supply System Historical Operating Results."

(2) Retail sales to City facilities.

(3) Retail sales to governmental entities other than the City.

(4) Accrued revenue for water service provided and not billed in the current year.

(5) Includes Kent, Covington and Lakehaven payments for Regional System, as well as Public Fire Protection fees and Cascade Water Alliance fees.

(6) Excludes City gross earnings tax, which is payable after debt service.

(7) Includes all Regional System revenues and expenses, including depreciation before Capital Contributions. See "Net Income (Loss) Before Capital Contributions" column in the "Regional Water Supply System Historical Operating Results" table.

(8) All adjustments exclude Second Supply System.

(9) Includes SDC revenue as recognized and excludes deferred SDC revenue. See "SECURITY FOR THE BONDS"

(10) Includes debt service on Tacoma Water parity bonds only.

Capital Improvement Program

Tacoma Water biennially prepares a ten-year business plan, which includes capital improvements, additions and renovations to the Water System necessary to address engineering recommendations, regulatory requirements and water quality standards and to provide for present and projected future customer needs. From this projection of need, Tacoma Water derives its Capital Improvement Program for the Water System. This program is an element of the City's Growth Management Act ("GMA") Comprehensive Plan, which contains a six-year projection of projects and is updated annually. The following table summarizes Tacoma Water's 2013-2016 Capital Improvement Program.

Tacoma Water 2013-2016 Capital Improvement Program (\$000)

Uses of Funds	2013	2014	2015	2016
General Plant	\$ 4,745	\$ 1,193	\$ 7,279	\$ 5,679
Water Supply	8,107	8,939	4,422	8,791
Water Quality	3,373	605	520	520
Water Distribution	13,047	13,048	14,178	14,378
Second Supply System Projects(1)	52,954	41,326	1,508	255
Environ Stewardship/Conservation	1,000	250	250	2,375
Total Uses	\$ 83,226	\$ 65,361	\$ 28,157	\$ 31,998

(1) Includes Tacoma Water's First Diversion and Second Supply System Filtration Treatment Project funding obligations.

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

LITIGATION CONCERNING THE BONDS AND TACOMA WATER

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

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

TAX MATTERS

Tax Exemption

Exclusion From Gross Income. In the opinion of Bond Counsel, under existing federal law and assuming compliance with applicable requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issue date of the Bonds, interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals.

Continuing Requirements. The City is required to comply with certain requirements of the Code after the date of issuance of the Bonds in order to maintain the exclusion of the interest on the Bonds from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Bond proceeds and the facilities financed or refinanced with Bond proceeds, limitations on investing gross proceeds of the Bonds in higher yielding investments in certain circumstances, and the requirement to comply with the arbitrage rebate requirement to the extent applicable to the Bonds. The City has covenanted in the Bond Ordinance to comply with

those requirements, but if the City fails to comply with those requirements, interest on the Bonds could become taxable retroactive to the date of issuance of the Bonds. Bond Counsel has not undertaken and does not undertake to monitor the City's compliance with such requirements.

Corporate Alternative Minimum Tax. While interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, under Section 55 of the Code, tax exempt interest, including interest on the Bonds, received by corporations is taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations (as defined for federal income tax purposes). Under the Code, alternative minimum taxable income of a corporation will be increased by 75% of the excess of the corporation's adjusted current earnings (including any certain tax exempt interest) over the corporation's alternative minimum taxable income determined without regard to such increase. A corporation's alternative minimum taxable income, so computed, that is in excess of an exemption of \$40,000, which exemption will be reduced (but not below zero) by 25% of the amount by which the corporation's alternative minimum taxable income exceeds \$150,000, is then subject to a 20% minimum tax.

A small business corporation is exempt from the corporate alternative minimum tax for any taxable year beginning after December 31, 1997, if its average annual gross receipts during the three-taxable-year period beginning after December 31, 1993, did not exceed \$5,000,000, and its average annual gross receipts during each successive three-taxable-year period thereafter ending before the relevant taxable year did not exceed \$7,500,000.

Tax on Certain Passive Investment Income of S Corporations. Under Section 1375 of the Code, certain excess net passive investment income, including interest on the Bonds, received by an S corporation (a corporation treated as a partnership for most federal tax purposes) that has Subchapter C earnings and profits at the close of the taxable year may be subject to federal income taxation at the highest rate applicable to corporations if more than 25% of the gross receipts of such S corporation is passive investment income.

Foreign Branch Profits Tax. Interest on the Bonds may be subject to the foreign branch profits tax imposed by Section 884 of the Code when the Bonds are owned by, and effectively connected with a trade or business of, a United States branch of a foreign corporation.

Possible Consequences of Tax Compliance Audit. The Internal Revenue Service (the "IRS") has established a general audit program to determine whether issuers of tax-exempt obligations, such as the Bonds, are in compliance with requirements of the Code that must be satisfied in order for interest on those obligations to be, and continue to be, excluded from gross income for federal income tax purposes. Bond Counsel cannot predict whether the IRS would commence an audit of the Bonds. Depending on all the facts and circumstances and the type of audit involved, it is possible that commencement of an audit of the Bonds could adversely affect the market value and liquidity of the Bonds until the audit is concluded, regardless of its ultimate outcome.

Certain Other Federal Tax Consequences

Bonds Not "Qualified Tax Exempt Obligations" for Financial Institutions. Section 265 of the Code provides that 100% of any interest expense incurred by banks and other financial institutions for interest allocable to tax exempt obligations acquired after August 7, 1986, will be disallowed as a tax deduction. However, if the tax exempt obligations are obligations other than private activity bonds, are issued by a governmental unit that, together with all entities subordinate to it, does not reasonably anticipate issuing more than \$10,000,000 of tax exempt obligations (other than private activity bonds and other obligations not required to be included in such calculation) in the current calendar year, and are designated by the governmental unit as "qualified tax exempt obligations," only 20% of any interest expense deduction allocable to those obligations will be disallowed.

The City is a governmental unit that, together with all subordinate entities, reasonably anticipates issuing more than \$10,000,000 of tax exempt obligations (other than private activity bonds and other obligations not required to be included in such calculation) during the current calendar year and has not designated the Bonds as "qualified tax-exempt obligations" for purposes of the 80% financial institution interest expense deduction. Therefore, no interest expense of a financial institution allocable to the Bonds is deductible for federal income tax purposes.

Original Issue Premium. The Bonds have been sold at prices reflecting original issue premium ("Premium Bonds"). An amount equal to the excess of the purchase price of a Premium Bond over its stated redemption price

at maturity constitutes premium on such Premium Bond. A purchaser of a Premium Bond must amortize any premium over such Premium Bond's term using constant yield principles, based on the purchaser's yield to maturity. The amount of amortizable premium allocable to an interest accrual period for a Premium Bond will offset a like amount of qualified stated interest on such Premium Bond allocable to that accrual period, and may affect the calculation of alternative minimum tax liability described above. As premium is amortized, the purchaser's basis in such Premium Bond is reduced by a corresponding amount, resulting in an increase in the gain (or decrease in the loss) to be recognized for federal income tax purposes upon a sale or disposition of such Premium Bond prior to its maturity. Even though the purchaser's basis is reduced, no federal income tax deduction is allowed. Purchasers of Premium Bonds, whether at the time of initial issuance or subsequent thereto, should consult with their own tax advisors with respect to the determination and treatment of premium for federal income tax purposes and with respect to state and local tax consequences of owning such Premium Bonds.

Reduction of Loss Reserve Deductions for Property and Casualty Insurance Companies. Under Section 832 of the Code, interest on the Bonds received by property and casualty insurance companies will reduce tax deductions for loss reserves otherwise available to such companies by an amount equal to 15% of tax exempt interest received during the taxable year.

Effect on Certain Social Security and Retirement Benefits. Section 86 of the Code requires recipients of certain Social Security and certain Railroad Retirement benefits to take receipts or accruals of interest on the Bonds into account in determining gross income.

Other Possible Federal Tax Consequences. Receipt of interest on the Bonds may have other federal tax consequences as to which prospective purchasers of the Bonds may wish to consult their own tax advisors.

Potential Future Federal Tax Law Changes. From time to time, there are legislative proposals in Congress which, if enacted, could require changes in the description of federal tax matters relating to the Bonds set forth above or adversely affect the market value of the Bonds. It cannot be predicted whether future legislation may be proposed or enacted that would affect the federal tax treatment of interest received on the Bonds. Prospective purchasers of the Bonds should consult with their own tax advisors regarding any proposed or pending legislation that would change the federal tax treatment of interest on the Bonds.

DESCRIPTION OF RATINGS

Moody's Investors Service Inc. and Standard & Poor's Ratings Services, a business unit within Standard & Poor's Financial Services LLC, have assigned ratings of "Aa2" and "AA," respectively, to the Bonds. Ratings were applied for by the City and certain information was supplied by the City to the rating agencies to be considered in evaluating the Bonds. The ratings reflect only the views of the rating agencies and an explanation of the significance of the ratings may be obtained from the rating agencies. There is no assurance that the ratings will be retained for any given period of time or that the ratings will not be revised downward, suspended, or withdrawn entirely by the rating agencies if, in their judgment, circumstances so warrant. Any such downward revision, suspension, or withdrawal of the ratings would be likely to have an adverse effect on the market price of the Bonds.

UNDERWRITING

The Bonds are being purchased by Goldman, Sachs & Co, New York, New York, at an aggregate price of \$75,206,585, which represents the principal amount of the Bonds, plus an original issue premium of \$10,558,096, less an underwriter's discount of \$146,511. After the initial public offering, the public offering prices may be varied from time to time.

FINANCIAL ADVISORS

SDM Advisors Inc., Mount Vernon, Washington and A. Dashen & Associates, Bellevue, Washington have acted as financial advisors to Tacoma Water in connection with the issuance of the Bonds. The financial advisors have not audited, authenticated, or otherwise verified the information set forth in this Official Statement or the other information available from Tacoma Water with respect to the appropriateness, accuracy, and completeness of the disclosure of such information, and the financial advisors make no guarantee, warranty, or other representation on any matter related to such information. SDM Advisors Inc. and A. Dashen & Associates are independent financial

advisory and consulting organizations and are not engaged in the business of underwriting, marketing, or trading of municipal securities or any other negotiable instruments.

APPROVAL OF COUNSEL

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

CERTAIN INVESTMENT CONSIDERATIONS

This section contains certain additional considerations and is not meant to be comprehensive or definitive.

Initiative and Referendum

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

Local Measures. Under the City Charter, voters may initiate City Charter amendments and local legislation, including modifications to existing legislation, and through referendum may prevent legislation passed by the City Council from becoming law; provided that ordinances authorizing bonds, adopting annual budgets, or making appropriations are not subject to referendum as well as ordinances not subject to referendum under state law (including rate ordinances).

Limitations on Remedies

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

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

Municipal Bankruptcies

A municipality such as the City must be specifically authorized under State law in order to seek relief under Chapter 9 of the U.S. Bankruptcy Code (the "Bankruptcy Code"). A creditor, however, cannot bring an involuntarily bankruptcy proceeding against a municipality, including the City. The Federal bankruptcy courts have

broad discretionary powers under the Bankruptcy Code. Chapter 39.64 RCW, entitled the “Taxing District Relief Act,” permits any “taxing district” (defined to include cities) to voluntarily petition for relief under the Bankruptcy Code.

The legal opinion of Bond Counsel regarding the validity of the Bonds will be qualified by reference to bankruptcy, reorganization, insolvency, fraudulent conveyance, moratorium and other similar laws affecting the rights of creditors generally, and by general principles of equity. See Appendix E.

Seismic and Other Considerations

Tacoma Water’s facilities are in an area of seismic activity, with frequent small earthquakes and occasional moderate and larger earthquakes. The City can give no assurance regarding the effect of an earthquake, a tsunami from seismic activity in the State or in other areas, a volcano or other natural disaster or that proceeds of insurance carried by the Department would be sufficient, if available, to rebuild and reopen Tacoma Water’s facilities or that Tacoma Water facilities or surrounding facilities and infrastructure could or would be rebuilt and reopened in a timely manner following a major earthquake or other natural disaster.

CONTINUING DISCLOSURE UNDERTAKING

Basic Undertaking to Provide Annual Financial Information and Notice of Listed Events. To meet the requirements of paragraph (b)(5) of United States Securities and Exchange Commission (“SEC”) Rule 15c2-12 (“Rule 15c2-12”), as applicable to a participating underwriter for the Bonds, the City will undertake (the “Undertaking”) for the benefit of holders of the Bonds to provide or cause to be provided, either directly or through a designated agent, to the Municipal Securities Rulemaking Board (“MSRB”) in an electronic format as prescribed by the MSRB, accompanied by identifying information as prescribed by the MSRB: (a) annual financial information and operating data of the type included in this Official Statement as generally described below (“annual financial information”); and (b) timely notice (not in excess of ten business days after the occurrence of the event) of the occurrence of any of the following events with respect to the Bonds: (i) principal and interest payment delinquencies; (ii) non payment related defaults, if material; (iii) unscheduled draws on debt service reserves reflecting financial difficulties; (iv) unscheduled draws on credit enhancements reflecting financial difficulties; (v) substitution of credit or liquidity providers, or their failure to perform; (vi) adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notice of Proposed Issue (IRS Form 5701 – TEB) or other material notices or determinations with respect to the tax status of the Bonds; (vii) modifications to rights of holders of the Bonds, if material; (viii) Bond calls (other than scheduled mandatory redemptions of Term Bonds), if material, and tender offers; (ix) defeasances; (x) release, substitution, or sale of property securing repayment of the Bonds, if material; (xi) rating changes; (xii) bankruptcy, insolvency, receivership or similar event of the City, as such “Bankruptcy Events” are defined in Rule 15c2-12; (xiii) the consummation of a merger, consolidation, or acquisition involving the City or the sale of all or substantially all of the assets of the City, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and (xiv) appointment of a successor or additional trustee or the change of name of a trustee, if material.

The City also will provide to the MSRB timely notice of a failure by the City to provide required annual financial information on or before the date specified below.

Type of Annual Financial Information Undertaken to be Provided. The annual financial information that the City undertakes to provide will consist of (i) annual financial statements showing ending fund balances for the Water System, including the Regional System, prepared (except as otherwise noted therein) in accordance with the Budget Accounting and Reporting System presented by the Washington State Auditor pursuant to RCW 43.09.200 (or any successor statute), which statements will not be audited, except that if and when audited financial statements are otherwise prepared and available to the City they will be provided; (ii) principal amount of outstanding Parity Bonds and debt service coverage; and (iii) list of current Participants if other than the Participants at the date of the Bond Ordinance; and will be provided to the MSRB not later than the last day of the ninth month after the end of each fiscal year of the City (currently, a fiscal year ending December 31 as such fiscal year may be changed as required or permitted by State law, commencing with the City’s fiscal year ending December 31, 2013).

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

Amendment of Undertaking. The Undertaking is subject to amendment after the primary offering of the Bonds without the consent of any holder of any Bond, or of any broker, dealer, municipal securities dealer, participating underwriter, rating agency, or the MSRB, under the circumstances and in the manner permitted by Rule 15c2-12.

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

Termination of Undertaking. The City's obligations under the Undertaking shall terminate upon the legal defeasance of all of the Bonds. In addition, the City's obligations under the Undertaking shall terminate if those provisions of Rule 15c2-12 which require the City to comply with the Undertaking become legally inapplicable in respect of the Bonds for any reason, as confirmed by an opinion of nationally recognized bond counsel or other counsel familiar with federal securities laws delivered to the City, and the City provides timely notice of such termination to the MSRB.

Remedy for Failure to Comply with Undertaking. If the City or any other obligated person fails to comply with the Undertaking, the City will proceed with due diligence to cause such noncompliance to be corrected as soon as practicable after the City learns of that failure. No failure by the City or other obligated person to comply with the Undertaking will constitute a default in respect of the Bonds. The sole remedy of any Beneficial Owner of a Bond will be to take such actions as that holder deems necessary, including seeking an order of specific performance from an appropriate court, to compel the City or other obligated person to comply with the Undertaking.

Prior Compliance with Continuing Disclosure Undertakings

The City has entered into previously continuing disclosure undertakings under Rule 15c2-12. On February 17, 2013, the City filed missing information regarding assessments levied, collected and uncollected for the years 2007 through 2011 in connection with its Consolidated Local Improvement District No. 60 Bonds. The City believes it is currently in compliance with its previous undertakings.

Other Obligated Persons

The City agrees to provide or cause to be provided, either directly or through a designated agent, to the MSRB, as designated by the SEC, in accordance with Rule 15c2-12, in electronic format as prescribed by the MSRB accompanied by identifying information as prescribed by the MSRB, with respect to each "Obligated Person," such Obligated Person's audited financial statements prepared in accordance with generally accepted accounting principles; provided, that if such Obligated Person's financial statements are not yet available, the City shall provide unaudited financial statements in substantially the same format, and audited financial statements when they become available. "Obligated Person" means any person or entity which, at the time, is obligated directly or indirectly by contract, generally or through an enterprise, fund or account, to make payment in the then current or any succeeding Fiscal Year to be applied to pay at least 10% of the aggregate amount of principal of and interest scheduled to become due in such year on the Bonds. Kent and Covington are currently "Obligated Persons" with respect to the Bonds.

MISCELLANEOUS

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

APPENDIX A

SUMMARY OF THE BOND ORDINANCE

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

Definitions

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

“Accreted Value” means, with respect to any Capital Appreciation Bond, as of the time of calculation, the sum of the amount representing the initial principal amount of such bond plus interest accrued, compounded thereon as of the most recent compounding date. With respect to any particular Payment Date, the Accreted Value is the amount set forth on the Accreted Value Table included as part of the form of Capital Appreciation Bond. In the event the Accreted Value of any Capital Appreciation Bond is required to be determined as of a date other than the Payment Date, the Accreted Value shall be determined by adding to the Accreted Value for the next preceding Payment Date the product obtained by multiplying (a) the difference between the Accreted Value for the next Payment Date and the Accreted Value for the next preceding Payment Date, by (b) the ratio obtained by dividing by 180 the number of days elapsed since the next preceding Payment Date (calculated on the basis of a 360-day year of 12 30-day months).

“Accreted Value Table” means the Accreted Value Table printed on the Capital Appreciation Bonds reflecting the Accreted Value of such Bonds as of any Payment Date.

“Annual Debt Service” means the amount required to be paid in a calendar year for (1) interest due in such calendar year on all outstanding Parity Bonds (excluding the accrued interest paid to the City upon issuance of Parity Bonds), (2) principal of all outstanding Serial Bonds due in such calendar year, and (3) any Mandatory Amortization Installment for such calendar year. If on such date of calculation the interest rate on any Variable Interest Rate Bonds shall then be fixed for a specified period, including pursuant to a Payment Agreement, the interest rate used for such specified period for the purpose of the foregoing calculation shall be such actual interest rate. For purposes of computing Annual Debt Service on any Parity Bonds which constitute Balloon Indebtedness, it shall be assumed that the principal of such Balloon Indebtedness, together with interest thereon at the rate applicable to such Balloon Indebtedness, shall be amortized in equal annual installments over a term equal to the lesser of (1) 25 years or (2) the average weighted useful life (expressed in years and rounded to the next highest integer) of the properties and assets constituting the project (if any) financed out of the proceeds of such Balloon Indebtedness. The interest on Parity Bonds designated as Build America Bonds or similar bonds, including the 2010B Bonds, for purposes of calculating the Annual Debt Service for purposes of the Reserve Requirement, shall be based on the net interest after the 35% federal direct payment or such other federal direct payment to be received for the 2010B Bonds and Future Parity Bonds.

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

“Balloon Indebtedness” means any series of Parity Bonds more than 25% of the principal of which, in accordance with the terms of such Parity Bonds, is due and payable in any one Fiscal Year either by reason of the stated maturity date of such Parity Bonds or pursuant to a sinking fund installment; provided that with respect to any Parity Bonds issued as Term Bonds, such Bonds shall only be treated as Balloon Indebtedness if more than 25% of the principal thereof is due in any one Fiscal Year pursuant to the applicable sinking fund requirement or upon the stated maturity date thereof (assuming that the only principal due on the stated maturity date thereof will be the principal remaining outstanding after all redemptions have been made pursuant to the applicable sinking fund requirement).

“Bond Obligation” means, as of any given date of calculation, the sum of (1) the aggregate principal amount of all outstanding Current Interest Bonds and (2) the aggregate Accreted Value of all outstanding Capital Appreciation Bonds calculated as of the date of calculation if that date is a Payment Date or as of the next preceding Payment Date if the date of calculation is not a Payment Date.

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

“Capital Appreciation Bonds” means Parity Bonds, the interest on which accrues and compounds, payable at maturity or earlier redemption.

“Certified Public Accountant” means an independent licensed certified public accountant (or firm of certified public accountants) selected by the City.

“Current Interest Bonds” means Parity Bonds, the interest on which is paid periodically.

“Engineer” means an independent licensed professional engineer (or firm of licensed professional engineers) selected by the City and experienced and skilled in the operation of water systems of comparable size and character to the Regional System.

“Fiscal Year” means the fiscal year used by the City at any time. At the time of the adoption of the Bond Ordinance, the Fiscal Year is the 12-month period beginning January 1 of each year.

“Future Parity Bonds” means any revenue bonds or any other revenue obligations of the City, issued in accordance with the Bond Ordinance after the date of issuance of the Bonds, that are secured by a lien and charge equal to the lien and charge securing the payment of the principal of and interest on the Bonds and the Outstanding Parity Bonds.

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

“Mandatory Amortization Installment” means, for any Fiscal Year, the principal amount of Term Bonds required to be purchased, redeemed or paid in such year as established by the ordinance or resolution of the City authorizing the issuance of such Term Bonds.

“Maximum Interest Rate” means, with respect to any particular Variable Interest Rate Bond, a numerical rate of interest, which shall be set forth in any ordinance authorizing such Bond, that shall be the maximum rate of interest such Bond may at any time bear.

“Net Revenues” means, for any period, the excess of Revenues over Operating Expenses for such period, excluding from the computation of Revenues any profit or loss derived from the sale or other disposition, not in the ordinary course of business, of properties, rights or facilities of the Regional System or gains or losses resulting from the early extinguishment of debt or the requirements to mark assets or liabilities to market.

“Operating Expenses” means all expenses incurred by the City in causing the Regional System to be operated and maintained in good repair, working order and condition, including without limitation: deposits, premiums, assessments or other payments for insurance, if any, on the Regional System; payments into pension funds; State-imposed taxes; payments made to any other person or entity for the receipt of water supply or transmission or other right, commodity or service; payments made to any other person or entity that are required in connection with the operation of the Regional System or the acquisition or transmission of water and that are not subordinate to the lien of the Parity Bonds; and payments with respect to any other expenses of the Regional System that are properly treated as operation and maintenance expenses under generally accepted accounting principles applicable to municipal corporations. Operating Expenses do not include any depreciation or taxes levied or imposed by the City,

Payment Agreement payments, or payments to the City in lieu of taxes, any Rebate Amount, or capital additions or capital replacements to the Regional System.

“Outstanding Parity Bonds” means the outstanding 2002 Bonds and the 2010 Bonds.

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

“Parity Payment Agreement” means a Payment Agreement under which the City’s payment obligations are expressly stated to be secured by a pledge of and lien on Net Revenues on an equal and ratable basis with the Net Revenue required to be paid into the Bond Fund to pay and secure the payment of the principal of and interest on Parity Bonds.

“Participants’ Payments” means all payments received from the Participants under the Project Agreement.

“Participants’ Systems” or “Participant’s System” means the City’s Water System, the City of Kent’s water system, Covington Water District’s water system, and Lakehaven Utility District’s water and sewer system.

“Payment” means, for purposes of the provisions of the Bond Ordinance relating to parity derivative products, any payment (designated as such by an ordinance) required to be made by or on behalf of the City under a Payment Agreement and which is determined according to a formula set forth in the Payment Agreement.

“Payment Agreement” means a written agreement, for the purpose of managing or reducing the City’s exposure to fluctuations or levels of interest rates, currencies or commodities or for other interest rate, investment, asset or liability management purposes, entered into on either a current or forward basis by the City and a Qualified Counterparty, all as authorized by any applicable laws of the State. Such agreement may or may not be characterized by a structure of reciprocity of payment.

“Payment Date” means the dates on which principal and/or interest on the Parity Bonds is due and payable. For purposes of the section of the Bond Ordinance relating to parity derivative products, “Payment Date” means any date specified in the Payment Agreement on which a City Payment or Receipt is due and payable under the Payment Agreement.

“Payor” means a Qualified Counterparty to a Payment Agreement that is obligated to make one or more payments thereunder.

“Permitted Investments” means investments that are now or may hereafter be permitted to the City by the laws of the State of Washington.

“Qualified Counterparty” means a party (other than the City or a party related to the City) who is the other party to a Payment Agreement that has or whose obligations are unconditionally guaranteed by a party that has at least an investment grade rating from a Rating Agency or who is otherwise qualified to act as the other party to a Payment Agreement under any applicable laws of the State.

“Qualified Insurance” means any municipal bond insurance policy or surety bond issued by any insurance company licensed to conduct an insurance business in any state of the United States (or by a service corporation acting on behalf of one or more such insurance companies), which insurance company or companies, as of the time of issuance of such policy or surety bond, are currently rated in one of the two highest rating categories by two Rating Agencies.

“Qualified Letter of Credit” means any letter of credit issued by a financial institution for the account of the City on behalf of the owners of the Parity Bonds, which institution maintains an office, agency or branch in the United States and as of the time of issuance of such letter of credit is currently rated in one of the two highest rating categories by two Rating Agencies.

“Rating Agencies” means Moody’s, S&P or another nationally recognized rating agency rating municipal bonds.

“Receipt” means any payment (designated as such by an ordinance) to be made to, or for the benefit of, the City under a Payment Agreement by the Payor.

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

“Regional System” means the Regional Water Supply System, comprised of certain property and facilities to obtain and receive deliveries of water for the Participants from the exercise by Tacoma of the Second Diversion Water Right from the Green River and granted by the State of Washington Department of Ecology, which property and facilities include (i) a Main Branch pipeline to Tacoma with a 72 MGD nominal capacity; (ii) Headworks improvements associated with the Second Diversion Water Right; (iii) related fisheries and environmental enhancements; (iv) improvements and additions to the Howard Hanson Dam to raise the summer storage pool to elevation 1,167 in phase I to provide an additional 20,000 acre feet of water storage, together with improvements and additions related to accommodating fish passage; and (v) additional related water treatment facilities; and as the same will be added to, improved and extended for as long as any of the Parity Bonds are outstanding. The Regional System shall not include the Water System or any other separate system.

“Reserve Account Requirement” means for the Bonds, an amount equal to Average Annual Debt Service on the outstanding Bonds, but in no case shall the amount in the Reserve Account allocable to the Bonds exceed 10% of the proceeds of such Bonds. The Reserve Account Requirement, with respect to Future Parity Bonds will be either (1) an amount equal to Average Annual Debt Service on such issuance of Future Parity Bonds, but in no case shall the amount in the Reserve Account allocable to such issuance of Future Parity Bonds exceed 10% of the proceeds of such bonds, or (2) the ordinance authorizing such issuance of Future Parity Bonds may provide for the creation of a separate reserve account, in which case the Reserve Account Requirement, if any, for such issuance of Future Parity Bonds may be set in such ordinance and the Reserve Account created by Ordinance No. 27001 shall not secure such series of Future Parity Bonds. In the case of Variable Interest Rate Bonds, for the purpose of calculating Annual Debt Service, the interest rate thereon shall be calculated on the assumption that such bonds will bear interest during such period at a rate equal to the rate most recently reported by The Bond Buyer as the Bond Buyer Index for long-term revenue bonds as of the date the Parity Bonds are sold; provided, that if on such date of calculation the interest rate on such bonds shall then be fixed for a specified period, the interest rate used for such specified period for the purpose of the foregoing calculation shall be such actual interest rate.

“Revenues” means the income, revenues, receipts and loan proceeds derived by the City through the ownership and operation of the Regional System, including Participants’ Payments, but, except as provided in the Bond Ordinance, shall not include any income derived by the City through the ownership and operation of the Water System or any other separate utility system of the City.

“Variable Interest Rate” means a variable interest rate or rates to be borne by a series of Parity Bonds or any one or more maturities within a series of Parity Bonds. The method of computing such variable interest rate shall be specified in the ordinance authorizing such series of Parity Bonds. Such variable interest rate shall be subject to a Maximum Interest Rate and there may be an initial rate specified, in each case as provided in such ordinance, or a stated interest rate that may be changed from time to time as provided in the ordinance authorizing such Bonds. Such ordinance shall also specify either (i) the particular period or periods of time or manner of determining such period or periods of time for which each value of such variable interest rate shall remain in effect or (ii) the time or times upon which any change in such variable interest rate shall become effective.

“Variable Interest Rate Bonds” for any period of time means Parity Bonds that during such period bear a Variable Interest Rate, provided that Parity Bonds the interest rate on which shall have been fixed for the remainder of the term thereof shall no longer be Variable Interest Rate Bonds.

“Water System” means the water system of the City as it now exists, and all additions thereto and betterments and extensions thereof at any time made, but shall not include the Regional System or any future separate water system created by the City.

“Water System Bonds” means the City’s (i) \$51,380,000 original principal amount of Water System Revenue and Refunding Bonds, 2003; (ii) \$46,550,000 original principal amount of Water System Revenue and Refunding Bonds, 2005; (iii) \$76,755,000 original principal amount of Water System Revenue Bonds, 2009; (iv) \$29,100,000 original principal amount of Water System Revenue Refunding Bonds, 2010A; (v) \$74,985,000 original principal amount of Water System Revenue Bonds, 2010B (Taxable Build America Bonds – Direct Payment) and (vi) \$78,940,000* original principal amount of Water System Revenue and Refunding Bonds, 2013, issued pursuant to Ordinance Nos. 27109, 27405, 27837, 27902 and 28137, respectively, and any obligations thereafter issued on a parity with such Water System Bonds.

Regional System—Creation; Administration; Transfer of Facilities

A separate water supply and transmission utility system designated as the Regional Water Supply System has been created within the Water Division of the Department. The Regional System shall be administered by the Department as a separate utility system within the Water Division in accordance with the same administrative requirements of the City Charter, the Tacoma Municipal Code and state law as are applicable to the administration of the Water System.

Revenue Fund; Flow of Funds of the Regional System

Revenue Fund. The City will pay into the Revenue Fund all of the Revenues and all other money required to be paid into the Revenue Fund pursuant to the Bond Ordinance. The City has covenanted to pay into the Revenue Fund in each month, as an operating expense of the Water System, from Gross Revenues of the Water System an amount which, together with other Participants’ Payments and other Revenues available for such purpose, is equal to the Regional Supply System Costs which are then unpaid together with the estimated Regional Supply System Costs for the next succeeding month. The Treasurer may create separate accounts within the Revenue Fund.

Flow of Funds. In each month, the City shall apply amounts in the Revenue Fund first, to the payment of Operating Expenses for such month and second, to the deposit in the Bond Fund of the amounts required pursuant to the Bond Ordinance and, in the event the City has entered into any Parity Payment Agreement (as described in the Bond Ordinance) on a parity of lien with the Parity Bonds, to make any regularly scheduled City Payments adjusted by any regularly scheduled Receipt (provided, however, that termination payments with respect to any Parity Payment Agreement shall not rank on a parity of lien with the Parity Bonds); and, in the event the City has entered into a reimbursement agreement authorized by the Bond Ordinance, to make all payments required to be made on a parity of lien with the Parity Bonds pursuant to such reimbursement agreement in connection with a Qualified Letter of Credit, Qualified Insurance, or other credit facility, provided that if there is not sufficient money to make all payments under more than one such reimbursement agreement, the payments shall be made on a pro rata basis. After such required payments are made, amounts in the Revenue Fund may be used to pay junior lien obligations of the Regional System, to finance capital improvements or for any other lawful purpose of the Regional System.

Payment of and Security for Parity Bonds

Bond Fund. The Bond Fund shall be used solely for the purposes of paying the principal of, premium, if any, and interest on Parity Bonds and retiring Parity Bonds prior to maturity. The Bond Fund contains the Debt Service Account and the Reserve Account. The City has obligated itself irrevocably to set aside and to pay into the Bond Fund out of the Revenue Fund amounts sufficient (together with other available funds on hand and paid into the Bond Fund) to pay the principal of, premium, if any, and interest on the 2002 Bonds, the 2010 Bonds, the Bonds and all other Parity Bonds from time to time outstanding as the same respectively become due and payable, either at the maturity thereof or in accordance with the terms of any Mandatory Amortization Installment schedule established for the retirement of Term Bonds. The fixed amounts to be paid into the Bond Fund, to the extent that such payments are not made from bond proceeds or from other money that may legally be available therefor, shall be made out of the Revenue Fund into the Bond Fund in the following order of priority: first, to pay interest; second, to pay principal and Mandatory Amortization Installments; and third, into the Reserve Account.

* Preliminary, subject to change.

Money in the Bond Fund shall be transmitted to the Bond Registrar in amounts sufficient to meet the maturing installments of principal of, premium, if any, and interest on all Parity Bonds when due.

Money in the Bond Fund may, at the option of the City, be invested and reinvested as permitted by law in Permitted Investments. At the City's option, earnings on investments in the Bond Fund may be retained in the Bond Fund or transferred to the Revenue Fund, except that earnings on investments in the Reserve Account shall first be applied to remedy any deficiency in such Account.

The City will pay into the Reserve Account out of proceeds of the Bonds and/or acquire Qualified Insurance, if necessary, so that the amount in the Reserve Account at least equals the Reserve Account Requirement. The City may, at any time, substitute Qualified Insurance or a Qualified Letter of Credit for the money and investments in the Reserve Account or may substitute money and investments for Qualified Insurance or a Qualified Letter of Credit in accordance with the Bond Ordinance. Such Qualified Insurance or Qualified Letter of Credit shall not be cancelable on less than five years' notice.

On receipt of a notice of cancellation of any Qualified Letter of Credit or Qualified Insurance or upon notice that the entity providing the Qualified Letter of Credit or Qualified Insurance no longer meets the requirements specified in the Bond Ordinance, the City shall substitute a Qualified Letter of Credit or Qualified Insurance in the amount required to make up the deficiency created in the Reserve Account or in the alternative shall deposit, on or before the 25th day of each of the 36 succeeding calendar months (commencing with the 25th day of the calendar month next following the date of the notice) one thirty-sixth of the amount sufficient, together with other money and investments on deposit in the Reserve Account, to equal the Reserve Account Requirement in effect as of the date the cancellation or disqualification of the entity becomes effective.

Valuation of the amount in the Reserve Account and all subaccounts therein shall be made by the City on each December 31 and may be made on any other date. Such valuation shall be at the market value of the obligations in such account and such subaccounts (including accrued interest); provided, that investments which mature within one year shall be valued at their maturity value. If at any time the money and value of Permitted Investments in the Reserve Account shall exceed the amount of money and value of Permitted Investments then required to be maintained therein, such excess may be transferred to the Revenue Fund.

In the event that there shall be a deficiency in the Debt Service Account, the City shall promptly make up such deficiency from available funds in the Reserve Account by the withdrawal of cash therefrom for that purpose and by the sale or redemption of obligations held in the Reserve Account, if necessary, in such amounts as will provide cash in the Reserve Account sufficient to make up any such deficiency, and if a deficiency still exists immediately prior to an interest payment date and after the withdrawal of cash, the City shall then draw from any Qualified Letter of Credit, Qualified Insurance, or other equivalent credit facility in sufficient amount to make up the deficiency. The City has covenanted in the Bond Ordinance that any deficiency created in the Reserve Account by reason of any withdrawal for payment into the Debt Service Account shall be made up from money in the Revenue Fund first available after providing for the required payments into such Debt Service Account and after providing for payments under any reimbursement agreement entered into by the City under the Bond Ordinance.

The Bond Ordinance does not require the establishment of a Reserve Account Requirement for any Future Parity Bonds. The Reserve Account Requirements, if any, with respect to Future Parity Bonds will be specified in the ordinance authorizing the issuance of such Future Parity Bonds. The ordinance authorizing the issuance of Future Parity Bonds shall provide for further approximately equal monthly payments into the Reserve Account from the money in the Revenue Fund, in such amounts and at such times so that by no later than five years from the date of issuance of such Future Parity Bonds or by the final maturity established for such series of Future Parity Bonds, whichever occurs first, there will be credited to the Reserve Account an amount equal to the Reserve Account Requirement, if any. The City may obtain Qualified Insurance or a Qualified Letter of Credit for amounts required by to be paid out of the Reserve Account. Such Qualified Letter of Credit or Qualified Insurance shall not be cancelable on less than five years notice.

When a series of Parity Bonds is refunded in whole or in part, money may be withdrawn from the Reserve Account to pay or provide for the payment of refunded Parity Bonds; provided that immediately after such withdrawal there shall remain in or be credited to the Reserve Account money, Qualified Insurance, Qualified Letter of Credit and

Permitted Investments in an amount equal to the Reserve Account Requirement or so much thereof as is then required to be maintained.

Pledge of Net Revenue and Lien Position. The Parity Bonds are special limited obligations of the City payable from and secured solely by Revenues, including the amount of Gross Revenues of the Water System and Participants' Payments required to be deposited in the Revenue Fund pursuant to the Bond Ordinance, subject to the prior payment of Operating Expenses, and other funds specifically pledged thereunder. The City has pledged as security for the payment of the principal, premium, if any, and interest on the Parity Bonds in accordance with their terms and the provisions of the Bond Ordinance, and any City Payments or reimbursement obligations as set forth therein:

(1) the proceeds of the sale of the Parity Bonds to the extent held in the funds and accounts established by the Bond Ordinance,

(2) the Revenues, including such Gross Revenues of the Water System and Participants' Payments as provided therein, and

(3) the money and investments, if any, credited to the funds and accounts established by the Bond Ordinance, and the income therefrom.

The Revenues and other money and securities pledged shall immediately be subject to the lien of the pledge without any physical delivery or further act, and the lien of this pledge shall be valid and binding as against all parties having claims of any kind in tort, contract or otherwise against the City.

All Parity Bonds shall be equally and ratably payable and secured under the Bond Ordinance, except as to insurance which may be obtained by the City to insure the repayment of one or more series or maturities within a series.

Contract Resource Obligation. The obligations of the City under the Project Agreement shall be treated as a Contract Resource Obligation of the Water System to the Regional System for all purposes of the Water Bond Authorizing Ordinances, including for the purpose of treating all amounts payable by the City under the Project Agreement as Operation and Maintenance Expenses of the Water System as defined in the Water Bond Authorizing Ordinances.

Payments from the Water System. The City covenants that it shall pay into the Revenue Fund in each month, as an operating expense of its Water System, from Gross Revenues of the Water System an amount which, together with other Participants' Payments and other Revenues available for such purpose, is equal to the Regional Supply System Costs which are then unpaid together with the estimated Regional Supply System Costs for the next succeeding month.

Covenants with Bondowners

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

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

Rate Covenants. The City shall establish, maintain and collect contract charges or other amounts for water and other goods and services sold or supplied through the facilities of the Regional System that will provide the City with Revenues sufficient for the payment of Regional Supply System Costs. The City shall establish, maintain and collect rates and charges for water and other goods and services sold or supplied through the facilities of the Water System sufficient to pay the cost of operation and maintenance of the Water System and to provide Gross Revenues of the Water System sufficient, together with amounts on deposit in the Revenue Fund and available for such purpose (including Participants' Payments), to pay all Regional Supply System Costs and all obligations against Gross Revenues of the Water System.

New Participants; Assignments of Participants' Shares. The City will not amend the Project Agreement in any manner that would materially impact the security for Parity Bonds, increase or reduce a Participant's obligations to pay its share of debt service on the Parity Bonds or any Future Parity Bonds, other than to allow for a new Participant or an existing Participant (other than the City) to assign its interests in the Project Agreement if (i) the new Participant signs a project agreement substantially in the form of the Project Agreement, (ii) the new Participant's water system is rated in one of the three highest categories by one Rating Agency, (iii) the Participant's resolutions or ordinances authorizing outstanding water revenue bonds permit the Participant to pay all costs it owes under the Project Agreement as an operating and maintenance expense of its water system and any other utility that is combined with its water system, (iv) the tax-exempt status of any outstanding Parity Bonds issued as tax-exempt obligations or the entitlement of the City to receive federal direct payments from the United States Treasury with respect to any outstanding Parity Bonds issued as Build America Bonds will not be affected, and (v) to the extent that the new Participant's share of debt service on any Parity Bonds exceeds 10%, the new Participant shall execute a continuing disclosure undertaking that satisfies the requirements of Rule 15c2-12.

Sale, Transfer or Disposition of the Regional System. The City may sell, transfer or otherwise dispose (each, as used in this subparagraph, a "transfer") of any of the works, plant, properties, facilities or other part of the Regional System only consistent with State law, the City Charter and one or more of the following:

(1) The City may exchange any part of the Regional System for works, plant, properties or facilities of substantially the same type, use and value; or

(2) The City may transfer or dispose if the facilities or property transferred are not material to the operation of the Regional System, or shall have become unserviceable, inadequate, obsolete or unfit to be used in the operation of the Regional System or are no longer necessary, material or useful to the operation of the Regional System; or

(3) The City may sell, lease, mortgage or otherwise dispose of the Regional System if the aggregate depreciated cost value of the facilities or property being transferred in any Fiscal Year comprise no more than 5% of the assets of the Regional System; or

(4) The City may transfer or dispose if provision is made for the replacement thereof or for the payment, redemption or other retirement of a principal amount of Parity Bonds equal to the greater of the following amounts:

A. An amount in the same proportion to the net Bond Obligation of Parity Bonds then outstanding (defined as the total Bond Obligation of such Parity Bonds outstanding less the amount of cash and investments in the Debt Service Account) that the revenues attributable to the part of the Regional System transferred for any 12 consecutive of the most recent 24 months bears to the total revenues for such period; or

B. An amount in the same proportion to the net Bond Obligation of Parity Bonds then outstanding that the book value of the part of the Regional System sold or disposed of bears to the book value of the entire Regional System immediately prior to such transfer.

Books and Accounts. It will keep proper books, records and accounts with respect to the operations, income and expenditures of the Regional System in accordance with generally accepted accounting practices relating to municipal utilities, and will cause those books, records and accounts to be audited on an annual basis by the State Auditor or by a Certified Public Accountant selected by the City. It will prepare annual financial and operating statements after the close of each Fiscal Year of the Regional System showing in reasonable detail the financial condition of the Regional System.

Maintenance of Insurance. The City will keep the Regional System insured against risks, accidents or casualties, at least to the extent that insurance is deemed prudent and/or necessary by the other Participants; provided, the City may, with the other Participants' approval, institute or continue a self-insurance program with respect to any or all of the aforementioned risks. In the event of any loss or damage, the City will use insurance funds to repair or replace the damaged portion of the insured property; or in the event the City should determine not to repair or reconstruct such damaged portion of the properties of the Regional System, the proceeds of such insurance or self-insurance funding shall be transferred to the Reserve Account to the extent that such transfer shall be necessary to make up

any deficiency in the Reserve Account and the balance, if any, shall at the option of the City, be used for repairs, renewals, replacements, or additions to or extension of the Regional System or be used in the retirement of Parity Bonds prior to maturity.

Future Parity Bonds

The City has reserved the right to issue Future Parity Bonds for any lawful purpose of the City relating to the Regional System, including but not limited to, acquiring, constructing and installing additions, betterments and improvements to and extensions of, acquiring necessary equipment for, or making necessary renewals, replacements or repairs and capital improvements to the Regional System and refunding any outstanding indebtedness. The City covenants that Future Parity Bonds shall be issued only upon compliance with the following conditions:

- (1) The Project Agreement shall be in effect.
- (2) At the times of the issuance of such Future Parity Bonds there is no deficiency in the Bond Fund or in any of the accounts therein.
- (3) The ordinances authorizing the issuance of the Future Parity Bonds shall require that there shall be paid into the Reserve Account in the Bond Fund (A) from the proceeds of such Future Parity Bonds an amount such that the amount on deposit in the Reserve Account, allowing for any amount covenanted in an ordinance authorizing the issuance of outstanding Parity Bonds to be paid into the Reserve Account over five years in equal monthly installments as provided in the Bond Ordinance, is equal to the Reserve Account Requirement, if any, or (B) from the Revenue Fund in not more than five years in equal monthly installments as provided in the Bond Ordinance such that the amount on deposit in the Reserve Account is equal to the Reserve Account Requirement. Upon the issuance of any Future Parity Bonds, the City shall recalculate the Reserve Account Requirement.
- (4) Without obtaining a certificate described in A or B below, Future Parity Bonds may be issued for refunding purposes as described below. For all other Future Parity Bonds there shall be on file with the City Clerk either:
 - A. A certificate of the Finance Director (or equivalent official) of each Participant (including the City in the case of the Water System) that will be responsible for paying debt service on the Future Parity Bonds stating that "Revenues" or "Gross Revenues" (as defined in the Participant's System bond ordinances or resolutions) in any 12 consecutive months out of the most recent 24 months preceding the delivery of the Future Parity Bonds then proposed to be issued, as determined from the financial statements of the Participant's System, were sufficient to pay the operation and maintenance expenses of the Participant's System and the Participant's portion of the debt service on the Future Parity Bonds then proposed to be issued based on the highest debt service in the next three calendar years following the year through which interest is capitalized or the Project being financed is placed in service, whichever is later, and "Net Revenues" (as defined in the Participant's System bond ordinances or resolutions) for such 12 month period were sufficient to pay debt service on the Participant's senior lien water revenue bonds and meet the Participant's rate coverage required by such ordinance or resolution; or
 - B. For each Participant (including the City) that will be responsible for paying debt service on the Future Parity Bonds, a certificate of an Engineer or a Certified Public Accountant showing that the "Adjusted Revenues" for each calendar year during the life of the Future Parity Bonds proposed to be issued will be sufficient to pay the operation and maintenance expenses of the Participant's System and the Participant's portion of the debt service on outstanding Parity Bonds and on the Future Parity Bonds then proposed to be issued based on the highest debt service in the next three calendar years following the year through which interest is capitalized or the Project being financed is placed in service, whichever is later, and "Adjusted Net Revenues" will be sufficient to pay debt service on the Participant's senior lien water revenue bonds and meet the Participant's rate coverage required by the ordinance or resolution authorizing such senior lien bonds.

The "Adjusted Revenues" or "Adjusted Net Revenues," as applicable, shall be the Participant's System water revenue for a period of any 12 consecutive months out of the 24 months immediately preceding the date of delivery of such proposed Future Parity Bonds (the "Base Period") as adjusted by such Engineer or Accountant to take into consideration changes in revenues estimated to occur under the following conditions for each year after such

delivery for so long as any Parity Bonds, including the Future Parity Bonds proposed to be issued, shall be outstanding:

(1) the additional revenues that would have been received if any change in rates and charges adopted prior to the date of such certificate and subsequent to the beginning of the Base Period and effective within 12 months of the certificate had been in force during the full Base Period;

(2) the additional net revenues that would have been received if any facility of the Participant's System that became fully operational after the beginning of the Base Period had been so operating for the entire Base Period;

(3) the additional revenues to the Participant's System estimated by such Engineer or Accountant to be received (a) as a result of any additions, betterments and improvements to and extensions of any facilities of the Participant's System which are under construction at the time of such certificate or (b) as a result of improvements to the Regional System to be constructed or acquired from the proceeds of the Future Parity Bonds to be issued; and

(4) the additional revenues that would have been received if any customers added to the Participant's System during the Base Period or subsequent thereto had been customers for the entire Base Period.

Such Accountant or Engineer may rely upon, and the Accountant's or Engineer's certificate shall have attached thereto, financial statements of the Participant's System, certified by the Finance Director, showing income and expenses for the period upon which the same is based.

In the event that any Future Parity Bonds provided for in the Bond Ordinance are issued for refunding purposes and the issuance of such refunding Future Parity Bonds results in a present value monetary saving to the City and such refunding Future Parity Bonds will not require an increase of greater than \$5,000 in debt service payments to be paid in any Fiscal Year or calendar year thereafter than would have been required to be paid in the same Fiscal Year or calendar year for Annual Debt Service on the Parity Bonds being refunded, then the requirements of paragraph (4) above need not be complied with to permit such refunding Future Parity Bonds to be issued, although the provisions of paragraphs (1), (2) and (3) above must still be complied with.

In making any calculations required to be made by a Finance Director or the Engineer or Accountant in paragraph (4) above, in the case of Variable Interest Rate Bonds, for purposes of calculating Annual Debt Service the interest rate thereon shall be calculated on the assumption that such bonds will bear interest at a rate equal to the rate most recently reported by The Bond Buyer as the Bond Buyer's Index for long-term revenue bonds; provided, that if on such date of calculation the interest rate on such bonds shall then be fixed to maturity, the interest rate used for such specified period for the purpose of the foregoing calculation shall be such actual interest rate.

Reimbursement Obligations

In the event that the City elects to meet the Reserve Account Requirement as to any issue of Parity Bonds through the use of a Qualified Letter of Credit, Qualified Insurance or other equivalent credit enhancement device, the City may contract with the entity providing such Qualified Letter of Credit, Qualified Insurance or other equivalent credit enhancement device that the City's reimbursement obligation, if any, to such entity ranks on a parity of lien with the Parity Bonds.

In the event that the City elects additionally to secure any issue of Variable Interest Rate Bonds through the use of a letter of credit, insurance or other equivalent credit enhancement device, the City may contract with the entity providing such letter of credit, insurance or other equivalent credit enhancement device that the City's reimbursement obligation, if any, to such entity ranks on a parity of lien with the Parity Bonds; provided, that the payments due under such reimbursement agreement are such that if such reimbursement obligation were a series of Future Parity Bonds, such Future Parity Bonds could be issued in compliance with the provisions of the Bond Ordinance.

Parity Payment Agreements

A Payment made under a Payment Agreement may be on a parity with the Bonds if the Payment Agreement satisfies the requirements for Future Parity Bonds described in the provisions of the Bond Ordinance relating to Future Parity Bonds, taking into consideration regularly scheduled Payments and Receipts (if any) under the Payment Agreement. The following shall be conditions precedent to the use of any Payment Agreement on a parity with the Bonds:

(1) The City shall obtain an opinion of Bond Counsel on the due authorization and execution of such Payment Agreement, the validity and enforceability thereof and opining that the action proposed to be taken is authorized or permitted by the Bond Ordinance or the applicable provisions of any supplemental ordinance and will not adversely affect the excludability for federal income tax purposes of the interest on any outstanding Parity Bonds issued as tax-exempt obligations or the entitlement of the City to receive federal direct payments from the United States Treasury with respect to any outstanding Parity Bonds issued as Build America Bonds.

(2) Prior to entering into a Payment Agreement, the City shall adopt an ordinance setting forth such matters and provisions as required by the Bond Ordinance.

If the City enters into a Parity Payment Agreement, Payments shall be made from the Debt Service Account in the Bond Fund and Annual Debt Service shall include any regularly scheduled City Payments adjusted by any regularly scheduled Receipts during a Fiscal Year. Receipts shall be made directly into the Bond Fund. Obligations to make unscheduled payments, such as termination payments, may not be entered into on a parity with the Bonds.

Junior Lien Obligations

The City may issue bonds, notes, or other obligations secured by a lien and charge junior to the lien and charge of the Parity Bonds. The City may enter into Payment Agreements with a claim on Net Revenues junior to that of the Bonds.

Advance Refunding or Defeasance of Bonds

The City may issue refunding bonds or use money available to pay the principal of and interest on the Bonds as the same become due and to redeem, refund or defease all such then-outstanding Bonds (the "Defeased Bonds") and to pay the costs of such refunding or defeasance. In the event that money and/or "Government Obligations," as such obligations are now or may hereafter be defined under RCW 39.53 or other applicable State law, maturing at such time or times and bearing interest to be earned thereon in amounts sufficient to redeem and retire the Bonds in accordance with their terms are set aside in a special account and such money and the principal of and interest on such obligations are irrevocably set aside and pledged for such purpose, then no further payments need be made into the Bond Fund for the payment of the principal of and interest on the Bonds so provided for and such Bonds shall cease to be entitled to any lien, benefit or security of the Bond Ordinance except the right to receive the funds so set aside and pledged, and such Bonds shall be deemed not to be outstanding under the Bond Ordinance.

Amendatory or Supplemental Ordinances

Without Bond Owners' Consent. The Council may pass an ordinance supplemental to the Bond Ordinance, for one or more of the following purposes:

(1) To add covenants which shall not adversely affect the interests of the owners of any Parity Bonds or to surrender any right or power reserved to or conferred upon the City; or

(2) To cure any ambiguities or correct any defective provision contained in the Bond Ordinance or any ordinance authorizing Parity Bonds and which shall not adversely affect the interest of the owners of the Parity Bonds.

Any such supplemental ordinance of the City may be passed without the consent of the owners of any Parity Bonds if the City obtains an opinion of Bond Counsel to the effect that such supplemental ordinance is solely for one or more of the purposes stated above and will not adversely affect the interests of the owners of Parity Bonds.

With Bond Owners' Consent. With the consent of the owners of not less than 51% in aggregate Bond Obligations of the Parity Bonds at the time outstanding, the City may pass an ordinance or ordinances supplemental thereto for the purpose of adding any provisions to or changing in any manner or eliminating any of the provisions of the Bond Ordinance or of any supplemental ordinance; provided, however, that no such supplemental ordinance shall:

(1) Extend the fixed maturity of any Parity Bonds, or reduce the rate of interest thereon, or extend the times of payment of interest thereon from their due dates, or reduce the amount of the principal thereof, or reduce any premium payable on the redemption thereof, without the consent of the owner of each bond so affected; or

(2) Reduce the aforesaid percentage of bondowners required to approve any such supplemental ordinance, without the consent of the owners of all of the Parity Bonds then outstanding.

It shall not be necessary for the consent of bondowners to approve the particular form of any proposed supplemental ordinance, but it shall be sufficient if such consent shall approve the substance thereof. To the extent the Bonds are insured, the Insurer may consent on behalf of owners of the Bonds to any amendment to the Bond Ordinance so long as the Insurer is not in default on its obligations to pay.

Defaults and Remedies

Events of Default. The following shall constitute "Events of Default" with respect to the Parity Bonds:

(1) If a default is made in the payment of the principal of or interest on any of the Parity Bonds when the same shall become due and payable; or

(2) If the City defaults in the performance of any of the covenants, conditions and agreements in the Bond Ordinance or any ordinance authorizing Parity Bonds and such default or defaults have continued for six months after it has received from the Bondowners' Trustee or from the registered owners of not less than 25% in principal amount of the Parity Bonds, a written notice specifying and demanding the cure of such default. However, if the default in the performance of any covenants, conditions and agreements is one which cannot be completely remedied within the six months after written notice has been given, it shall not be an Event of Default as long as the City has taken active steps within the six months after written notice to remedy the default and is diligently pursuing such remedy; or

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

Bondowners' Trustee. So long as such Event of Default has not been remedied, a bondowners' trustee (the "Bondowners' Trustee") may be appointed by the registered owners of 25% in principal amount of the Parity Bonds, by an instrument or concurrent instruments in writing signed by such registered owners of the Parity Bonds or by their attorneys-in-fact duly authorized and delivered to such Bondowners' Trustee. Any Bondowners' Trustee shall be a bank or trust company organized under the laws of the State of Washington or the State of New York or a national banking association. The bank or trust company acting as Bondowners' Trustee may be removed at any time, and a successor Bondowners' Trustee may be appointed, by the registered owners of a majority in principal amount of the Parity Bonds. The Bondowners' Trustee may require such security and indemnity as may be reasonable against the costs, expenses and liabilities that may be incurred in the performance of its duties.

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

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

enforce the specific performance of any covenant, agreement or condition contained in the Bond Ordinance or in any ordinance authorizing Parity Bonds.

The remedy of acceleration is expressly denied to the registered owners of the Parity Bonds. The respective registered owners of the Parity Bonds shall be conclusively deemed irrevocably to appoint the Bondowners' Trustee the lawful trustee of the respective registered owners of those Parity Bonds, with authority to institute any such action, suit or proceeding; to receive as trustee and deposit in trust any sums becoming distributable on account of those Parity Bonds; to execute any documents for the receipt of money; and to do all acts that the registered owner might have done in person. The Bondowners' Trustee may not consent to accept or adopt, on behalf of any registered owner of the Parity Bonds, any plan of reorganization or adjustment affecting the Parity Bonds or any right of any registered owner, or may not vote the claims of the registered owners in any receivership, insolvency, liquidation, bankruptcy, reorganization or other proceeding to which the City is a party.

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

- (1) to the payment of the charges, expenses, advances and compensation of the Bondowners' Trustee and the charges, expenses, counsel fees, disbursements and compensation of its agents and attorneys; and
- (2) to the payment of interest then due on the Parity Bonds in the order of maturity of such installments and, if the amount available is not sufficient, then to the payment thereof ratably; and
- (3) to the payment of the unpaid principal amounts of any Parity Bonds which shall have become due (other than Parity Bonds previously called for redemption for the payment of which money is held, whether at maturity or by redemption, in the order of their due dates and, if the amount available shall not be sufficient, then to the payment thereof ratably).

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

The Bondowners' Trustee shall not be required to expend or risk its own funds or otherwise incur individual liability in the performance of any of its duties or in the exercise of any of its rights or powers as the Bondowners' Trustee.

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

Suits by Individual Bondowners Restricted. Neither the registered owner nor the beneficial owner of any Parity Bond shall have any right to institute any action, suit or proceeding at law or in equity for the enforcement of the same unless an Event of Default has happened and is continuing; a Bondowners' Trustee has been appointed; and such owner previously shall have given to the Bondowners' Trustee written notice of the Event of Default on account of which such suit, action or proceeding is to be instituted; and

- (1) the registered owners of 25% in principal amount of the Parity Bonds, after the occurrence of such Event of Default, have made written request of the Bondowners' Trustee and have afforded the Bondowners' Trustee a reasonable opportunity to institute such suit, action or proceeding; and
- (2) there have been offered to the Bondowners' Trustee security and indemnity satisfactory to it against the costs, expenses and liabilities to be incurred therein or thereby; and
- (3) the Bondowners' Trustee has refused or neglected to comply with such request within a reasonable time.

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APPENDIX B

PARTICIPANTS IN THE SECOND SUPPLY PROJECT

The information in this Appendix B has been furnished to the City by the City of Kent, Covington Water District, and Lakehaven Utility District (the other “Participants”) for use in this Official Statement. Such information is not to be construed as a representation by or on behalf of the City. Although the City has no reason to believe that the information in this Appendix B is not accurate or complete, the City has not independently verified such information and does not guarantee the accuracy or completeness of such information. At or prior to the time of delivery of the Bonds, each Participant will certify to the City that the information pertaining to such Participant in this Appendix B and elsewhere in this Official Statement is true and correct and does not contain any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements in this Appendix B and elsewhere in this Official Statement pertaining to such Participant, in light of the circumstances under which they were made, not misleading.

The City of Kent

Under the Second Supply Project Agreement, the City of Kent, Washington (“Kent”) is entitled to use its 7/36 Participant Share of the Project and is obligated to pay its Participant Share of Project Costs. See “THE SECOND SUPPLY PROJECT—Project Participants.” Kent is responsible for paying \$11,400,000 (approximately 24%) of the principal on the 2010 Bonds and \$14,790,000 (approximately 23%) of the principal on the Bonds. The following provides a brief summary of Kent and its water collection and distribution system (the “Kent Water System”).

Introduction. Kent is an optional municipal code city located in South King County, Washington. Kent was incorporated in 1890 and, in 2012, had an estimated population of 119,100. Kent is governed by a mayor and a seven-member City Council.

The Kent Water System was established in 1920, has a service area of approximately 24 square miles, served approximately 14,429 accounts in 2012, and presently consists of the sources of water shown below. The Kent Water System is accounted for as a separate enterprise fund for purposes of Kent’s annual budget and annual financial report.

Water Supply. Kent Water System’s sources of water supply as of December 31, 2012 included: Clark Springs, Kent Springs, East Hill well, the Regional Water Supply System, 212th Plant, Armstrong Springs, Seven Oaks, Garrison Creek and O’Brien well. The Kent Water System’s total reliable pumping capacity is about 29.91 million gallons per day (“MGPD”) from 22 water wells, interties, and two springs, and has approximately 24.9 million gallons of reservoir capacity and 1,254.72 million gallons of surface storage capacity. Auxiliary power generators are provided at selected pumping stations. Kent considers the Kent Water System’s source, storage, and transmission capabilities to be adequate for its customers.

Customer Information. In 2012, the Kent Water System provided water service to approximately 14,429 accounts, approximately 73% of which were residential. Customer data and usage by class for the last five years is presented below.

	Kent Water System Water Consumption (ccf)				
	2008	2009	2010	2011	2012
Residential	846,886	886,832	793,858	790,552	800,765
Other	2,638,228	2,606,693	2,327,920	2,352,119	2,356,837
Total	3,485,114	3,493,525	3,121,778	3,142,671	3,157,602

Source: The City of Kent

**Kent Water System
Annual Water Billing**

	2008	2009	2010	2011	2012
Residential	\$1,539,689	\$2,178,431	\$2,709,589	\$2,716,821	\$2,788,953
Other	5,616,060	7,383,646	9,516,676	9,973,902	10,241,211
Total	\$7,155,749	\$9,562,077	\$12,226,265	\$12,690,723	\$13,030,164

Source: The City of Kent

The following table identifies the Kent Water System's ten largest customers by billings.

**Largest Customers of the Kent Water System
As of December 31, 2012**

Customer	Billings
Boeing Defense & Space Group	\$ 207,383
Danone Waters of North America	240,230
King County	148,731
Air Liquide Industrial US LP	165,188
Ralcorp Frozen Bakery Products	118,161
Kings Command Foods	140,749
Aramark Uniform Services	143,534
Rexan Beverage Can Co.	117,098
Northwest Center for Retarded	112,482
Oberto Sausage Company	136,288

Source: The City of Kent

Water Rates. The following table shows the Kent Water System's current water rates (for both summer and winter consumption). Water rates were increased effective June 1, 2009, January 1, 2010, January 1, 2011, January 1, 2012 and most recently January 1, 2013.

Kent Water System Water Rates	
Monthly bill/ccf	Rate(l)
<u>Inside City</u>	
May 1-September 30 (summer rates)	
Less than or equal to 700 ccf(2)	\$3.99 per 100 cf
Greater than 700 ccf	\$5.09 per 100 cf
October 1-April 30 (winter rates)	
Less than or equal to 700 ccf	\$3.03 per 100 cf
Greater than 700 ccf	\$4.10 per 100 cf
<u>Outside City</u>	
May 1-September 30 (summer rates)	
Less than or equal to 700 ccf	\$4.88 per 100 cf
Greater than 700 ccf	\$5.99 per 100 cf
October 1-April 30 (winter rates)	
Less than or equal to 700 ccf	\$3.99 per 100 cf
Greater than 700 ccf	\$5.09 per 100 cf

(1) This does not include a fixed monthly demand charge for service and meter.

(2) ccf = cubic feet.

Source: The City of Kent

Outstanding Debt. As of December 31, 2012, the City of Kent had \$22,110,000 in Combined Utility System Revenue Bonds outstanding, payable in part from the City of Kent's water system revenues.

Bond Ordinance. Pursuant to Ordinance No. 3925, Kent issued its Combined Utility System Revenue Bonds, Series 2009. Under the bond ordinance, Kent has pledged the Net Revenue of the System and ULID Assessments.

"System" means (a) the water collection and distribution system of the City of Kent, as it existed as of the passage of Ordinance No. 3925, and including all additions, betterments and extensions at any time made; (b) the sanitary sewage collection and disposal system of the City of Kent, as it existed as of the passage of Ordinance No. 3925, and including all additions, betterments and extensions at any time made; (c) the storm and surface water utility of the City of Kent, as it existed as of the passage of Ordinance No. 3925, and including all additions, betterments and extensions at any time made, and (d) any other system or utility that may lawfully be combined with the foregoing.

"Net Revenue" means Revenue of the System less Costs of Maintenance and Operation.

"Revenue of the System" means all of the earnings and revenues received by the City of Kent from the maintenance and operation of the System and connection and capital improvement charges collected for the purpose of defraying the costs of capital facilities of the System, including investment earnings, but excluding government grants, proceeds from the sale of System property, City of Kent taxes collected by or through the System, principal proceeds of bonds and earnings or proceeds from any investment in a trust, defeasance or escrow fund created to defease or refund System obligations (until commingled with any other earnings and revenues of the System) or held in a special account for the purpose of paying a rebate to the United States Government under the Code. Revenue of

the System shall also include any federal or state reimbursements or operating expenses to the extent such expenses are included as Costs of Maintenance and Operation; provided, however, that Revenue of the System shall not include ULID Assessments. Amounts withdrawn from the Coverage Stabilization Account shall increase Revenue for the period in which they are withdrawn, and amounts deposited in the Coverage Stabilization Account shall reduce Revenue for the period during which they are deposited. Credits to or from the Coverage Stabilization Account that occur within 90 days after the end of a fiscal year may be treated as occurring within such fiscal year.

“Costs of Maintenance and Operation” means all reasonable expenses incurred by the City of Kent in causing the System of the City of Kent to be operated and maintained in good repair, working order and condition, deposits, premiums, assessments or other payments for insurance, if any, on the System; payments into pension funds; State-imposed taxes; amounts due under Contract Resource Obligations (but only at the times described in Ordinance 3925); payments made to any other person or entity that are required in connection with the operation of the System or the acquisition or transmission of water or sewer or storm water and that are not subordinate to the lien of Parity Bonds; and payments with respect to any other expenses of the System that are properly treated as operation and maintenance expenses under generally accepted accounting principles applicable to municipal corporations, but shall not include any payments for principal or interest or into the Reserve Account, depreciation or taxes levied or imposed by the City or payments to the City in lieu of taxes, or capital additions or capital replacements to the System.

The City of Kent has covenanted to establish, maintain and collect rates and charges for service of its System for so long as any bonds are outstanding under Ordinance No. 3925 as will permit it to maintain Net Revenue in each fiscal year at least equal to 120% of the amounts required in such fiscal year to be paid as scheduled debt service (principal and interest) on all parity bonds, subtracting from the scheduled debt service (1) the amount of ULID Assessments collected in such year and (2) Debt Service Offsets, including without limitation federal interest subsidy payments designated as such. Furthermore, in determining compliance with the Rate Covenant, Net Revenues are subject to adjustment to reflect the following: (a) it is the intent of the City of Kent that regularly scheduled net payments under parity derivative products be reflected in the calculation of debt service with respect to the associated parity bonds and not as adjustments to revenue or costs of maintenance and operation, and (b) Revenue and Costs of Maintenance and Operation may be adjusted, regardless of then-applicable generally accepted accounting principles, for certain items (*e.g.*, to omit unrealized gains or losses in investments) to reflect more fairly the System’s annual operating performance.

Under the resolution, the City of Kent has reserved the right to issue future bonds with a lien on Net Revenue on a parity with the lien thereon of its outstanding system revenue bonds and parity payment agreements, upon compliance with certain conditions set forth therein.

The City of Kent’s obligations to debt service on the 2010 Bonds and the Bonds are Contract Resource Obligations of the City of Kent, payable as Costs of Maintenance and Operation. Kent may at any time enter into one or more contracts or obligations for the acquisition, from facilities to be constructed, of water, sewer or storm water supply, transmission, treatment or other commodity or service relating to the System. Kent may determine that such contract or other obligation is a Contract Resource Obligation, and may provide that all payments under the Contract Resource Obligation (including payments prior to the time that water, sewer or storm water supply, transmission, treatment or other commodity or service is being provided, or during a suspension or after the termination of supply or service) shall be Costs of Maintenance and operation if certain conditions and requirements are met. Contract Resource Obligations treated as Costs of Maintenance and Operation therefore enjoy a prior lien on Revenue of the System.

Certain Historical Results. The following table shows historical operating revenues and expenses for the Kent Water System From 2008 through 2012.

**Kent Water System
Historical Financial Results for the Years Ended December 31**

	2008	2009	2010	2011	2012(1)
OPERATING REVENUES					
Sales	\$8,315,263	\$11,370,578	\$14,954,024	\$15,529,327	\$15,768,625
Charges for services	455,656	435,741	441,241	455,142	480,512
Other operating revenue	8,007	70,218	31,028	2,363	375
TOTAL OPERATING REVENUES	8,778,926	11,876,537	15,426,293	15,986,832	16,249,512
OPERATING EXPENSES(2)					
Salaries and wages	1,958,483	2,079,644	2,072,111	2,223,798	2,118,013
Benefits	654,349	736,993	805,346	961,979	987,483
Supplies	553,701	539,574	497,700	472,806	610,546
Services and charges	5,406,516	5,141,974	5,654,808	6,071,794	6,974,111
TOTAL OPERATING EXPENSES	8,573,049	8,498,185	9,029,965	9,730,377	10,690,153
TOTAL OPERATING INCOME	205,877	3,378,352	6,396,328	6,256,455	5,559,359
NON-OPERATING REVENUE (EXPENSES)					
Interest Income	553,465	245,475	107,174	66,457	55,064
Unrealized net gain/(loss) in fair value of investments	(19,666)	(109,904)	(15,323)	(10,861)	(483)
Miscellaneous non-operating revenues	71,116	73,718	76,914	90,209	95,781
Interest Expense (3)	(74,140)	(320,046)	(615,233)	(649,138)	(630,207)
TOTAL NON-OPERATING REVENUE (EXPENSES)	530,775	(110,757)	(446,468)	(503,333)	(479,845)
DEBT SERVICE (Principal Reductions)					
Revenue Bonds 2009 A&B	0	105,000	432,500	447,500	460,000
Tacoma Revenue Bonds 2010 (4)	0	0	0	0	0
Tacoma Revenue Bonds 2002 (4)	230,324	158,806	147,467	142,537	148,946
Public Works Trust Fund Payments(5)	1,059,028	1,059,028	1,059,028	1,059,028	1,059,028
TOTAL DEBT SERVICE (Principal Reductions)	1,289,352	1,322,834	1,638,995	1,649,065	1,667,974
BALANCE AVAILABLE FOR CAPITAL IMPROVEMENTS AND OTHER PURPOSES	\$ (552,700)	\$1,944,761	\$4,310,865	\$4,104,057	\$3,411,540
DEBT SERVICE COVERAGE(6)	N/A	13.03x	6.03z	5.89x	5.24x

(1) Preliminary, unaudited.

(2) Excludes depreciation. Excludes payments to the City of Tacoma for the Regional System. For financial reporting purposes, payments are presented as debt service.

(3) Interest expense on Revenue Bonds, 2009 A&B and State Public Works Trust Fund Loans.

(4) City of Tacoma issued debt for Regional System. Recorded with the City of Kent as a contract or long-term non-bonded debt.

(5) Repayment of State Public Works Trust Fund Loans.

(6) Debt service coverage calculated on revenue bond debt service only.

Source: City of Kent

Covington Water District

Under the Second Supply Project Agreement, Covington Water District ("Covington") is entitled to use its 7/36 Participant Share of the Project and is obligated to pay its Participant Share of Project Costs. Covington is responsible for paying debt service on \$3,515,000 (approximately 7%) of the principal amount of the 2010 Bonds and is expected to be responsible for \$14,165,000 (approximately 22%) of the principal amount of the Bonds. Covington has received State Revolving Fund loans for the Filtration Treatment Project and is expected to

contribute \$8,080,000 of loan proceeds to finance a portion of its share of the project. In order to reduce the amount that Tacoma would need to borrow to pay its share of additional costs of the Filtration Treatment Project, Tacoma has agreed to use a portion of Covington's share of unspent 2010 Bond proceeds for Tacoma's share of the project, and in return, pay a portion of the principal of and interest on the 2010 Bonds that are currently the responsibility of Covington. See "THE SECOND SUPPLY PROJECT—Project Participants." The following provides a brief summary of Covington and its financial condition.

Introduction. Covington was organized in 1960 for the purpose of providing water services to areas of southeastern King County, east of Kent and the City of Auburn. Covington encompasses approximately 55 square miles, including unincorporated areas as well as all of the City of Covington, approximately 60% of the City of Maple Valley and approximately 10% of the City of Black Diamond. Of these cities, only Black Diamond has a water utility, and Covington continues to provide water to these incorporated areas.

Covington is managed by a five-member Board of Water Commissioners. The Board serves as the governing body of Covington and has the authority to set rates and charges. The Board appoints a general manager, who is responsible for the administration of Covington. Covington operates its facilities with a total of approximately 39 full- and part-time employees.

Water Supply. The Covington system contains over 250 miles of mains and appurtenances including fire hydrants. Covington presently has 11 active wells with water rights totaling 5,765 gallons per minute ("GPM") or 7.5 MGD. Present pump capacity is 9,080 GPM. All of Covington's average daily water demand (approximately 3 MGD) can be met from its own wells. Summer water demand (approximately 6 MGD) is met through a combination of Covington's wells, and the Second Supply Project water. The partnership in the Regional System assures Covington of a sufficient water supply well into the future. Covington has storage tanks at eight sites with a storage capacity of approximately 21.5 million gallons.

Covington was a partner in the Cascade Water Alliance ("Cascade") until December 2012. Cascade was formed in 1999 as a nonprofit corporation by eight Washington cities and special purpose districts, including Covington. In 2012 Cascade converted to a joint municipal utility services authority of the State, authorized by laws of the State and by a Joint Municipal Utilities Services Agreement entered into by its members, including Covington. Under the agreement each member has agreed to pay to Cascade member charges, which are the primary source of revenues for Cascade. In 2012, Covington paid Cascade \$407,539, or 1.14% of all member charges, which were a Contract Resource Obligation, payable as an operating expense of Covington. Covington has never taken any water from Cascade and after evaluating its water supply resources, determined that it has adequate resources to meet its water requirements for the foreseeable future without Cascade. As a result the District withdrew from Cascade in December 2012. Covington made its withdrawal payment to Cascade in the amount of approximately \$6 million and has no further obligations to Cascade.

Customer Information. Covington provides water service to 16,883 accounts, of which approximately 98% are single-family residential. Customer data and usage by class for the years 2008 through 2012 is presented below.

**Covington Water District Water Sales
(including Flat Rate)**

	2008	2009	2010	2011	2012
Residential	\$7,770,845	\$8,807,658	\$8,482,531	\$8,550,494	9,319,117
Non-residential	496,808	551,706	603,141	667,754	750,370
Rental Equipment	64,738	16,134	21,213	31,583	46,639
Total	\$8,332,391	\$9,375,498	\$9,106,885	\$9,249,831	10,116,126

Source: Covington Water District.

The following table shows Covington's largest customers based upon consumption and billing amount in 2012.

**Covington Water District
2012 Largest Customers**

Customer Name	Consumption (ccf)	Amount	Percent of Operating Revenues
Washington National Golf LLC	22,207	\$70,417	0.70%
Fred Meyer	6,768	26,294	0.26
Camp Berachah	6,568	25,707	0.25
WM Glacier	6,243	23,796	0.24
Covington Medical Park	4,625	30,084	0.30

Water Rates. Water rates and charges are set by resolution. Covington adopted the following rate schedule effective January 1, 2013. All water bills include a fixed and a commodity charge.

**Covington Water District
Water Rates and Charges
(Effective January 1, 2013)**

Meter Size	Flat Rate Charge by Meter Size			
	Residential (Billed Bi-Monthly)	Non-Residential Inside Meter (Billed Bi-Monthly)	Non-Residential Outside Meter (Billed Monthly)	Wholesale (Billed Monthly)
5/8" meter	\$ 37.00	\$ 52.70	\$ 26.35	\$ 65.90
3/4" meter	45.05	68.75	34.40	86.00
1" meter	61.30	100.75	50.40	126.00
1 1/2" meter	102.00	180.85	90.45	226.15
2" meter	150.55	276.95	138.50	346.25
3" meter	280.45	533.10	266.55	666.40
4" meter	426.75	820.90	410.45	1,026.15

Residential Customers Billed Every Other Month (\$ for ccf)					
	Less than 8 ccf	9-14 ccf	15-20 ccf	21-34 ccf	More than 34 ccf
Single Meter					
Winter	\$2.70	\$3.95	\$5.10	\$5.90	\$6.90
Summer	2.70	3.95	6.70	8.50	9.90
Dual Meter (Inside Use)					
Winter	2.70	3.95	5.10	5.90	6.90
Summer	2.70	3.95	6.70	8.50	9.90
Dual Meter (Outside Use)					
Winter	2.70	3.95	5.10	5.90	6.90
Summer				8.50(1)	9.90
Kidney Dialysis					
Winter	2.70	3.95	5.10	5.90	6.90
Summer	2.70	3.95	6.70	8.50	9.90

(1) Less than 34 ccf.

Residential Customers Billed Every Month (\$ for ccf)					
	Less than 4 ccf	5-7 ccf	8-10 ccf	11-17 ccf	More than 17 ccf
Sugarloaf (1)					
Winter	\$2.70	\$3.95	\$5.10	\$5.90	\$6.90
Summer	2.70	3.95	6.70	8.50	9.90
	Less than 120 ccf	121-210 ccf	211-300 ccf	301-510 ccf	More than 510 ccf
Ravensdale (serving 30 connections through a master meter) (1)					
Winter	\$2.70	\$3.95	\$5.10	\$5.90	\$6.90
Summer	2.70	3.95	6.70	8.50	9.90
	Less than 40 ccf	41-70 ccf	71-100 ccf	101-170 ccf	More than 170 ccf
Special Benefit Area #2 (Supplying 10 Properties) (1)					
Winter	\$2.70	\$3.95	\$5.10	\$5.90	\$6.90
Summer	2.70	3.95	6.70	8.50	9.90

(1) In addition, billed a flat rate of \$18.50 monthly.

Non-Residential Customers		
	All Winter Usage	All Summer Usage
Non-Residential Inside Use	\$3.05	\$5.50
Non-Residential Outside use	3.20	8.00

Non-Residential Customers			
	Flat Charge	All Winter Usage	All Summer Usage
Hydrant Meter Rental Off Site (per week)	\$73.70	\$3.95	\$8.50
Hydrant Meter Rental On Site (per day)	37.75	3.95	8.50
Residential Service Meter Rental (per week)	14.75	3.95	8.50

Source: Covington Water District

Outstanding Debt. As of January 23, 2013, Covington had outstanding \$8,865,000 principal amount of Water System Improvement and Refunding Revenue Bonds, 2013. In addition, as of December 31, 2012, Covington had outstanding Public Works Trust Fund Loans in the total principal amount of \$11,116,175.

Bond Resolution. Pursuant to Covington Resolution No. 3071, Covington has pledged the Gross Revenue of its Water System to pay the principal and interest of its outstanding revenue bonds, subject only to the payment of Operation and Maintenance Costs and less payments required under any Contract Resource Obligations (“Net Revenues”). Additionally the outstanding revenue bonds are secured by the gross amount of all assessments from any existing utility local improvement district (“ULID”) and connection charges. The revenue bonds are special obligations of Covington, payable only from the Bond Fund.

The Water System means Covington’s existing water supply system, as the same shall be added to, bettered, improved and extended, for as long as any parity revenue bonds are outstanding.

“Gross Revenue of the Water System” means all of the earnings and revenues received by Covington from the maintenance and operation of the Water System and all earnings from the investment of money on deposit in the various funds of Covington, including from the collection of connection charges. However, Gross Revenue shall not include principal proceeds of future parity bonds or other borrowings, assessments, government grants, tax proceeds,

earnings from investments in the reserve account, or earnings or proceeds from any investments in a trust, defeasance or escrow fund created to defease or refund Water System obligations (until commingled with other earnings and revenues of the Water System defined as Gross Revenue) or held in a special account for the purpose of paying rebate to the United States.

“Operation and Maintenance Costs” mean all expenses incurred by Covington in causing its Water System to be operated and maintained in good repair, working order and condition, including without limitation: deposits, premiums, assessment or other payments for insurance, if any, on the Water System, payments into pension funds, State-imposed taxes, and payments with respect to any other expenses of the Water System that are properly treated as maintenance and operation expenses under generally accepted accounting principles applicable to municipal corporations. The term Operation and Maintenance Costs does not include any depreciation or capital addition or capital replacements to the Water System.

Under the resolutions, Covington is to deposit all Gross Revenue of the Water System, except for earnings on the Bond Fund and other funds, to the Maintenance Fund, to be used for the following purposes in the following order of priority: (a) to pay Maintenance and Operation Expenses; (b) to pay principal of and interest on outstanding parity bonds; (c) to reimburse any provider of a municipal bond insurance policy; (d) to replenish the reserve account; (e) to pay any junior lien revenue obligation; and (f) to retire by redemption or purchase any outstanding revenue bonds or short-term revenue obligations of Covington, to make necessary additions, betterments, improvements and repairs to or extensions and replacements of the Water System, to make deposits into the Rate Stabilization Account, or for any other lawful Covington System purposes.

Covington has covenanted to establish, maintain and collect rates and charges for water service (and for all other utility services that may be provided by Covington’s System) which, together with collections of Assessments, will make available for the payment of principal of and interest on outstanding revenue bonds and any future parity bonds in an amount equal to at least 1.25 times average annual debt service.

Under the resolutions, Covington has reserved the right to issue future bonds with a lien on Net Revenue of the Covington System on a parity with the lien thereon of its outstanding revenue bonds, upon compliance with certain conditions set forth therein.

Certain Historical Results. The following table shows Covington's historical operating revenues (without connection revenue) from 2008 through 2012.

Covington Water District
Historical Financial Results for the Years 2008 – 2012

DEBT SERVICE WITH CONNECTION REVENUE	2008	2009	2010	2011	Preliminary 2012
OPERATING REVENUES:					
Water Service	\$8,332,391	\$9,375,498	\$9,106,885	\$9,249,831	\$10,116,126
Street Light Service	155,370	172,908	175,620	177,962	178,431
Other Revenue	160,997	413,774	433,889	465,501	437,720
TOTAL OPERATING REVENUES	\$8,648,758	\$9,965,180	\$9,716,394	\$9,893,294	10,732,277
OPERATING EXPENSES (1):					
Total Production Costs	\$ 485,505	\$ 558,923	\$ 291,038	\$ 326,460	\$293,611
Total Purchased Water	769,692	811,211	726,226	499,203	485,621
Facility Operations Division	1,096,540	1,036,400	1,124,423	1,034,474	1,066,957
Engineering Division	323,137	503,839	300,323	244,386	294,256
Water Resource & Env'tl. Division	397,138	433,328	465,669	462,291	508,386
Business Services Department	1,467,581	1,527,447	1,564,977	1,586,357	1,620,087
Administration	1,278,413	1,517,666	1,501,955	1,457,780	1,458,027
Street Light Expense	145,989	144,174	147,799	150,184	151,074
Taxes	424,509	424,946	427,579	447,539	482,503
Contract Resource Obligation Payments (2)	996,479	940,282	948,674	1,483,139	1,398,479
TOTAL OPERATING EXPENSES	\$7,384,983	\$7,898,216	\$7,498,663	\$7,691,813	\$7,759,001
NET OPERATING INCOME (LOSS) BEFORE RESERVE	\$1,263,775	\$2,066,964	\$2,217,731	\$2,201,481	\$2,973,276
NONOPERATING REVENUES (EXPENSES) (3)					
Interest Income (4)	\$ 702,801	\$ 386,013	\$ 181,891	\$ 110,778	\$209,258
Miscellaneous Income	12,456	12,768	12,768	12,768	12,768
TOTAL NONOPERATING REVENUE	\$ 715,257	\$ 398,781	\$ 194,659	\$ 123,546	\$ 222,026
CAPITAL CONTRIBUTIONS (5)					
Connection Charges (6)	\$5,012,924	\$ 744,690	\$1,589,338	\$ 595,707	\$1,508,104
TOTAL AVAIL./DEBT SERVICE	\$6,991,956	\$3,210,435	\$4,001,728	\$2,920,734	\$4,703,406
DEBT SERVICE REQUIREMENTS	\$ 903,013	\$ 911,158	\$ 405,787	\$ 405,289	\$ 403,326
BOND DEBT COVERAGE RATIO	7.74x	3.52x	9.86x	7.21x	11.66x

(1) Excludes depreciation.

(2) Payments for the Regional System.

(3) Excludes loss on sale of assets, interest expense on debt financing, and amortized debt discounts.

(3) Excludes interest from restricted funds.

(4) Excludes donated capital assets.

(5) Includes meter installation charges and facility charges.

Source: Covington

Lakehaven Utility District

Under the Second Supply Project Agreement, the Lakehaven Utility District (“Lakehaven”) is entitled to use its Participant Share of the Project and is obligated to pay its Participant Share of Project Costs. Lakehaven is not responsible for paying debt service on the 2010 Bonds or the Bonds. See “THE SECOND SUPPLY PROJECT—Project Participants.” Lakehaven has a combined water and sewer system. The following provides a brief summary of Lakehaven and its financial condition.

Introduction. Lakehaven was incorporated in 1956. In 1985, voters authorized the consolidation of King County Water District No. 124 into Lakehaven Sewer District. In conjunction with this merger, Lakehaven Sewer District changed its name to “Federal Way Water and Sewer District.” A merger with King County Water District No. 56 was completed in 1987. In 1994, Lakehaven changed its name to “Lakehaven Utility District,” as it is now known.

Lakehaven is located in the southwest corner of King County adjacent to the Pierce County boundary. Puget Sound and the Green River Valley border Lakehaven on the west and east respectively. Lakehaven’s northern border generally follows South 280th Street, except for a narrow strip of land extending north along the Puget Sound to South 252nd Street. Lakehaven provides service to most of the City of Federal Way and to small portions of the cities of Auburn, Pacific, Tacoma, Des Moines, and Milton. In addition, Lakehaven serves an unincorporated area of King County approximately 18 square miles north of Federal Way and west of Auburn. Lakehaven encompasses an area of approximately 35 square miles with a service population of approximately 112,000 people. Lakehaven is primarily residential in character with approximately 75% of the land area devoted to single-family dwellings.

Lakehaven is governed by a five-member Board of Commissioners, and managed under the direction of its General Manager. Lakehaven employs approximately 100 employees.

Water Supply. Lakehaven’s water system includes 450 miles of mainline, 24 wells, and 12 storage tanks with an approximate storage capacity of 31 million gallons. The average daily pumping rate is about 10 million gallons per day (“MGD”). Lakehaven’s sewer system includes 350 miles of mainline, 27 pump stations and two secondary wastewater treatment plants. The Redondo Plant is designed for an average flow of 5.6 MGD. The Lakota Plant is designed for an average flow of 10.0 MGD.

Customer Information. Lakehaven provides water service to approximately 29,235 accounts, 93% of which are residential. Customer data and usage by class for the last five years is presented below.

Lakehaven Customer Usage By Class (ccf)

	2008	2009	2010	2011	2012
Residential	3,746,930	3,912,350	3,406,973	3,303,746	3,354,123
Non-residential	889,129	844,940	948,540	905,105	1,052,162
Total	4,572,282	4,757,290	4,355,513	4,208,851	4,406,285

Source: Lakehaven

Lakehaven Annual Water Billing (in \$1000)

	2008	2009	2010	2011	2012
Residential	\$6,642	\$7,494	\$8,274	\$9,350	\$10,436
Non-residential	1,601	1,817	1,999	2,279	2,623
Total	\$8,243	\$9,311	\$10,273	\$11,629	\$13,059

Source: Lakehaven

The following table shows Lakehaven's five largest customers based on billings in 2012.

Lakehaven's Largest Customers

Customer Name	Consumption (ccf)	Amount
Fairfield Glen Park LLC	38,669	\$ 464,711
Campus Grove	28,280	348,783
KW Multi-Family Management Group	24,988	265,210
Weidner Apartment Homes	17,812	263,493
St Croix	19,570	262,643

Source: Lakehaven

Water Rates.

Lakehaven's Water Rates Effective January 1, 2012

Customer Classification	Meter Size	Fixed Monthly	Bi-Monthly Fee	Plus (+)	Block One 0-16 CCF	Block Two 17-30 CCF	Block Three 31-50 CCF	Block Four Over 50 CCF
Single Family Residential	5/8"	\$11.30	\$22.60	Plus	\$1.43	\$2.86	\$4.29	\$5.72
	3/4"	15.24	30.48	Plus	1.43	2.86	4.29	5.72
	1"	23.10	46.20	Plus	1.43	2.86	4.29	5.72
	1-1/2"	42.76	85.52	Plus	1.43	2.86	4.29	5.72
	2"	66.36	132.72	Plus	1.43	2.86	4.29	5.72

Customer Classification	Meter Size	Fixed Monthly	Bi-Monthly Fee	Plus (+)	Winter Per CCF	Summer Per CCF
Non-Residential (Commercial, Irrigation, Public Authority)	5/8"	\$11.30	\$22.60	Plus	\$1.61	\$3.74
	3/4"	15.24	30.48	Plus	1.61	3.74
	1"	23.10	46.20	Plus	1.61	3.74
	1-1/2"	42.76	85.52	Plus	1.61	3.74
	2"	66.36	132.72	Plus	1.61	3.74
	3"	129.28	258.56	Plus	1.61	3.74
	4"	200.06	400.12	Plus	1.61	3.74
	6"	396.69	793.38	Plus	1.61	3.74

Dormant Charge for Irrigation	\$11.30	\$22.60
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Multi-Family Residential (Per Dwelling Unit)	Fixed Monthly	Bi-Monthly Fee	Plus (+)	Winter Per CCF	Summer Per CCF
	\$6.70	\$13.40	Plus	\$1.55	\$1.70

Fire Sprinkler	Meter Size	Fixed Monthly	Bi-Monthly Fee	Plus (+)	Winter Per CCF	Summer Per CCF
	5/8"	\$6.02	\$12.04	Plus	\$1.61	\$3.74
	3/4"	7.21	14.42	Plus	1.61	3.74
	1"	9.61	19.22	Plus	1.61	3.74
	1-1/2"	15.57	31.14	Plus	1.61	3.74
	2"	22.73	45.46	Plus	1.61	3.74
	3"	41.84	83.68	Plus	1.61	3.74
	4"	63.34	126.68	Plus	1.61	3.74
	6"	123.03	246.06	Plus	1.61	3.74

Source: Lakehaven

**Lakehaven's Sewer Rates
Effective January 1, 2012**

	FIXED MONTHLY	FIXED BI- MONTHLY	USAGE CHARGE PER CCF
Single/Multi- Family Residential	\$11.67	\$23.34	\$2.48 (usage based on wet month average)
King County/METRO	11.67	23.34	4.08 (usage based on wet month average)
Pierce County	11.67	23.34	3.22 (usage based on wet month average)

Non-Residential	FIXED MONTHLY	FIXED BI- MONTHLY	CCF
CDC #1	\$11.67	\$23.34	\$2.48
CDC #2	11.67	23.34	3.93
CDC #3	11.67	23.34	5.37
CDC #4	11.67	23.34	6.81
CDC #5	11.67	23.34	8.25
Pierce County CDC #1	11.67	23.34	3.22
Pierce County CDC #2	11.67	23.34	4.66
Edgewood CDC #1	16.67	33.34	3.43
Edgewood CDC #2	16.67	33.34	4.82

Source: Lakehaven

Outstanding Debt. As of December 31, 2012, Lakehaven had outstanding \$9,890,000 of its Water and Sewer Revenue Refunding Bonds, 2005 (the "2005 Bonds"), as well as \$10,150,348 in Public Works Trust Fund Loans. Lakehaven expects to refund its outstanding 2005 Bonds within the next six months.

Bond Resolution. Pursuant to Lakehaven Resolution No. 2005-1039 authorizing Lakehaven's 2005 Bonds, such bonds are secured by a pledge of the Net Revenues of the Lakehaven System (as described below). The 2005 Bonds are further secured by a lien on any Utility Local Improvement District ("ULID") Assessments levied in any future ULID if the bonds secured by these ULID Assessments are issued on a parity of lien with Lakehaven's outstanding water and sewer revenue bonds. The 2005 Bonds are special fund revenue obligations of Lakehaven, payable solely from the bond fund into which is deposited Net Revenue of the Lakehaven System.

"System" means the existing combined water supply and distribution system and sanitary sewage collection and disposal system of Lakehaven, and any additional utility combined therein pursuant to law, as the same shall be added to, bettered, improved and extended, for as long as any of the parity water revenue bonds of Lakehaven are outstanding.

"Gross Revenue" is defined to include all of the earnings and revenues received by Lakehaven from the ownership, maintenance and operation of the System and all earnings from the investment of money on deposit in the various funds of Lakehaven (except earnings produced by amounts or securities in any other refunding or defeasance escrow), and all connection and capital improvement charges collected for the purpose of defraying the costs of capital facilities of the System, and excluding Assessments, government grants, tax proceeds and principal proceeds of bonds or other obligations of Lakehaven.

"Net Revenue" is defined as Gross Revenue less Maintenance and Operation Expenses.

"Maintenance and Operation Expenses" are defined to mean all expenses incurred by Lakehaven in causing the System to be operated and maintained in good repair, working order and condition, including all administrative and other expenses attributable to the System, and payments to other entities for the transmission, treatment and disposal of sewage, and the supply, transmission, delivery and storage of water, but shall not include any depreciation expenses or Lakehaven or city levied taxes or charges in lieu of taxes.

Gross Revenue of the Lakehaven System, except for earnings on the Bond Fund and funds other than the Maintenance Fund, shall be credited to the Maintenance Fund of Lakehaven to be used only for the following purposes, in the following order of priority: (a) to pay Maintenance and Operation Expenses; (b) to pay principal of

and interest on outstanding parity bonds; (c) to replenish the Reserve Account; (d) to pay junior lien revenue obligations; and (e) to retire by redemption or to purchase any outstanding revenue bonds or other revenue obligations of Lakehaven, to make necessary additions, betterments, improvements and repairs to or extensions and replacements to the Water System, or for any other lawful Lakehaven purpose.

Under the resolutions, Lakehaven has covenanted to meet a Coverage Requirement, defined as Net Revenue of the System at least equal to 1.25 times the annual debt service in that current year on applicable bonds which are not Assessment Bonds and also at least equal to the annual debt service in that year plus Reserve Policy Costs, plus Net Revenue of the System (not used in the coverage calculation for bonds which are not Assessment Bonds), together with collections on Assessments, at least equal to 1.00 times the Annual Debt Service in that current year on all Assessment Bonds.

Under the resolutions, Lakehaven has reserved the right to issue future bonds with a lien on Net Revenue of the System on a parity with the lien thereon of its outstanding water revenue bonds, upon compliance with certain conditions set forth therein.

Certain Historical Results. The following table shows historical operating revenues and expenses from 2008 through 2012.

Lakehaven Historical Financial Results					
	2008	2009	2010	2011	2012(1)
OPERATING REVENUES					
Customer Sales & Service Fees	\$ 20,162,542	\$ 21,986,967	\$ 23,515,438	\$ 25,782,962	\$ 27,739,207
Permits, Inspection & Delinquency Fees	320,512	328,794	362,200	425,487	445,840
Developer Revenues & Administrative Charges	399,983	339,124	415,318	391,050	344,147
Street Lighting Revenues	340,617	341,884	341,784	342,035	338,172
Total Operating Revenues	\$ 21,223,654	\$ 22,996,769	\$ 24,634,740	\$ 26,941,534	\$ 28,867,366
OPERATING EXPENSES					
Maintenance & Operations	\$ 12,451,911	\$ 12,831,892	\$ 13,079,946	\$ 12,656,365	\$ 11,815,407
Administrative & General	3,447,967	3,683,990	3,670,636	3,367,131	3,857,647
Depreciation and Amortization	7,684,971	7,152,585	7,384,939	7,543,156	7,319,640
Taxes, Other Than Income Tax	615,434	655,617	734,638	836,061	920,618
Total Operating Expenses	\$ 24,200,283	\$ 24,324,084	\$ 24,870,159	\$ 24,672,713	\$ 23,913,312
Net Operating Income	\$ (2,976,629)	\$ (1,327,315)	\$ (235,419)	\$ 2,268,821	\$ 4,954,054
NON-OPERATING INCOME (EXPENSE)(1)					
Interest Expense	\$ (1,042,010)	\$ (812,103)	\$ (798,475)	\$ (660,756)	\$ (922,381)
Amortization of Debt Expenses	(36,941)	(27,749)	(21,265)	(17,139)	(15,000)
Gain(Loss) on Disposal of Fixed Assets	8,107	8,016	(11,716)	(325,905)	(46,012)
Interest Income	579,405	271,931	187,614	441,759	346,918
Other Income	164,637	311,199	216,733	384,231	190,988
Total Non-Operating Income (Expense)	\$ (326,802)	\$ (248,706)	\$ (427,109)	\$ (447,810)	\$ (430,485)
Net Income to Retained Earnings	\$ (3,303,431)	\$ (1,576,021)	\$ (662,528)	\$ 1,791,011	\$ 4,523,567
Capital Contributions	\$ 5,868,034	\$ 3,444,864	\$ 2,899,093	\$ 2,329,617	\$ 5,208,768
Balance Available For Capital Improvements And Other Purposes	\$ 19,516,199	\$ 15,369,212	\$ 15,377,452	\$ 18,581,112	\$ 19,741,599
Total Debt Service	\$ 3,371,895	\$ 3,579,564	\$ 3,480,908	\$ 2,766,442	\$ 2,549,193
Debt Service Coverage					
Assessment	29.76	20.89	104.86	N/A	N/A
Non-Assessment	2.15	2.16	2.64	3.83	5.16

(1) Unaudited.

Source: Lakehaven

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APPENDIX C

BOOK-ENTRY SYSTEM

The following information has been provided by the Depository Trust Company, New York, New York (“DTC”). The City makes no representation regarding the accuracy or completeness thereof, or for the absence of material changes in such information subsequent to the date hereof. Beneficial Owners (as hereinafter defined) should therefore confirm the following with DTC or the Participants (as hereinafter defined).

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

DTC, the world’s largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has a Standard & Poor’s rating of AA+. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com (which website is not incorporated by reference).

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

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

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

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

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

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

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

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

APPENDIX D
CITY OF TACOMA WATER SYSTEM
2011 AND 2012 FINANCIAL STATEMENTS

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ANNUAL

TACOMA WATER

2012

**FINANCIAL
REPORT**



Public Utility Board

LAURA FOX

Chair

DAVID NELSON

Vice-Chair

WOODROW JONES

Secretary

BRYAN FLINT

Member

MARK PATTERSON

Member

WILLIAM A. GAINES
Director of Utilities/CEO

LINDA MCCREA
Superintendent

ANDREW CHERULLO
Finance Director

DEPARTMENT OF PUBLIC UTILITIES
CITY OF TACOMA

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES

TACOMA WATER

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FINANCIAL DATA

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REPORT OF INDEPENDENT AUDITORS

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

Report on Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Washington Department of Public Utilities, Water Division (the Division), which comprise the Statements of Net Position as of December 31, 2012 and 2011, 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Division as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis on pages 5 through 11 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.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedules presented on pages 40 through 67 are not a required part of the basic financial statements, but are supplemental information presented for the purposes of additional analysis. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and, accordingly, we express no opinion on it.

A handwritten signature in blue ink that reads "Miss Adams LLP". The signature is written in a cursive, flowing style.

Portland, Oregon
April 3, 2013

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis of Tacoma Water's (the Utility) financial performance provides an overview of the financial activities for the years ended December 31, 2012 and 2011. 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 accounting principles generally accepted in the United States of America applied on a consistent basis and includes 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, 2012 and 2011, 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 Utility'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 the financial statements provide additional disclosures that are essential to a full understanding of the data provided in the financial statements. They are an integral part of the Utility's presentation of financial position, results of operations and changes in cash flows.

Financial Highlights

- The assets of Tacoma Water exceeded its liabilities by \$452.9 million in 2012, \$429.2 million in 2011 and by \$417.7 million in 2010. Of these amounts, \$42.5 million in 2012, \$22.0 million in 2011, and \$13.7 million in 2010 were available to meet Tacoma Water's ongoing obligations to citizens and creditors.
- Tacoma Water's total net positions increased by \$23.7 million in 2012, \$11.5 million in 2011 and \$5.1 million in 2010.
- Tacoma Water's operating revenues were \$80.7 million, an increase of \$15.3 million, compared to \$65.4 million in 2011 due to an average water rate increase of 5.2% and other operating revenues and contract resource obligations. Operating revenues increased \$2.4 million in 2011 compared to 2010 operating revenues of \$63.0 million.
- In 2012, Tacoma Water's net utility plant of \$722.9 million represented an increase of \$61.7 million over the 2011 \$661.2 million balance. Major projects contributing to the increase include the Green River Water Filtration Facility and Main Replacement Projects. Utility plant increased \$24.6 million over the 2010 \$636.6 million balance.
- Tacoma Water's current assets increased by \$25.0 million during 2012 and increased \$1.2 million during 2011. The increases in 2012 are primarily in operating fund cash and accounts receivable. Current assets decreased by \$5.6 million during 2010.

- Tacoma Water's Long-Term Debt decreased by \$10.6 million during 2012, decreased \$3.5 million during 2011 and increased \$129.1 million during 2010. The increase in 2010 are due to the bond issuances for the Green River Water Filtration Facility.
- The Utility transferred \$5.0 million of revenues into the Rate Stabilization account.

Overview of the Financial Statements

The Utility reported operating income of \$29.3, \$15.1 and \$10.9 million for 2012, 2011 and 2010 respectively. In 2012, operating revenues increased by \$15.3 million while operating expenses increased \$1.0 million.

Net income was \$23.7, \$11.5 and \$5.1 million in 2012, 2011 and 2010 respectively. Non-operating revenues net of expenses decreased \$0.2 million. Capital contributions for 2012 decreased \$1.4 million compared to a decrease of \$0.5 million in 2011. The decrease in 2012 reflects a \$5.0 million transfer to the rate stabilization fund.

The following table highlights Tacoma Water's operating results for the years 2012 - 2010.

Operating Results (In thousands)

	2012	2011	2010	12/11 Increase (Decrease)	11/10 Increase (Decrease)
Operating Revenues	\$ 80,681	\$ 65,404	\$ 62,987	\$ 15,277	\$ 2,417
Operating Expenses	51,350	50,318	52,072	1,032	(1,754)
Operating Income	29,331	15,086	10,915	14,245	4,171
Net Non-Operating Income (Expense)	(12,087)	(11,889)	(12,771)	(198)	882
Capital Contributions	7,834	9,251	9,714	(1,417)	(463)
Federal BAB Subsidies and Grants	3,841	4,006	2,355	(165)	1,651
Transfers Out	(5,227)	(4,961)	(5,111)	(266)	150
Change in Net Position	\$ 23,692	\$ 11,493	\$ 5,102	\$ 12,199	\$ 6,391

Net Position

Net position may serve over time as a useful indicator of the Utility's financial position. Assets exceeded liabilities by \$452.9, \$429.2 and \$417.7 million for 2012, 2011 and 2010 respectively. Net position increased \$23.7 million in 2012 mainly due to increased operating revenues of \$15.3 million partially offset by increased operating and non-operating expense of \$0.7 million. In addition, contributions decreased \$1.4 million and transfers increased \$0.3 million.

Net investment in capital assets represents the Utility's equity investment in capital assets. In 2012, this amounted to \$384.7 million, an increase of \$2.3 million compared to 2011. Investment in capital assets in 2011 was \$382.4 million representing an increase of \$1.1 million compared to 2010.

Restricted net position for 2012 was \$25.6 million, an increase of \$0.9 million from 2011. Restricted net position for 2011 was \$24.7 million, reflecting an increase of \$2.0 million from 2010.

In 2012, unrestricted net position increased \$20.5 million to \$42.5 million. Unrestricted net position for 2011 was \$22.0 million, representing an increase of \$8.4 million from 2010 balance of \$13.7 million.

The analysis below highlights changes in Tacoma Water's net position for the years 2012, 2011 and 2010.

Tacoma Water's Net Position

(In thousands)

Description	2012	2011	2010	12/11 Increase (Decrease)	11/10 Increase (Decrease)
Net Utility & Non-Utility Plant	\$ 723,400	\$ 661,701	\$ 637,140	\$ 61,699	\$ 24,561
Current and Other Assets	227,809	255,451	276,789	(27,642)	(21,338)
Total Assets	<u>\$ 951,209</u>	<u>\$ 917,152</u>	<u>\$ 913,929</u>	<u>\$ 34,057</u>	<u>\$ 3,223</u>
Net Position:					
Net Investment in Capital					
Assets	\$ 384,739	\$ 382,444	\$ 381,316	\$ 2,295	\$ 1,128
Restricted	25,635	24,727	22,728	908	1,999
Unrestricted	42,506	22,017	13,651	20,489	8,366
Total Net Position	<u>452,880</u>	<u>429,188</u>	<u>417,695</u>	<u>23,692</u>	<u>11,493</u>
Long-Term Debt	409,181	419,801	423,577	(10,620)	(3,776)
Current and Other LT Liabilities	89,148	68,163	72,657	20,985	(4,494)
Total Liabilities	<u>498,329</u>	<u>487,964</u>	<u>496,234</u>	<u>10,365</u>	<u>(8,270)</u>
Total Net Position and Liabilities	<u>\$ 951,209</u>	<u>\$ 917,152</u>	<u>\$ 913,929</u>	<u>\$ 34,057</u>	<u>\$ 3,223</u>

Revenues

Total operating revenues in 2012 were \$80.7 million an increase of \$15.3 million (23.4%) compared to 2011. Total operating revenues increased \$2.4 million (3.8%) in 2011 compared to 2010. In 2012 an average rate increase of 5.2% effective January 1, 2012 and higher usage resulted in increased water sales of \$3.3 million (5.8%). In addition, other operating revenue increased \$5.6 million largely due to a \$5.0 million minimum daily purchase agreement restructuring and finally, contract obligations for the Regional Water Supply System (RWSS) partners increased \$6.4 million.

The following table highlights water sales by type of customer for 2012, 2011 and 2010.

Water Sales

(In thousands)

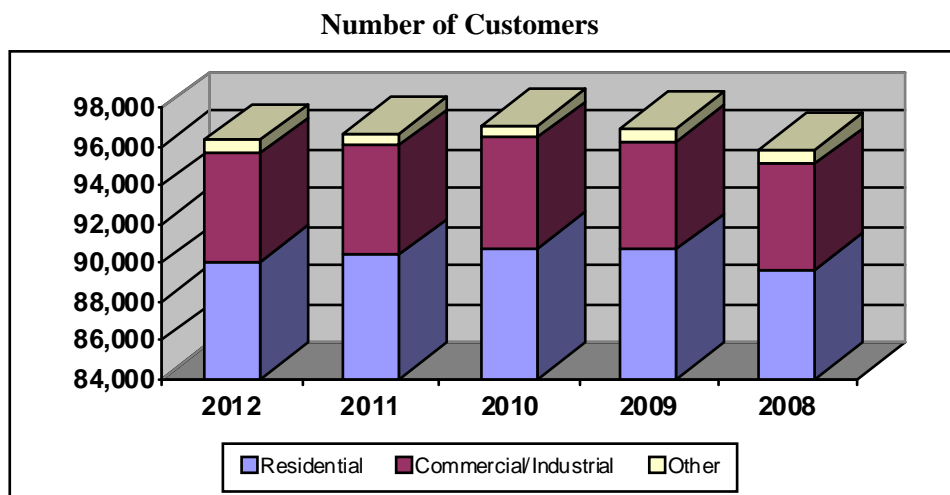
Type of Customer	2012	2011	2010	12/11 Increase (Decrease)	11/10 Increase (Decrease)
Residential and Domestic	\$ 38,686	\$ 36,682	\$ 35,454	\$ 2,004	\$ 1,228
Commercial and Industrial	10,621	10,101	10,050	520	51
Special Rate – Simpson Tacoma	5,032	4,774	3,799	258	975
Municipal	383	400	364	(17)	36
Other Public Buildings and Grounds	1,910	1,816	1,702	94	114
Sale to Other Utilities	2,090	1,625	1,530	465	95
Unbilled Revenue	417	479	(648)	(62)	1,127
Total	<u>\$ 59,139</u>	<u>\$ 55,877</u>	<u>\$ 52,251</u>	<u>\$ 3,262</u>	<u>\$ 3,626</u>

In 2012, approximately 65.4% of water sales were to residential and domestic customers compared to 65.6% in 2011 and 67.9% in 2010. In 2012, commercial and industrial sales were 18.0% compared to 18.1% in 2011 and 19.2% in 2010. Special rate sales to Simpson Tacoma Kraft were 8.5% of total sales in 2012 and 2011 compared to 7.3% in 2010.

Customers

Over the last five years, the overall number of customers has remained relatively stable. In 2012, 93.5% of all customers were residential, 5.8% were commercial and industrial, with 0.7% in the other customer classes.

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

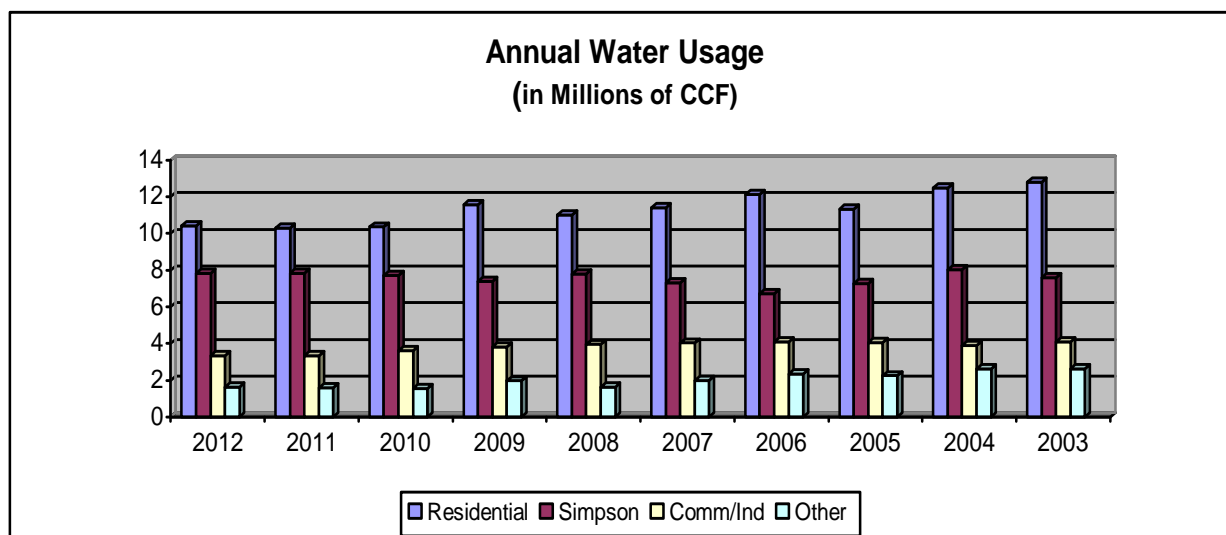


Water Users

The Utility generates the majority of its revenues from its residential and domestic customer base. Residential customers used 10.4 million CCF (100 cubic feet) (44.9%) of the 23.2 million CCF consumed by the Utility's customers in 2012; Simpson Tacoma Kraft Company used approximately 7.8 million CCF (33.8%); commercial and industrial customers used 3.3 million CCF (14.4%); the remaining 1.6 million CCF (6.9%) consumed by other customers.

Looking at the 10-year water usage trend, 2003 was the highest year with 27.11 million CCF, and 2011 was the lowest year with 23.0 million CCF. The trend indicates a general decline in usage since 2003 which reflects the result of plumbing code changes, conservation activities and reduced wholesale consumption.

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



Expenses

In 2012, operating expenses increased \$1.0 million (2.1%), compared to a decrease of \$1.8 million in 2011.

Source of Supply expense decreased by \$0.4 million (8.0%) because the Utility implemented a new work schedule that allowed downsizing of the workforce during 2012, in addition to regulatory work ending in 2011. Transmission and Storage expense decreased by \$0.3 million (13.2%) largely due to a onetime adjustment for electricity expense in 2012.

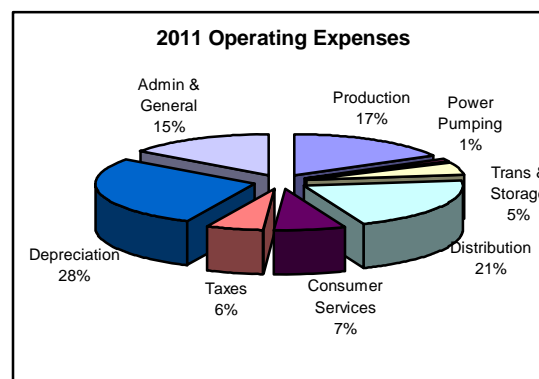
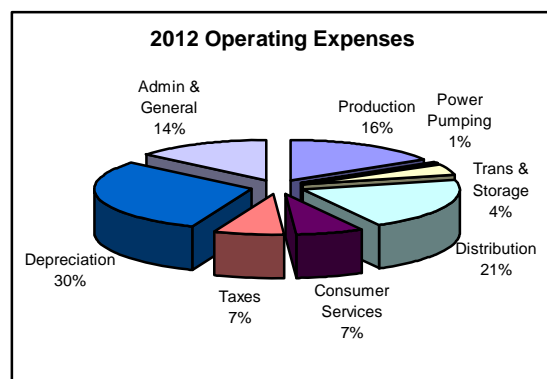
Depreciation expenses increased by \$0.9 million (6.1%) in 2012 mainly due to increase in depreciable asset by \$46.4 million during 2011. Tax expenses increased by \$0.4 million (12.2%) in 2012 largely due to increased water revenues. Customer Accounting and Consumer Services expense increased \$0.2 million (6.6%) in 2012 largely due to computer upgrades and SAP software related expenses.

The following table highlights Tacoma Water's operating expenses for 2012 – 2010.

Operating Expenses (In thousands)

Category	2012	2011	2010	12/10 Increase (Decrease)	11/10 Increase (Decrease)
Source of Supply	\$ 5,044	\$ 5,485	\$ 5,310	\$ (441)	\$ 175
Water Treatment	3,335	3,119	3,400	216	(281)
Total Production Expense	8,379	8,604	8,710	(225)	(106)
Power Pumping Expense	280	306	282	(26)	24
Transmission and Storage Expense	2,273	2,619	2,525	(346)	94
Distribution Expense	10,633	10,367	12,232	266	(1,865)
Customer Accounting and Service	3,833	3,594	3,460	239	134
Taxes	3,485	3,107	3,143	378	(36)
Depreciation	15,263	14,390	14,475	873	(85)
Administrative and General	7,204	7,331	7,244	(127)	87
Total Operating Expenses	\$ 51,350	\$ 50,318	\$ 52,071	\$ 1,032	\$ (1,753)

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



Capital Assets–Utility Plant

Tacoma Water invests in a broad range of utility assets and at the end of 2012 had \$722.9 million in net utility plant, an increase of \$61.7 million from 2011. The largest increase was in construction work in progress of \$43.1 million largely from the Green River Water Filtration construction project. In 2011, Tacoma Water had \$661.2 million in net utility plant, an increase of \$24.6 million compared to 2010. In 2012, 12.7 miles of water main were added or replaced compared to 11.4 miles in 2011; and 6.9 miles in 2010. The effect of the economic turnaround continues to be slow for private development activity. Construction was completed on 12

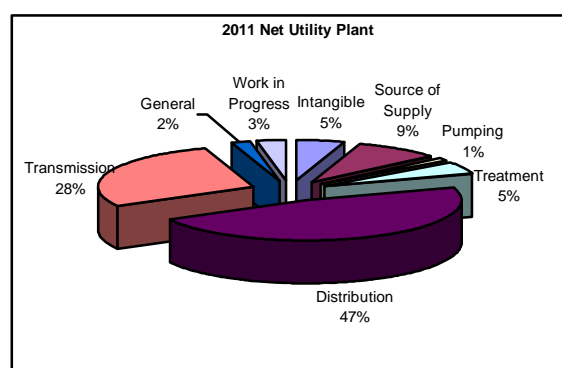
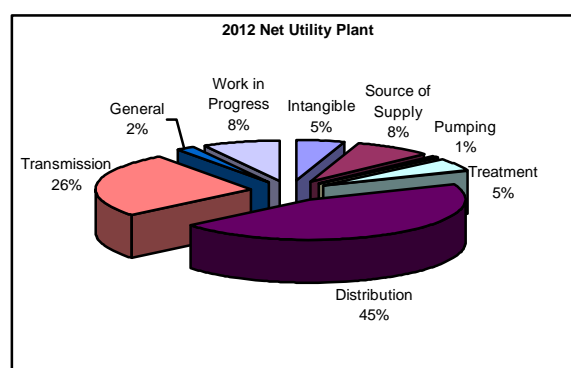
private contracts in 2012, resulting in 2.44 miles; 8 private contracts in 2011, added 2.0 miles; and 8 private contracts in 2010, added 0.9 miles.

The following table summarizes Tacoma Water's capital assets, net of accumulated depreciation, for the years ended December 31, 2012, 2011 and 2010.

Capital Assets, Net of Accumulated Depreciation
(In thousands)

Net Utility Plant	2012	2011	2010	12/10 Increase (Decrease)	11/10 Increase (Decrease)
Intangible Plant	\$ 35,086	\$ 34,865	\$ 34,818	\$ 221	\$ 47
Source of Supply Plant	60,843	60,174	61,534	669	(1,360)
Pumping Plant	6,037	6,180	6,385	(143)	(205)
Water Treatment Plant	33,244	34,744	36,328	(1,500)	(1,584)
Transmission Plant	187,349	186,002	157,878	1,347	28,124
Distribution Plant	326,563	312,427	298,735	14,136	13,692
General Plant	14,189	10,334	9,584	3,855	750
Construction Work In Progress	59,541	16,427	31,331	43,114	(14,904)
Total	<u>\$ 722,852</u>	<u>\$ 661,153</u>	<u>\$ 636,593</u>	<u>\$ 61,699</u>	<u>\$ 24,560</u>

The following graphs provide a visual presentation of the allocation of Tacoma Water's capital investment in 2012 and 2011.



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

Debt Administration

As of year-end 2012, the Utility had outstanding revenue bond obligations of \$369.5 million (net of unamortized bond premiums); a decrease of \$7.3 million (1.9%) from 2011. In 2011, Tacoma Water had outstanding revenue bond obligations of \$376.8 million (net of unamortized bond premiums); a decrease of \$6.8 million (1.8%) from 2010.

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

The Utility is required by bond covenants to maintain debt service coverage ratio of 1.25 for principle and interest. Debt service coverage ratios were 2.02, 1.58, 1.64 in 2012, 2011 and 2010 respectively.

At the end of 2012, the Utility had an outstanding State loan balance of \$42.0 million compared to \$43.6 million in 2011 and \$40.0 million in 2010. During 2012, the Utility received an additional \$0.5 million against the 2008 Public Works Trust Fund Loan and \$0.4 million against the 2008 Drinking Water State Revolving Fund Loan. The Utility entered into three more

Drinking Water State Revolving Loan agreements for McMillin Reservoir and the Water Treatment Facility in 2012 totaling \$24.2 million for which no funds have been drawn.

Additional information on the Utility'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 information in this annual report. We prepared the financial statements according to accounting principles generally accepted in the United States of America and they fairly portray Tacoma Water's financial position and operating results.

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

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



William A. Gaines
Director of Utilities/CEO



Andrew Cherullo
Finance Director

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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATEMENTS OF NET POSITION

	DECEMBER 31,	
ASSETS	2012	2011
UTILITY PLANT		
In Service, at Original Cost	\$820,187,184	\$793,903,858
Less - Accumulated Depreciation	(156,876,447)	(149,177,559)
Total	663,310,737	644,726,299
Construction Work In Progress	59,541,533	16,426,998
Net Utility Plant	722,852,270	661,153,297
NON-UTILITY PROPERTY	547,480	547,480
RESTRICTED ASSETS		
Construction Funds	58,833,459	125,330,650
Debt Service Funds	3,318,052	3,091,834
Bond Reserve Funds	19,507,744	19,512,184
System Development Charge Fund	53,626,384	47,111,039
Other Cash and Equity in Pooled Investments	25,564,985	17,495,079
Notes & Contracts Receivable - SDC & Other	464,971	1,530,840
Total Special Funds	161,315,595	214,071,626
CURRENT ASSETS		
Operating Funds Cash and Equity in		
Pooled Investments	37,666,496	18,958,145
Accounts Receivable	10,503,161	5,693,200
(Net of Allowance for Doubtful Accounts		
of \$453,928 in 2012 and \$516,177 in 2011)		
BABs Interest Subsidies Receivable	320,064	320,064
Accrued Unbilled Revenues	4,026,679	3,609,693
Materials and Supplies	2,341,174	2,503,854
Interfund Receivable	947,380	68,381
Prepayments.....	602,606	250,184
Total Current Assets	56,407,560	31,403,521
OTHER ASSETS		
Unamortized Issuance Costs	3,021,623	3,255,278
Regulatory Asset-Public Fire Protection Fees ...	4,274,592	3,514,579
Regulatory Asset-Hyada Surcharges	1,025,593	1,149,511
Unamortized Losses on Refunding Bonds	1,764,332	2,056,555
Total Other Assets	10,086,140	9,975,923
TOTAL ASSETS	<u>\$951,209,045</u>	<u>\$917,151,847</u>

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

	DECEMBER 31,	
NET POSITION AND LIABILITIES	2012	2011
NET POSITION		
Net Investment in Capital Assets	\$384,739,201	\$382,443,716
Restricted for:		
Regional Water Supply System Construction Fund .	-	360,122
Water Assurance and System Development Charge ..	24,265,546	23,113,760
Debt Service Funds	1,368,679	1,253,432
Unrestricted	42,506,333	22,017,058
Total Net Position	452,879,759	429,188,088
LONG-TERM DEBT, NET OF CURRENT MATURITIES		
Revenue Bonds	362,310,380	370,169,234
Public Works Trust Fund Loans	23,495,090	25,136,305
Drinking Water State Revolving Fund Loan	15,659,868	15,958,759
Muckleshoot Agreements	7,715,713	8,536,459
Total Long-Term Debt	409,181,051	419,800,757
CURRENT LIABILITIES		
Current Maturities of Long-Term Liabilities	10,842,324	9,250,850
Accrued Taxes	1,595,790	1,174,893
Accrued Expenses and Contracts Payable	17,996,478	3,801,668
Salaries, Wages and Fringe Benefits Payable	1,063,601	1,019,509
Interest Payable	1,949,375	1,838,402
Customers' Deposits	265,961	269,732
Interfund Payables	1,371,061	819,643
Total Current Liabilities	35,084,590	18,174,697
LONG-TERM LIABILITIES		
Retained on Contract Payments	22,000	27,000
Customer Advances for Construction	4,356,297	4,563,137
Deferred Revenue	8,968,764	9,967,221
Rate Stabilization	35,575,447	30,575,447
Long-Term Accrued Compensated Absences	2,122,259	2,201,281
Other Long-Term Liabilities	3,018,878	2,654,219
Total Long-Term Liabilities	54,063,645	49,988,305
TOTAL LIABILITIES	498,329,286	487,963,759
TOTAL NET POSITION AND LIABILITIES	\$951,209,045	\$917,151,847

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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,	
	2012	2011
OPERATING REVENUES		
Sale of Water	\$59,138,998	\$55,877,567
Other Operating Revenues	11,381,473	5,748,678
Contract Resource Obligation Revenues	10,160,260	3,777,789
Total Operating Revenues	80,680,731	65,404,034
OPERATING EXPENSES		
Operations	13,186,350	13,292,512
Production	8,379,807	8,603,834
Administrative and General	11,036,295	10,925,265
Depreciation	15,262,686	14,389,681
Other Taxes	3,485,243	3,106,516
Total Operating Expenses	51,350,381	50,317,808
Net Operating Income	29,330,350	15,086,226
NON-OPERATING REVENUES (EXPENSES)		
Interest Income	2,320,753	3,141,374
Other	288,182	(12,371)
Interest on Long-Term Debt	(19,706,065)	(19,997,829)
Amortization of Debt Expense, Premium and Loss on Refunding	127,976	1,605
Interest Charged to Construction	4,881,993	4,977,850
Total Non-Operating Expenses	(12,087,161)	(11,889,371)
Net Income Before Capital Contributions and Transfers	17,243,189	3,196,855
Capital Contributions		
Cash	4,571,007	8,134,128
Donated Fixed Assets	3,263,338	1,116,549
Federal BAB Subsidies	3,840,767	3,840,771
Grants	-	165,438
Transfers		
City of Tacoma Gross Earnings Tax	(5,081,191)	(4,931,504)
Transfer to/from Other Funds	(145,439)	(29,232)
CHANGE IN NET POSITION	23,691,671	11,493,005
TOTAL NET POSITION - BEGINNING OF YEAR	429,188,088	417,695,083
TOTAL NET POSITION - END OF YEAR	\$452,879,759	\$429,188,088

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,	
	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash from Customers	\$74,829,339	\$64,773,377
Cash Paid to Suppliers	1,127,154	(12,715,293)
Cash Paid to Employees	(20,102,470)	(19,863,291)
Taxes Paid	(3,064,346)	(3,059,275)
Net Cash From Operating Activities	52,789,677	29,135,518
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Transfer to Other Funds	(145,439)	(29,232)
Transfer Out for Gross Earnings Tax	(5,081,191)	(4,931,504)
Net Cash From Non-Capital Financing Activities	(5,226,630)	(4,960,736)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital Expenditures, net.....	(68,816,329)	(32,855,808)
Proceeds from PWTF Loan	900,000	5,984,023
Debt Issuance Costs	-	(64,808)
Principal Payments on Long-Term Debt	(9,274,378)	(8,915,056)
Interest Paid	(19,595,092)	(22,055,215)
BABs Federal Interest Subsidies	3,840,767	4,459,254
Grants Received	-	165,438
System Development Charges, CIAC and Other	9,791,238	7,022,698
Net Cash From Capital and Related Financing Activities	(83,153,794)	(46,259,474)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest Received on Investments	2,320,753	3,141,374
Other Net Non-Op Revenues and Expenses	288,183	(12,371)
Net Cash From Investing Activities	2,608,936	3,129,003
Net Change in Cash and Equity in Pooled Investments	(32,981,811)	(18,955,689)
Cash & Equity in Pooled Investments at January 1 ...	231,498,931	250,454,620
Cash & Equity in Pooled Investments at December 31 .	<u>\$198,517,120</u>	<u>\$231,498,931</u>

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

	YEAR ENDED DECEMBER 31,	
	2012	2011
Reconciliation of Net Operating Income to Net Cash From Operating Activities:		
Net Operating Income	\$29,330,350	\$15,086,226
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	15,262,686	14,389,681
Cash from changes in operating assets and liabilities:		
Accounts Receivable and Unbilled Revenue	(5,226,947)	2,523,414
Interfund Receivables	(878,999)	271,927
Regulatory Asset-Public Fire Protection Fees	(760,013)	(3,514,579)
Regulatory Asset-Hyada Surcharges.....	123,918	98,708
Materials and Supplies	162,680	105,337
Prepayments	(352,422)	769,853
Deferred Rental Revenues	11,650	261,800
Accrued Taxes	420,897	47,241
Salaries, Wages and Fringe Benefits Payable	52,872	(38,353)
Accrued Compensated Absences	(87,802)	63,459
Customers' Deposits	(3,771)	10,679
Accrued Expenses and Contracts Payable	14,183,160	(407,465)
Interfund Payables	551,418	(532,410)
Total Adjustments	23,459,327	14,049,292
Net Cash From Operating Activities	<u>\$52,789,677</u>	<u>\$29,135,518</u>
Reconciliation of Cash and Equity in Pooled Investments to Balance Sheet:		
Cash and Equity in Pooled Investments		
in Special Funds	\$160,850,624	\$212,540,786
Cash and Equity in Pooled Investments		
in Operating Funds	37,666,496	18,958,145
Cash and Equity in Pooled Investments		
at December 31	<u>\$198,517,120</u>	<u>\$231,498,931</u>

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

**NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2012 AND 2011**

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

Tacoma Water owns and operates the City's Water System which includes a surface water supply source (the Watershed); several extensive well fields; a water transmission system consisting of several pipelines, water treatment and quality facilities; various reservoirs, standpipes and pump stations; and an extensive distribution system. Tacoma Water supplies water to approximately 96,000 customers and had approximately 256 employees as of December 31, 2012. Tacoma Water's service area includes the City of Tacoma and urbanized areas of Pierce and South King Counties. Water service outside the City limits is provided under franchises granted by both Pierce and King Counties. Tacoma Water is organized functionally as Water Distribution Engineering and Operations, Water Quality, Water Supply, Water Resource Planning, and Water Rates and Financial Planning.

WATER DISTRIBUTION ENGINEERING - To engineer, design, construct, inspect, and oversee the construction of the distribution system and its facilities; to provide engineering and construction supervision for mains, hydrants, services, meters, pressure reducing valves and pressure zones; to provide efficient customer service and support for development.

WATER DISTRIBUTION OPERATIONS - To effectively manage, construct, inspect, operate and maintain the distribution system and its facilities including mains, hydrants, valves, services and meters in an environmentally responsible manner; to provide efficient customer service and support for development.

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; to participate in shaping water quality legislation and regulations; to be aware of changes in water system security needs and to coordinate as directed.

WATER SUPPLY - To design, construct, inspect, operate and maintain the City's water supply structures, wells, pump stations, reservoirs, standpipes, transmission mains, Tacoma Water buildings and associated property, and electrical and mechanical equipment; to maintain pressure reducing stations and pipeline rights-of-way; to administer water rights; to track water system security issues and coordinate as needed.

WATER RESOURCE PLANNING - To plan for resources to meet future needs including conservation; to prepare system, strategic, and business plans for Tacoma Water; to support wholesale customers; to provide planning support for growth; to provide hydraulic modeling, GIS, maps and records, computer, SAP, and other technology support for Tacoma Water; and to manage Tacoma Water's asset management program.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

WATER RATES AND FINANCIAL PLANNING - To develop and maintain necessary tools and reports to assess the utility's financial health, identify issues, opportunities and recommend actions to maintain solid financial rating for the water utility and the Regional Water Supply System.

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) construction of new Treatment Facilities. Participants' rights and obligations with regard to the Second Supply Project are called out in the Second Supply Project Agreement. Tacoma has a 15/36 Participant Share and each of the others have a 7/36 Participant Share. A Participant Share represents a Participant's proportional right to receive water delivered by the Second Supply Project and represents a Participant's obligation to pay project costs, including Fixed and Variable Operation & Maintenance Costs, Initial Project Construction Costs and Capital Expenditures. Tacoma, consistent with the Project Agreement, is the owner and operator of the Second Supply Project.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

In June 2011, the GASB issued Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position effective for financial statements for periods beginning after December 15, 2011. The Division implemented this new pronouncement in the current year. The effect of the implementation of this statement to the Division is limited to renaming of "Net Assets" to "Net Position".

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.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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 WA State LGIP and/or a Municipal Investor interest bearing demand deposit account maintained with U.S. Bank.

The Division's equity in that portion of the City of Tacoma Investment Pool held in qualified public depositories at December 31, 2012 and 2011 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 of the State of Washington. 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 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.

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.

MATERIAL 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, extraordinary operations, notes and contracts receivable, and customer deposits.

BOND PREMIUM, ISSUANCE COSTS AND LOSS ON REFUNDING - Bond premium, discount and issuance costs are amortized over the life of the bonds using the weighted average of the

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

bonds outstanding. Losses on refunding are amortized on a straight-line basis over the applicable bond period.

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

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

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

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

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

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

COMPENSATED ABSENCES - The City has two different policies for compensated absences. The City's original policy allows employees to accrue vacation based on the number of years worked with a maximum accrual equal to the amount earned in a two-year period. These employees also accrue one day of sick leave per month without any ceiling on the maximum accrued. The City implemented a new policy in 1998 allowing employees to earn PTO (personal time off) without distinction between vacation and sick leave. Employees who worked for the City prior to the change could choose to stay with the original policy or opt to convert to the new policy. The amount of PTO earned is based on years of service. The maximum accrual for PTO is 960 hours, and upon termination, employees are entitled to compensation for unused PTO at 100%. Vacation pay and PTO are recorded as a liability and expense in the year earned. Based on historical information, 10% of compensated absences are considered short term.

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

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

Tacoma Water receives contract resource obligation revenue and debt service payments from our partners in the Second Supply Project Agreement which are recorded as operating revenue.

NON-OPERATING REVENUES AND EXPENSES – These are items that do not qualify as operating defined above such as interest and gain (loss) on disposition of property.

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

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

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

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

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

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

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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 and additionally, must pay a gross earnings tax to the City.

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), self-insurance liabilities and other contingencies. Actual results may differ from these estimates.

SIGNIFICANT RISKS AND UNCERTAINTIES - The Division is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include, but are not limited to, water conditions, weather and natural disaster-related disruptions, collective bargaining labor disputes, fish and other endangered species act issues, Environmental Protection Agency regulations and federal government regulations.

RECLASSIFICATIONS - Changes have been made to prior year account classifications as needed to conform to the current year presentation format. Such changes did not affect net position for this year.

NOTE 3 UTILITY PLANT - A summary of the balances and changes in utility plant follows:

	Balance December 31, 2011	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2012
Intangible Plant	\$ 34,902,822	\$ 389,111	\$ (205,753)	\$ -	\$ 35,086,180
Source of Supply Plant	76,455,691	2,483,372	(62,886)	-	78,876,177
Pumping Plant	9,142,701	85,249	(5,921)	-	9,222,029
Water Treatment Plant	45,097,165	59,680	(754,901)	-	44,401,944
Transmission Facilities	222,241,072	4,790,118	(90,337)	-	226,940,853
Distribution Facilities	377,190,175	19,174,736	(3,505,899)	-	392,859,012
General Plant	28,874,232	4,859,197	(787,001)	(145,439)	32,800,989
Total Water Plant In Service	793,903,858	31,841,463	(5,412,698)	(145,439)	820,187,184
Less Accumulated Depreciation	149,177,559	15,262,686	(5,244,445)	(2,319,353)	156,876,447
	644,726,299	16,578,777	(168,253)	2,173,914	663,310,737
Construction Work In Progress	16,426,998	74,810,559	-	(31,696,024)	59,541,533
Net Utility Plant	\$ 661,153,297	\$ 91,389,336	\$ (168,253)	\$ (29,522,110)	\$ 722,852,270

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

	Balance December 31, 2010	Additions	Retirements	Transfers & Adjustments	Balance December 31, 2011
Intangible Plant	\$ 34,854,971	\$ 220,310	\$ (172,459)	\$ -	\$ 34,902,822
Source of Supply Plant	76,057,618	434,423	(36,350)	-	76,455,691
Pumping Plant	9,121,209	25,492	(4,000)	-	9,142,701
Water Treatment Plant	45,124,694	(27,529)	-	-	45,097,165
Transmission Facilities	192,646,927	30,886,349	(1,292,204)	-	222,241,072
Distribution Facilities	362,138,047	17,936,010	(2,883,882)	-	377,190,175
General Plant	27,565,793	1,479,114	(139,131)	(31,544)	28,874,232
Total Water Plant In Service	747,509,259	50,954,169	(4,528,026)	(31,544)	793,903,858
Less Accumulated Depreciation	142,247,827	14,389,681	(4,355,566)	(3,104,383)	149,177,559
	605,261,432	36,564,488	(172,460)	3,072,839	644,726,299
Construction Work In Progress	31,331,339	36,018,284	-	(50,922,625)	16,426,998
Net Utility Plant	\$ 636,592,771	\$ 72,582,772	\$ (172,460)	\$ (47,849,786)	\$ 661,153,297

Utility Plant includes non-depreciable assets of \$56,843,169 for 2012 and \$54,953,363 for 2011.

NOTE 4 SPECIAL FUNDS - Cash and equity in pooled investments included in Tacoma Water's Special Funds consist of:

Cash and Equity in Pooled Investments	2012	2011
Construction Funds	\$ 58,833,459	\$ 125,330,650
Debt Service Funds	3,318,052	3,091,834
Bond Reserve Funds	19,507,744	19,512,184
System Development Charge Fund	53,626,384	47,111,039
Other Cash and Equity in Pooled Investments	25,564,985	17,495,079
Total	\$ 160,850,624	\$ 212,540,786

NOTE 5 LONG-TERM LIABILITIES – The Division's Long-term Liabilities are primarily for the purpose of capital improvements with the exception of the Muckleshoot liability. Long-term debt activities for 2012 and 2011 were as follows:

	Balance December 31, 2011	Additions	Reductions	Balance December 31, 2012	Due Within One Year
Revenue Bonds	\$ 371,500,000	\$ -	\$ (6,620,000)	\$ 364,880,000	\$ 7,205,000
Plus: Unamortized Premium	5,289,234	-	(653,854)	4,635,380	-
Net Revenue Bonds	376,789,234	-	(7,273,854)	369,515,380	7,205,000
Public Works Trust Fund Loans	27,246,270	500,000	(2,109,965)	25,636,305	2,141,215
Drinking Water State Revolving Fund Loan	16,311,391	400,000	(376,161)	16,335,230	675,362
Total Long-Term Debt	420,346,895	900,000	(9,759,980)	411,486,915	10,021,577
Muckleshoot Liability	8,704,712	-	(168,252)	8,536,460	820,747
Total Long-Term Liabilities	\$ 429,051,607	\$ 900,000	\$ (9,928,232)	\$ 420,023,375	\$ 10,842,324

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

	Balance December 31, 2010	Additions	Reductions	Balance December 31, 2011	Due Within One Year
Revenue Bonds	\$377,780,000	\$ -	\$ (6,280,000)	\$371,500,000	\$6,620,000
Plus: Unamortized Premium	5,798,980	-	(509,746)	5,289,234	-
Net Revenue Bonds	383,578,980	-	(6,789,746)	376,789,234	6,620,000
Public Works Trust Fund Loans	29,356,235	-	(2,109,965)	27,246,270	2,109,965
Drinking Water State Revolving Fund Loan	10,680,000	5,984,023	(352,632)	16,311,391	352,632
Total Long-Term Debt	423,615,215	5,984,023	(9,252,343)	420,346,895	9,082,597
Muckleshoot Liability	8,877,171	-	(172,459)	8,704,712	168,253
Total Long-Term Liabilities	<u>\$432,492,386</u>	<u>\$ 5,984,023</u>	<u>\$ (9,424,802)</u>	<u>\$429,051,607</u>	<u>\$9,250,850</u>

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

SENIOR LIEN BONDS

	<u>2012</u>	<u>2011</u>
2002 Regional Water Supply System Revenue Bonds, with interest rates ranging from 4.13% to 5.50%, due in yearly installments ranging from \$875,000 to \$7,400,000 through 2032. Original Issue: \$82,700,000	\$75,925,000	\$76,750,000
2003 Water System Revenue and Refunding Bonds, with interest rates ranging from 4.125% to 5.25%, due in yearly installments ranging from \$1,725,000 to \$3,505,000 through 2023. Original Issue: \$51,380,000	25,285,000	28,630,000
2005 Water System Revenue and Refunding Bonds, with interest rates ranging from 4.125% to 5.0%, due in yearly installments ranging from \$1,695,000 to \$4,760,000 through 2025. Original Issue: \$46,550,000	35,485,000	37,420,000
2009 Water System Revenue Bonds, with interest rate at 5.751%, with Build America Bond (BAB) rebate at 35% of interest, 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
2010A Water System Revenue Refunding Bonds, with interest rates ranging from 2.0% to 5.0%, due in yearly installments starting in 2013 ranging from \$530,000 to \$4,655,000 through 2023. Original Issue: \$29,100,000	28,585,000	29,100,000

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

2010B Water System Revenue Bonds, with interest rates ranging from 4.581% to 5.621%, with Build America Bond (BAB) rebate at 35% of interest, due in yearly installments starting in 2024 ranging from \$2,115,000 to \$15,390,000 through 2040.

Original Issue: \$74,985,000	74,985,000	74,985,000
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2010A Regional Water Supply System Revenue Bonds, with interest rates ranging from 2.0% to 4.0%, due in yearly installments starting in 2013 ranging from \$260,000 to \$355,000 through 2024. (See Note 6)

Original Issue: \$3,595,000	3,595,000	3,595,000
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2010B Regional Water Supply System Revenue Bonds, with interest rates ranging from 5.371% to 5.621%, with Build America Bond (BAB) rebate at 35% of interest, due in yearly installments starting in 2025 ranging from \$370,000 to \$5,775,000 through 2040. (See Note 6)

Original Issue: \$44,245,000	44,245,000	44,245,000
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Subtotal Sr. Lien Debt	364,880,000	371,500,000
Unamortized premium	4,635,380	5,289,234
Less Current Portion of Revenue Bond Debt	(7,205,000)	(6,620,000)
Long-term Portion of Revenue Bond Debt	\$362,310,380	\$370,169,234

Scheduled principal maturities on the bonds, gross interest payments and BAB interest rebates are as follows:

<u>Year</u>	<u>Principal</u>	<u>Total Interest</u>	<u>BAB Interest Rebate</u>
2013	\$7,205,000	\$19,060,732	\$3,840,767
2014	\$7,550,000	\$18,731,838	\$3,840,767
2015	\$7,940,000	\$18,401,975	\$3,840,767
2016	\$8,325,000	\$18,045,325	\$3,840,767
2017	\$8,760,000	\$17,651,863	\$3,840,767
2018-2022	\$54,295,000	\$81,517,121	\$19,203,835
2023-2027	\$56,020,000	\$67,935,251	\$18,904,918
2028-2032	\$65,185,000	\$53,045,837	\$16,697,043
2033-2037	\$88,350,000	\$32,840,156	\$11,494,053
2038-2040	\$61,250,000	\$7,016,245	\$2,455,686

The fair value of Tacoma Water's long-term debt is based on quoted market prices. The fair market value of the Water System Revenue Bonds at December 31, 2012 and 2011 was \$270,585,588 and \$290,255,249 respectively. The fair market value of the Regional Water Supply System Revenue Bonds at December 31, 2012 and 2011 was \$130,661,604 and \$137,410,245 respectively.

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

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

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

JUNIOR LIEN DEBT

	<u>2012</u>	<u>2011</u>
Public Works Trust Fund Loans		
2001 Public Works Trust Fund construction loan for the Second Supply Project (SSP), with interest of .5% per annum, due in yearly installments of \$533,333 through 2021.	\$4,800,000	\$5,333,333
2001 Public Works Trust Fund pre-construction loan for the SSP Howard Hanson Dam Additional Storage Project, with interest of .5% per annum, due in yearly installments of \$52,632 through 2021.	473,684	526,316
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.	5,312,500	5,843,750
2002 Public Works Trust Fund pre-construction loan for the Middle and Headworks section of the SSP, with interest of .5% per annum, due in yearly installments of \$54,180 through 2021.	487,616	541,796
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.	640,351	693,713
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.	5,188,235	5,558,824
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.	8,733,918	8,748,538
Drinking Water State Revolving Fund Loans		
2002 construction loan for the Portland Avenue Reservoir, with interest of 2.5% per annum, due in yearly installments of \$161,053 through 2021.	1,449,474	1,610,526
2008 construction loan for the McMillin Reservoir Reconstruction, with interest of 1.5% per annum, due in yearly installments of \$215,108 through 2028.	3,441,734	3,256,842
2009 construction loan for the McMillin Reservoir Reconstruction, with interest of 1% per annum, due in yearly installments of \$299,201 from 2013 through 2032.	5,984,023	5,984,023

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

2010 construction loan for the McMillin Reservoir
Reconstruction, with interest of 1.5% per annum, due in
yearly installments of \$273,000 from 2015 through 2034.

	5,460,000	5,460,000
Subtotal Junior Lien Debt	41,971,535	43,557,661
Less current portion of debt	(2,816,577)	(2,462,597)
Long-Term portion of Junior Lien Debt	<u>\$39,154,958</u>	<u>\$41,095,064</u>

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

<u>Year</u>	<u>Principal</u>	<u>Interest</u>
2013	\$2,816,577	\$409,848
2014	\$2,816,577	\$254,934
2015	\$3,089,577	\$585,245
2016	\$3,089,577	\$290,836
2017	\$3,089,578	\$265,790
2018-2022	\$14,646,690	\$953,262
2023-2027	\$8,254,975	\$462,880
2028-2032	\$3,621,984	\$153,211
2033-2034	\$546,000	\$12,285

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 Simpson Tacoma Kraft Company (Simpson) accounted for 8.5% and 8.5% of Tacoma Water's total water sales in 2012 and 2011, respectively. There were no outstanding accounts receivables from Simpson at year-end 2012 or 2011.

Tacoma Water has contracted with Simpson to supply certain quantities of water at a specified rate through July 31, 2015.

NOTE 8 FLEET SERVICES FUND - The Department of Public Utilities has established a Fleet Services Fund to perform scheduled maintenance, repair and replacement of the Department vehicles and related equipment. Transfers of vehicles and equipment from Tacoma Water to the Fleet Services Fund are accounted for as transfers.

Tacoma Water pays the Fleet Services Fund for the use of the vehicles and equipment to cover fleet operating expenses. Payments made by Tacoma Water in 2012 and 2011 were \$2,226,924 and \$2,336,806, respectively.

Fleet Services' management makes an annual assessment of the capital replacement reserve balance for appropriate funding levels. It is the Fund's policy to maintain the Fund's maximum balance at a level that will provide adequate purchasing power for a three-year cycle and to return any excess funds to customers based on their scheduled monthly payments. The solvency of the Replacement Fund also allowed Fleet Services to return a portion of interest earned on Fund investments for the year to their customers. In 2012 and 2011, Fleet Services returned 75% of the interest earned on the capital replacement reserve to Tacoma Water's replacement fund. The amounts refunded in 2012 and 2011 were \$62,242 and \$76,000, 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 \$496,377 in 2012 and \$120,000 in 2011. Assets in the Self-Insurance Fund total \$5.4 million which exceeds accrued and incurred but not reported liabilities. Equity in the Self-Insurance Fund is transferred to the appropriate operating divisions in accordance with GASB 10. Management believes Tacoma Water's investment in the Self-Insurance Fund is more than adequate to settle all its known or estimated claims.

The City purchases a \$15 million Fiduciary Policy with a \$25,000 deductible that provides for wrongful acts arising out of the administration of the City's employee benefits programs and a \$1 million crime Liability policy for employee dishonesty and for fraudulent or dishonest acts by employees for loss of money, securities and property. The insurance policies presently in effect include coverage on the Department's buildings and fleet vehicles as well as general liability and public official's liability. The current insurance policies have deductibles or self insured retentions of \$250,000 for buildings and vehicles and \$1.5 million for general comprehensive liability. The public official's policy has a \$200,000 deductible. The general government comprehensive liability policies provide \$15 million of coverage. The City has a policy to cover extraordinary worker's compensation claims with a statutory limit (\$1 million self insured retention).

NOTE 10 TACOMA EMPLOYEES' RETIREMENT SYSTEM FUND (TERS) - Employees of the Division are covered by the Tacoma Employees' Retirement System (the System), an actuarially funded system operated by the City. The following information is provided on a city-wide basis.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

This note emphasizes the employer disclosures and detailed information presented in an independent CAFR issued by the Retirement System. Further detailed information regarding these disclosures can be found in that report which may be obtained by writing to Tacoma Employees' Retirement System, 3628 South 35th Street, Tacoma, Washington 98409.

Plan Description and Contribution Information - The System is a single employer, defined benefit retirement plan covering employees of the City of Tacoma and is administered in accordance with RCW Chapter 41.28 and Chapter 1.30 of the Tacoma Municipal Code. There are 2,107 retirees and beneficiaries currently receiving benefits, 426 vested terminated members entitled to future benefits and 2,861 active members of the System, as of December 31, 2012.

Basis of Accounting - The financial statements are prepared using the accrual basis of accounting. Employee and employer contributions are recognized as revenues in the period in which employee services are performed and expenses are recorded when the corresponding liabilities are incurred, regardless of when payment is made. Benefit payments and refunds of contributions are recognized when due and payable in accordance with the terms of the plan.

Method Used to Value Investments - Equity securities, fixed income securities, real estate and short-term investments are all reported at fair market value. Fair market value was determined by our custodian bank utilizing standard industry practices. Private equity investments are reported by the managers subject to their fair market value policies. No investment in any one corporation or organization exceeded five percent of net position available for benefits.

Investments and Contracts - The System has no securities of the employer and related parties included in the plan assets. The System has not made any loans to the employer in the form of notes, bonds, or other instruments.

Benefits – There are two formulas that are used for calculating retirement benefits. The benefit will be determined 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 determined based on the member's age and years of service. Several options are available for the retiree to provide for the beneficiaries. The System also provides death and disability retirement.

Contributions - Covered employees are required by Chapter 1.30 of the Tacoma City Code to contribute a percentage of their gross wages to the System, and the employer contributes an additional percentage. The contribution rates are provided in the following table:

Applicable Period	Employer Rate	Member Rate	Total Rate
1/1/2001 to 02/01/2009	7.56%	6.44%	14.00%
2/2/2009 to 12/31/2009	8.64	7.36	16.00
1/1/2010 to 12/31/2010	9.72	8.28	18.00
1/1/2011 to 12/31/2011	10.26	8.74	19.00
1/1/2012 onward	10.80	9.20	20.00

Contributions city-wide totaled \$43.1 million in 2012 (\$22.7 million employer contributions and \$20.4 million employee contributions) and totaled \$42.4 million in 2011 (\$22.5 million employer contributions and \$19.9 million employee contributions). Contributions made by the Division were \$2.0 million and \$1.9 million in 2012 and 2011 respectively.

Funding Status and Progress - Historical trend information about TERS is presented herewith as supplementary information. This information is based on the most recent actuarial valuation performed, dated January 1, 2012, and is intended to help assess TERS funding status on a going-concern basis, assess progress made in accumulating assets to pay benefits when due, and make comparisons with other public employee retirement systems.

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

Schedule of Funding Progress (\$ in millions):

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (c) = (b)-(a)	Funded Ratio (d) = (a) / (b)	Covered Payroll (e)	UAAL as of Percentage of Covered Payroll (f) = (c) / (e)
1/1/2009	\$ 1,097.3	\$ 1,002.3	\$ (95.0)	109.5%	\$ 197.4	(48.1%)
1/1/2011	\$ 1,074.8	\$ 1,132.9	\$ 58.1	94.9%	\$ 219.6	26.5%
1/1/2012	\$ 1,068.3	\$ 1,185.5	\$ 117.2	90.1%	\$ 219.4	53.4%

Actuarial Methods and Significant Actuarial Assumptions:

Valuation Date	January 1, 2012
Actuarial Cost Method	Entry Age
Amortization Method	Level Percentage of the System's Projected Payroll
Remaining Amortization Period	30 years, Open, unless fixed rate amortizes less than 30 years
Asset Valuation Method	Assets are valued at market value, with a four year smoothing of all market value gains and losses.
Actuarial Assumptions:	
Investment Rate of Return	7.75%
Projected Salary Increases	4.25%
Includes Inflation at	3.25%
Postretirement Benefit Increases	2.125%

Annual Pension Cost and Net Pension Obligation - The City's annual pension cost and net pension obligation to the Retirement System for 2012 were as follows:

	(\$ in millions)
Annual Required Contribution (ARC)	\$ 22.7
Interest on Net Pension Obligation (NPO)	(1.1)
Adjustment to ARC	1.3
Annual Pension Cost (APC)	22.9
Employer Contributions made	22.7
Change in NPO	0.2
NPO at Beginning of Year	(13.7)
NPO at End of Year	\$ (13.5)

Trend Information (\$ in millions)			
Year Ending December 31,	Annual Pension Cost (APC)	% of APC Contributed	Net Pension Obligation
2010	\$ 17.0	125%	\$ (8.1)
2011	\$ 16.9	133%	\$ (13.7)
2012	\$ 22.9	99%	\$ (13.5)

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. Generally accepted accounting principles require 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 (4.00%).

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 would be required to report as an expense for the year. The ARC is equal to the Normal Cost plus an amount to amortize the Unfunded Actuarial Accrued Liability (UAAL) on a closed basis of 30 years, beginning January 1, 2007. The remaining amortization period for 2012 is 25 years.

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

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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

	January 1, 2009	January 1, 2011
Total membership:		
Active employees	3,633	3,675
Terminated vested employees	355	363
Retired employees & Dependents	815	790
Total	<u>4,803</u>	<u>4,828</u>
Annual Benefit Payments	\$ 8,319,788	\$ 9,569,648
Discount rate	4.00%	4.00%
Present Value of Benefits (PVB)	\$ 266,167,781	\$ 319,550,419
Actuarial Accrued Liability (AAL)	\$ 205,168,072	\$ 248,571,791
Assets	\$ -	\$ -
Unfunded Actuarial Accrued Liability (UAAL)	<u>\$ 205,168,072</u>	<u>\$ 248,571,791</u>
Normal Cost	\$ 5,615,626	\$ 5,559,350
Annual Required Contribution (ARC)	\$ 16,761,978	\$ 19,734,040

The following table shows the total value of the benefits provided, the member paid premiums and the City paid benefits as of December 31, 2012.

Value of Subsidy at 4.00% Interest Rate	Total Value of Benefits	Member Paid Premiums	City Paid Benefits
Present Value of Benefits (PVB)	\$ 445,647,729	\$ 126,097,310	\$ 319,550,419
Actuarial Accrued Liability (AAL)	\$ 305,186,964	\$ 56,615,173	\$ 248,571,791
Normal Cost	\$ 10,741,744	\$ 5,182,394	\$ 5,559,350
Annual Benefit Payments	\$ 12,218,978	\$ 2,649,330	\$ 9,569,648

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, 2012.

	City	Water
Determination of Annual Required Contribution:		
Normal Cost at Year-end	\$ 5,559,351	\$ 393,824
Amortization of UALL	14,174,690	144,425
Annual Required Contribution (ARC)	<u>\$ 19,734,041</u>	<u>\$ 538,249</u>
Determination of NET OPEB Obligation:		
Annual Required Contribution (ARC)	\$ 19,734,041	\$ 538,249
Interest on prior year Net OPEB Obligation	1,455,746	66,144
Adjustments to ARC	(1,720,609)	(64,256)
Annual OPEB Cost	19,469,178	540,137
Actual benefits paid	9,393,431	138,439
Increase in Net OPEB Obligation	10,075,747	401,698
Net OPEB Obligation - beginning of year	36,393,621	1,653,611
Net OPEB Obligation - end of year	<u>\$ 46,469,368</u>	<u>\$ 2,055,309</u>

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

Funding Status and Funding Progress - The following table shows the annual OPEB cost and net OPEB obligation for three years. This table is based upon a 4.00% interest rate.

	Annual OPEB Cost		Benefits Paid		Net OPEB Obligation	
Year Ended	City	Water	City	Water	City	Water
12/31/2010	\$ 16,700,184	\$ 467,968	\$ 9,206,060	\$ 120,660	\$ 26,366,848	\$ 1,225,900
12/31/2011	\$ 19,596,420	\$ 541,536	\$ 9,569,648	\$ 113,825	\$ 36,393,620	\$ 1,653,611
12/31/2012	\$ 19,469,178	\$ 540,137	\$ 9,393,431	\$ 138,439	\$ 46,469,368	\$ 2,055,309

As of January 1, 2011, the most recent actuarial valuation date, the Plan was zero percent funded. Based upon a 4% interest rate, the actuarial accrued liability for benefits was \$248.6 million, and the actuarial value of assets was zero, resulting in an Unfunded Actuarial Accrued Liability of \$248.6 million.

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 25 years.

Actuarial Methods and Significant Actuarial Assumptions:

Valuation Date	January 1, 2011
Census Date	January 1, 2011
Actuarial Cost Method:	Entry Age
Amortization Method:	Combination of level percentage and level dollar amount, see note above.
Remaining Amortization Period:	25 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	4.00% for pay-as-you-go funding
Medical Cost Trend	2011 8.1%
	2012 7.3%
	2013 6.6%
	2014-2019 6.5%
	2020-2027 6.4%
	Grading down to an ultimate of 5.2% in 2082 and beyond.
Projected Payroll Increases	4.25% per year

TACOMA WATER NOTES TO FINANCIAL STATEMENTS (continued)

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
- 20 years of service

NOTE 12 COMMITMENTS AND CONTINGENCIES

Capital Improvements – The financial requirement for Tacoma Water's 2011-2012 biennial Capital Improvement program is approximately \$64.0 million and Tacoma Water has substantial contractual commitments relating to the program. At December 31, 2012, the remaining financial requirement for Capital Improvement Programs relating to all prior biennia is approximately \$15.0 million.

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

General Legal Matters - The Utility is involved in various litigation in the normal course of business. In the opinion of management, the ultimate outcome of these claims will not have a material effect on the Utility's financial position beyond amounts already accrued as of December 31, 2012.

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STATISTICAL DATA (Unaudited)

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

TEN-YEAR FINANCIAL REVIEW

BALANCE SHEET	2012	2011	2010	2009
ASSETS				
Utility Plant - Net	\$722,852,270	\$661,153,297	\$636,592,771	\$604,657,775
Special Funds & Non-Util Prop	161,863,075	214,619,106	240,132,895	133,949,294
Current Assets	56,407,560	31,403,521	30,200,303	35,753,843
Other Assets	10,086,140	7,919,368	4,654,608	3,654,494
Total Assets	951,209,045	915,095,292	911,580,577	778,015,406
 NET ASSETS	452,879,759	429,188,088	417,695,083	412,592,671
LIABILITIES AND EQUITY				
Long-Term Debt	409,181,051	417,744,202	421,228,553	292,165,406
Current Liabilities	35,084,590	18,174,697	20,548,451	15,167,938
Long-Term Liabilities	54,063,645	49,988,305	52,108,490	58,089,391
Total Liabilities	498,329,286	485,907,204	493,885,494	365,422,735
TOTAL NET ASSETS AND LIABILITIES ...	\$951,209,045	\$915,095,292	\$911,580,577	\$778,015,406
 STATEMENT OF INCOME				
OPERATING REVENUES				
Residential and Domestic	\$38,685,705	\$36,682,278	\$35,453,730	\$36,643,366
Commercial and Industrial	10,620,950	10,101,108	10,049,782	9,659,078
Special Rate-Simpson/Other	5,031,760	4,774,237	3,798,922	4,153,327
Municipal	383,385	400,322	364,357	380,267
Other Public Bldgs and Grounds ...	1,909,782	1,815,865	1,702,656	1,861,111
Unbilled	416,986	478,594	(648,438)	187,966
Sales to Other Water Utilities ...	2,090,430	1,625,163	1,530,116	1,776,686
Total Water Sales	59,138,998	55,877,567	52,251,125	54,661,801
Other Operating Revenues	21,541,733	9,526,467	10,735,630	9,331,955
Total Operating Revenues	80,680,731	65,404,034	62,986,755	63,993,756
 OPERATING EXPENSES				
Operation and Maintenance	32,602,452	32,821,611	34,453,742	34,055,463
Taxes	3,485,243	3,106,516	3,142,772	3,093,311
Depreciation	15,262,686	14,389,681	14,474,964	13,845,799
Total Operating Expenses	51,350,381	50,317,808	52,071,478	50,994,573
NET OPERATING INCOME (LOSS)	29,330,350	15,086,226	10,915,277	12,999,183
NON-OPERATING REVENUES (EXPENSES)				
Other Income	288,183	(12,371)	33,795	497,331
Interest Income	2,320,753	3,141,374	2,370,993	1,955,385
Gain from Disposition of Property	-	-	-	26,100
Interest Charges (Net)	(14,696,096)	(15,018,374)	(15,175,660)	(9,076,156)
Net Income (Loss) Before				
Contributions & Transfers	17,243,190	3,196,855	(1,855,595)	6,401,843
Total Capital Contributions	7,834,345	9,250,677	9,713,596	7,120,993
Grants & Federal BAB Subsidies	3,840,767	4,006,209	2,355,132	244,683
Transfers Out	(5,226,630)	(4,960,736)	(5,110,721)	(5,185,152)
NET INCOME (LOSS)	\$23,691,672	\$11,493,005	\$5,102,412	\$8,582,367

Certain reclassifications made in the current year have not been restated for the prior years.

2008	2007	2006	2005 (As Restated)	2004	2003 (As Restated)
\$590,593,258	\$568,493,015	\$542,837,619	\$515,240,672	\$449,792,203	\$391,992,687
80,858,401	99,062,414	111,884,788	124,884,569	86,235,235	128,107,319
22,151,467	23,150,235	20,256,759	15,880,090	21,804,006	19,223,128
3,319,156	2,123,339	2,622,731	2,938,485	2,954,978	3,380,733
696,922,282	692,829,003	677,601,897	658,943,816	560,786,422	542,703,867
404,010,304	391,763,317	374,885,816	345,583,601	327,326,910	305,678,001
218,869,015	227,315,790	231,066,402	224,760,581	199,174,091	203,913,661
16,288,305	15,169,687	21,418,548	12,820,700	14,542,631	12,150,879
57,754,658	58,580,209	50,231,131	75,778,934	19,742,790	20,961,326
292,911,978	301,065,686	302,716,081	313,360,215	233,459,512	237,025,866
\$696,922,282	\$692,829,003	\$677,601,897	\$658,943,816	\$560,786,422	\$542,703,867
\$34,592,712	\$32,645,594	\$31,216,429	\$27,611,024	\$26,589,163	\$24,497,359
8,978,703	8,298,263	7,751,215	7,174,647	6,619,432	5,809,774
4,371,527	3,917,760	3,222,324	3,511,199	3,293,335	3,044,266
349,722	396,131	363,455	316,562	308,884	218,852
1,680,603	1,644,166	1,596,360	1,409,107	1,523,562	1,353,062
417,145	37,113	1,067,323	-	(903,969)	680,497
1,251,815	1,433,705	1,640,803	1,599,919	1,622,206	1,531,004
51,642,227	48,372,732	46,857,909	41,622,458	39,052,613	37,134,814
5,382,313	4,353,478	1,919,802	1,428,135	792,302	871,547
57,024,540	52,726,210	48,777,711	43,050,593	39,844,915	38,006,361
33,387,663	31,076,515	29,165,168	26,448,761	25,590,407	23,675,319
2,881,877	2,924,930	3,407,187	2,995,424	2,480,667	2,276,909
13,016,544	11,363,970	11,556,821	9,386,363	8,934,860	7,469,798
49,286,084	45,365,415	44,129,176	38,830,548	37,005,934	33,422,026
7,738,456	7,360,795	4,648,535	4,220,045	2,838,981	4,584,335
61,265	306,680	2,293,477	2,841,371	1,190,100	1,108,555
3,730,407	5,255,881	4,603,137	1,695,578	1,484,779	1,586,825
-	4,199,382	-	4,622,927	4,500	2,872,246
(8,406,264)	(8,484,405)	(8,403,448)	(7,185,197)	(6,253,392)	(3,655,291)
3,123,864	8,638,333	3,141,701	6,194,724	(735,032)	6,496,670
14,137,605	12,801,825	30,462,788	24,453,875	25,597,104	28,892,401
-	-	-	-	803,224	344,857
(5,014,482)	(4,562,657)	(4,302,274)	(3,951,776)	(4,016,387)	(3,407,309)
\$12,246,987	\$16,877,501	\$29,302,215	\$26,696,823	\$21,648,909	\$32,326,619

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

TEN-YEAR FINANCIAL REVIEW

BALANCE SHEET	2012	2011	2010
ASSETS			
Utility Plant - Net	\$223,896,711	\$203,938,358	\$207,242,527
Current Assets	41,256,611	55,640,447	59,811,400
Other Assets	<u>1,067,595</u>	<u>1,134,270</u>	<u>1,194,533</u>
Total Assets	266,220,917	260,713,075	268,248,460
 NET ASSETS	 137,267,801	 133,964,359	 138,246,799
LIABILITIES AND EQUITY			
Long-Term Debt	122,882,652	124,045,739	124,890,764
Current Liabilities	5,253,742	1,931,325	5,110,897
Long-Term Liab.	<u>816,722</u>	<u>771,652</u>	<u>-</u>
Total Liabilities	<u>128,953,116</u>	<u>126,748,716</u>	<u>130,001,661</u>
TOTAL NET ASSETS AND LIABILITIES ...	\$266,220,917	\$260,713,075	\$268,248,460
 STATEMENT OF INCOME			
OPERATING REVENUES			
CRO - Debt Service	\$6,272,476	\$6,239,797	\$5,119,047
CRO - O&M	2,478,238	1,778,186	2,732,956
CRO - Capital	<u>5,665,557</u>	<u>274,081</u>	<u>1,301,346</u>
Total Operating Revenues	14,416,271	8,292,064	9,153,349
 OPERATING EXPENSES			
Operation and Maintenance	2,510,085	2,485,977	2,458,379
Depreciation	<u>4,495,971</u>	<u>4,482,820</u>	<u>4,426,113</u>
Total Operating Expenses	7,006,056	6,968,797	6,884,492
NET OPERATING INCOME (LOSS)	7,410,215	1,323,267	2,268,857
NON-OPERATING REVENUES (EXPENSES)			
Other Income	-	-	-
Interest Income	407,622	396,391	861,775
Interest Charges (Net)	<u>(4,968,459)</u>	<u>(6,440,678)</u>	<u>(4,833,300)</u>
Net Income (Loss) Before Contributions & Transfers	2,849,378	(4,721,020)	(1,702,668)
Total Capital Contributions	(414,376)	(508,791)	(4,593,787)
Grants & Federal BAB Subsidies	868,328	868,328	306,327
Transfers	<u>112</u>	<u>79,043</u>	<u>1,435,898</u>
NET INCOME (LOSS)	<u>\$3,303,442</u>	<u>(\$4,282,440)</u>	<u>(\$4,554,230)</u>

Separate unaudited financial reporting for RWSS began with continuing disclosure requirements in 2004.

2009	2008	2007	2006	2005	2004
\$206,708,069	\$231,099,649	\$234,373,114	\$213,434,158	\$203,311,344	\$152,678,547
15,845,604	9,519,659	8,924,226	6,721,684	11,318,970	30,425,291
807,387	856,484	906,294	956,724	1,161,513	1,058,917
223,361,060	241,475,792	244,203,634	221,112,566	215,791,827	184,162,755
142,801,029	151,581,061	149,348,807	136,863,991	133,125,039	97,906,139
77,694,584	88,122,323	92,649,652	80,471,326	81,480,440	82,239,626
2,865,447	1,772,408	2,205,175	3,588,936	1,032,453	4,010,341
-	-	-	188,313	153,895	6,649
80,560,031	89,894,731	94,854,827	84,248,575	82,666,788	86,256,616
\$223,361,060	\$241,475,792	\$244,203,634	\$221,112,566	\$215,791,827	\$184,162,755
\$4,293,912	\$2,016,804	\$1,999,664	\$2,095,323	\$1,774,443	\$2,312,368
2,517,129	6,074,980	4,646,715	4,162,516	2,415,213	-
(339,930)	-	-	-	-	-
6,471,111	8,091,784	6,646,379	6,257,839	4,189,656	2,312,368
2,629,850	2,300,026	2,377,499	2,130,748	314,507	-
4,792,037	4,803,549	3,513,441	3,413,341	768,841	765,663
7,421,887	7,103,575	5,890,940	5,544,089	1,083,348	765,663
(950,776)	988,209	755,439	713,750	3,106,308	1,546,705
-	14,360	43,532	56,160	-	-
184,332	293,709	355,782	282,278	185,041	145,994
(3,918,240)	(3,411,937)	(4,083,294)	(4,354,244)	(3,775,570)	(2,948,229)
(4,684,684)	(2,115,659)	(2,928,541)	(3,302,056)	(484,221)	(1,255,530)
8,085,876	1,287,306	10,186,209	7,041,008	35,703,146	10,525,051
-	-	-	-	-	99,751
(12,181,224)	3,060,607	5,227,148	-	(25)	1,153,815
(\$8,780,032)	\$2,232,254	\$12,484,816	\$3,738,952	\$35,218,900	\$10,523,087

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

BOND DEBT SERVICE REQUIREMENTS
DECEMBER 31, 2012

<u>YEAR</u>	<u>PRINCIPAL</u>	<u>INTEREST</u>	<u>TOTAL</u>
2013	7,205,000	19,060,732	26,265,732
2014	7,550,000	18,731,838	26,281,838
2015	7,940,000	18,401,975	26,341,975
2016	8,325,000	18,045,325	26,370,325
2017	8,760,000	17,651,863	26,411,863
2018	9,215,000	17,224,863	26,439,863
2019	10,515,000	16,818,982	27,333,982
2020	10,990,000	16,350,300	27,340,300
2021	11,530,000	15,817,407	27,347,407
2022	12,045,000	15,305,569	27,350,569
2023	12,670,000	14,706,619	27,376,619
2024	10,140,000	14,076,569	24,216,569
2025	10,610,000	13,583,028	24,193,028
2026	11,065,000	13,058,923	24,123,923
2027	11,535,000	12,510,112	24,045,112
2028	12,025,000	11,913,012	23,938,012
2029	12,570,000	11,290,708	23,860,708
2030	13,105,000	10,640,430	23,745,430
2031	13,690,000	9,962,624	23,652,624
2032	13,795,000	9,239,063	23,034,063
2033	16,410,000	8,508,824	24,918,824
2034	17,015,000	7,573,677	24,588,677
2035	17,650,000	6,604,050	24,254,050
2036	18,300,000	5,598,235	23,898,235
2037	18,975,000	4,555,370	23,530,370
2038	19,680,000	3,474,037	23,154,037
2039	20,405,000	2,352,523	22,757,523
2040	21,165,000	1,189,685	22,354,685
	<u>\$364,880,000</u>	<u>\$334,246,343</u>	<u>\$699,126,343</u>

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

FUNDS AVAILABLE FOR DEBT SERVICE

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>
Total Income	\$88,715,624	\$76,867,233	\$73,374,289	\$66,821,912	\$61,944,933
Less: Operating Exp .	<u>36,087,695</u>	<u>35,928,127</u>	<u>37,596,514</u>	<u>37,148,774</u>	<u>36,269,540</u>
Income Available for Debt Service	<u>\$52,627,929</u>	<u>\$40,939,106</u>	<u>\$35,777,775</u>	<u>\$29,673,138</u>	<u>\$25,675,393</u>
Bond Redemption	6,668,750	6,308,333	6,092,083	5,896,250	6,046,250
Bond Interest	<u>19,342,423</u>	<u>19,624,326</u>	<u>15,700,645</u>	<u>9,941,993</u>	<u>9,465,014</u>
Debt Service Payable	<u>\$26,011,174</u>	<u>\$25,932,659</u>	<u>\$21,792,728</u>	<u>\$15,838,243</u>	<u>\$15,511,264</u>
Times Debt Service Covered.....	2.02	1.58	1.64	1.87	1.66

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

WATER PLANT IN SERVICE - YEAR 2012

PLANT ACCOUNTS

	Book Cost 1/1/12	Additions 2012
INTANGIBLE PLANT	\$ 34,902,822	\$ 389,111
SOURCE OF SUPPLY	76,455,691	2,483,372
PUMPING PLANT	9,142,701	85,249
WATER TREATMENT PLANT	45,097,165	59,680
TRANSMISSION PLANT	222,241,072	4,790,118
DISTRIBUTION PLANT	377,190,175	19,174,736
GENERAL PLANT	28,874,232	4,859,197
TOTAL WATER PLANT IN SERVICE	793,903,858	31,841,463
CONSTRUCTION WORK IN PROGRESS	16,426,998	74,810,559
TOTAL	<u>\$ 810,330,856</u>	<u>\$ 106,652,022</u>

DEPRECIATION ACCOUNTS

	Depreciation Rate %	Accumulated Depreciation 1/1/12	Annual Accrual Cr.
INTANGIBLE PLANT	-	\$ 37,500	\$ -
SOURCE OF SUPPLY PLANT	2.957	16,281,893	1,821,895
PUMPING PLANT	2.513	2,962,906	232,101
WATER TREATMENT PLANT	3.620	10,352,658	1,573,225
TRANSMISSION PLANT	1.668	36,239,375	3,640,284
DISTRIBUTION PLANT	1.876	64,762,779	7,071,366
GENERAL PLANT	7.915	18,540,448	923,815
TOTAL PLANT DEPRECIATION		<u>\$ 149,177,559</u>	<u>\$ 15,262,686</u>

1. Total Water Plant in Service includes non-depreciable land and land rights of \$56,843,169.
2. Total Book Cost of Plant Retired \$ (5,412,698)
Add: Cost of Land Sold: -
Intangible Plant: 168,253
Total Retirements \$ (5,244,445)

Retirements 2012	Transfers & Adjustments	Book Cost 12/31/12
\$ (205,753)	\$ -	\$ 35,086,180
(62,886)	-	78,876,177
(5,921)	-	9,222,029
(754,901)	-	44,401,944
(90,337)	-	226,940,853
(3,505,899)	-	392,859,012
(787,001)	(145,439)	32,800,989
(5,412,698)	(145,439)	820,187,184
-	(31,696,024)	59,541,533
<u>\$ (5,412,698)</u>	<u>\$ (31,841,463)</u>	<u>\$ 879,728,717</u>

Book Cost of Plant Retired	Cost of Removal	Salvage, Transfers and Adjustments	Accumulated Depreciation 12/31/12
\$ (37,500)	\$ -	\$ -	\$ -
(62,886)	(7,543)	-	18,033,359
(5,921)	(3,962)	-	3,185,124
(754,901)	(12,981)	-	11,158,001
(90,337)	(197,084)	-	39,592,238
(3,505,899)	(2,032,455)	-	66,295,791
(787,001)	(65,328)	-	18,611,934
<u>\$ (5,244,445)</u>	<u>\$ (2,319,353)</u>	<u>\$ -</u>	<u>\$ 156,876,447</u>

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

SUMMARY OF WATER BILLED
DECEMBER 31, 2012

	MILLION GALLONS, TOTAL		MILLION GALLONS, AVG DAILY	
	YEAR 2012	YEAR 2011	YEAR 2012	YEAR 2011
WATER BILLED				
Residential and Domestic	7,785.64	7,715.15	21.33	21.14
Commercial and Industrial	2,499.33	2,497.80	6.85	6.84
Special Rate--Simpson ...	5,860.99	5,851.70	16.06	16.03
Municipal	70.63	78.76	0.19	0.22
Other Public Bldgs and Grounds	457.27	490.54	1.25	1.34
Sales to Other Utilities	632.32	625.83	1.73	1.71
	<u>17,306.18</u>	<u>17,259.78</u>	<u>47.41</u>	<u>47.28</u>

NOTE: For conversion purposes, there are approximately 748 gallons in every
100 cubic feet of water.

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

SUMMARY OF WATER SALES - 2012

WATER SALES	AVERAGE MONTHS BILLED	C. CU. FT.	AMOUNT
RESIDENTIAL AND DOMESTIC SERVICE			
Single and Multiple Houses - Inside City	53,772	4,490,938	\$17,100,720
Multiple Unit Dwellings - Inside City	3,188	1,580,328	4,159,149
Sprinkling Services (Inside and Outside)	395	192,902	636,917
Fire Services (Inside and Outside)	146	491	71,444
Single and Multiple Houses - Outside City	30,806	3,188,216	13,439,771
Multiple Unit Dwellings - Outside City	1,783	955,734	3,277,704
Total Residential and Domestic Service	90,090	10,408,609	38,685,705
COMMERCIAL AND INDUSTRIAL SERVICE			
High Use Commercial (Inside and Outside)	8	820,998	1,290,964
Single and Multiple Buildings - Inside City	3,478	1,995,140	5,457,379
Sprinkling Services (Inside and Outside)	262	200,147	671,736
Fire Services (Inside and Outside)	1,075	6,948	2,029,035
Single and Multiple Buildings - Outside City ...	789	318,131	1,171,836
Total Commercial and Industrial Service	5,612	3,341,364	10,620,950
SERVICES WITH SPECIAL RATE			
Simpson Tacoma Kraft Company	1	7,835,544	5,031,760
MUNICIPAL WATER SERVICES			
Fountains, Buildings and Grounds	172	94,392	342,138
Fire Services	34	40	41,247
Total Municipal Water Service	206	94,432	383,385
OTHER PUBLIC BUILDINGS AND GROUNDS			
Single and Multiple Buildings - Inside	160	323,282	852,430
Single and Multiple Buildings - Outside	52	87,062	270,794
Fire Services	77	200,863	570,032
Sprinkling Services	117	125	216,526
Total Other Public Buildings and Grounds	406	611,332	1,909,782
SALES TO OTHER UTILITIES - Total	18	910,332	2,090,430
Unbilled Revenue			416,986
TOTAL WATER SALES	96,333	23,201,613	\$59,138,998

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

STATISTICS
AS OF DECEMBER 31, 2012

Tacoma Water System:

2012 average daily delivery exclusive of pulp mill	34.2	MG
Average daily delivery pulp mill	16.0	MG
Total average daily delivery	50.3	MG
2012 maximum daily production August 16, 2012	80.4	MG
2012 minimum daily production . . . February 8 2012	26.4	MG
Total water produced in 2012*.	18,393	MG

Regional Water Supply System (RWSS):

Total average daily delivery	9.3	MG
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Average daily consumption per single family

residential service	171	GPD
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Miles of transmission and wells supply mains -

28" to 96" diameter (includes North Fork wells system).	142	
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Miles of distribution mains - 2" to 24" in diameter.

Fire hydrants.	10,225	
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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 MGD water right. Tacoma is also a partner in a Regional Water Supply System (RWSS) and holds a 27 MGD annual average share of that 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 has an excellent record for unsurpassed quality, meeting all the standards of the U.S. Environmental Protection Agency and the Washington State Department of Health.

Storage facilities are provided at 15 locations. These facilities consist of 10 concrete basins or reservoirs and 12 steel standpipes. The combined storage capacity is equal to approximately 181 million gallons. Of this storage capacity 108 million gallons are located at McMillin Reservoir approximately 14 miles southeast of Tacoma.

* Includes losses and water for self-consumption.

MG equals million gallons.

GPD equals gallons per day.

CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

TAXES AND EMPLOYEE WELFARE CONTRIBUTIONS
FOR THE YEAR 2012

FEDERAL

Social Security (FICA)		\$1,444,114
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STATE OF WASHINGTON

Retail Sales	\$298,592	
Utilities and Business Activities Tax	<u>2,991,555</u>	
Total		3,290,147

COUNTY

Real Property	<u>27,866</u>	
Total		27,866

MUNICIPALITIES

City of Tacoma Gross Earnings Tax	5,081,191	
City of Lakewood Administrative Fee	6,620	
City of Puyallup Administrative Fee	13,255	
City of University Place Administrative Fee	451,139	
City of Fircrest Administrative Fee	<u>6,330</u>	
		<u>5,558,535</u>

TOTAL TAXES		<u><u>\$10,320,662</u></u>
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Taxes as a % of Total Revenues of \$83,001,484		12.43%
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EMPLOYEE WELFARE CONTRIBUTIONS

Industrial Insurance and Medical Aid	\$166,534	
Pensions	1,954,051	
Medical Insurance	3,599,426	
Dental Insurance	<u>402,280</u>	

TOTAL EMPLOYEE WELFARE CONTRIBUTIONS		<u><u>\$6,122,291</u></u>
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CITY OF TACOMA, WASHINGTON
DEPARTMENT OF PUBLIC UTILITIES
TACOMA WATER

2012 WATER RATES

			READY TO SERVE CHARGE PER MONTH	
			INSIDE TACOMA	OUTSIDE TACOMA
METER SIZE				
5/8	inch	.....	\$16.76	\$20.11
3/4	inch	.....	\$25.15	\$30.17
1	inch	.....	\$41.91	\$50.29
1-1/2	inch	.....	\$83.80	\$100.56
2	inch	.....	\$134.08	\$160.90
3	inch	.....	\$251.40	\$301.68
4	inch	.....	\$419.00	\$502.80
6	inch	.....	\$838.00	\$1,005.60
8	inch	.....	\$1,340.80	\$1,608.96
10	inch	.....	\$1,927.40	\$2,312.88
12	inch	.....	\$2,828.25	\$3,393.90

			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			\$1.368	\$1.642
First 500 cubic ft. of water consumption per month during the summer months of June through September			\$1.368	\$1.642
Each 100 cubic ft. of water consumption over 500 cubic ft. during the summer months of June through September			\$1.710	\$2.053
<u>Commercial and Industrial</u>				
General Service			\$1.497	\$1.797
Large Volume Service (over 65,000 cubic feet annually)			\$1.381	\$1.658
<u>Parks and Irrigation Service</u>				
Each 100 cubic feet of water consumption			\$1.990	\$2.388

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. 27970 and were effective January 1, 2012.

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

2012 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	\$21.29	2.99
3	inch	\$31.00	2.99
4	inch	\$51.79	2.99
6	inch	\$116.17	2.99
8	inch	\$206.81	2.99
10	inch	\$323.48	2.99
12	inch	\$517.40	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).

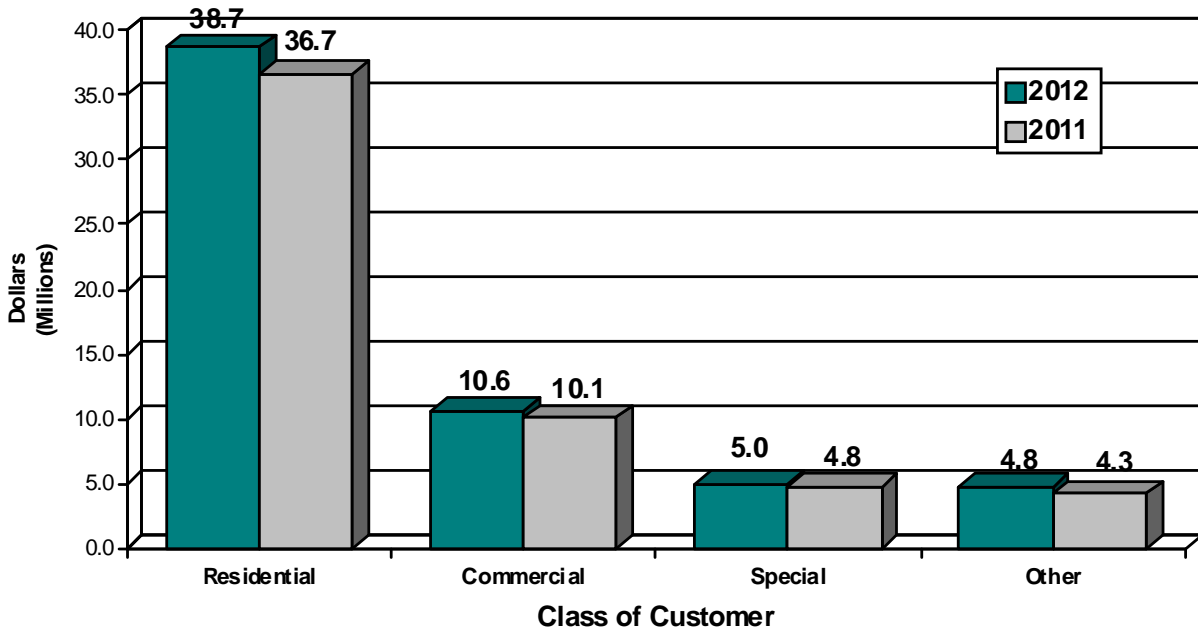
CONSUMPTION

Rates per 100 cubic feet per month \$3.726

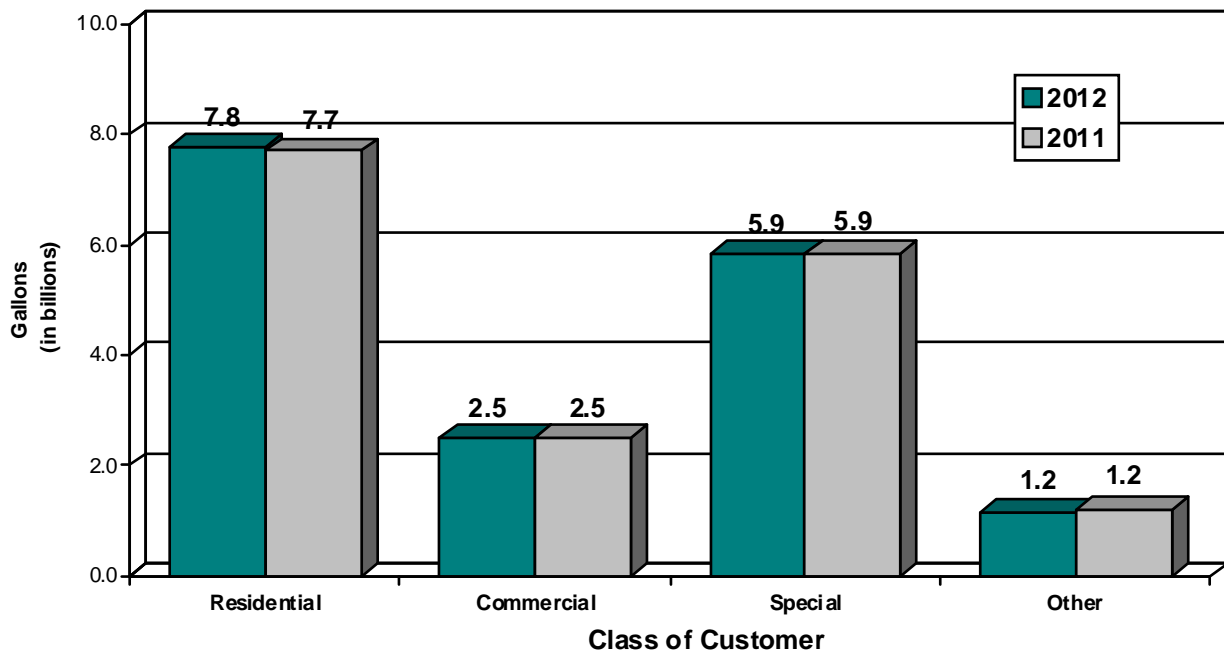
The above rates for fire service shall apply where City water is used for all purposes on such premises exclusive of that amount allowed for testing and leakage.

The Fire Protection Rates were established by Ordinance No. 27970 and were effective January 1, 2012.

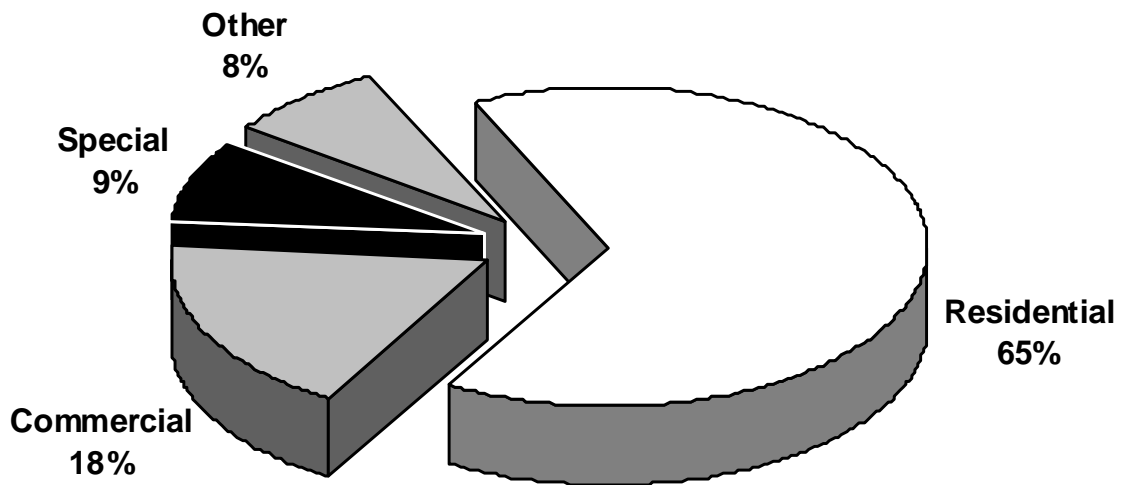
WATER SALES
Year to Date - December 2012 & 2011



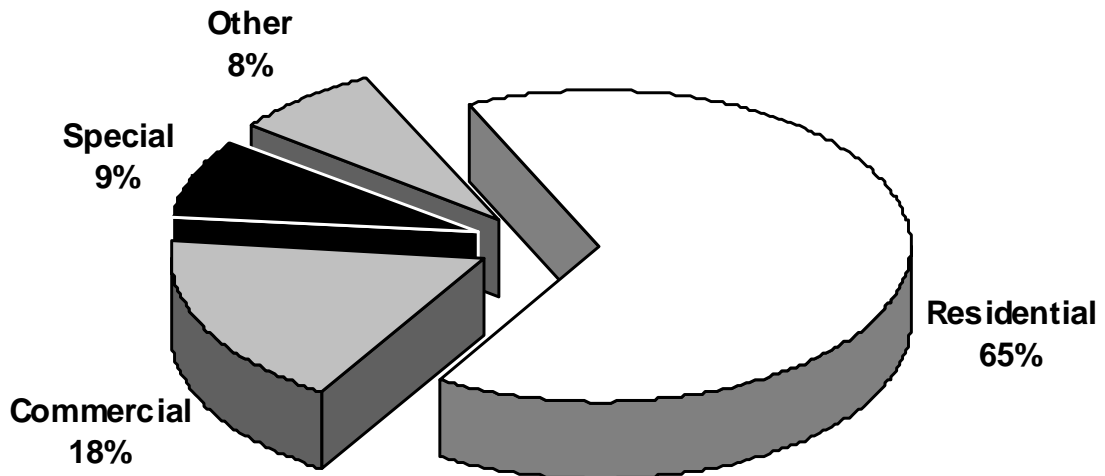
WATER CONSUMPTION
Year to Date - December 2012 & 2011



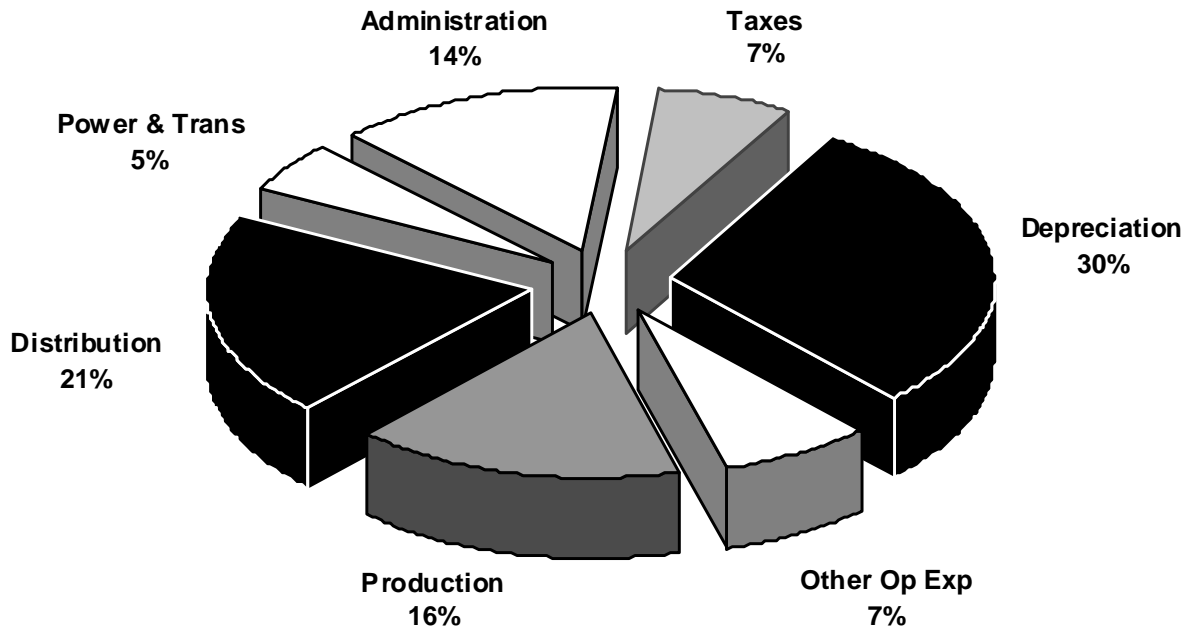
WATER SALES
Year to Date - December 2012
(\$59,138,998)



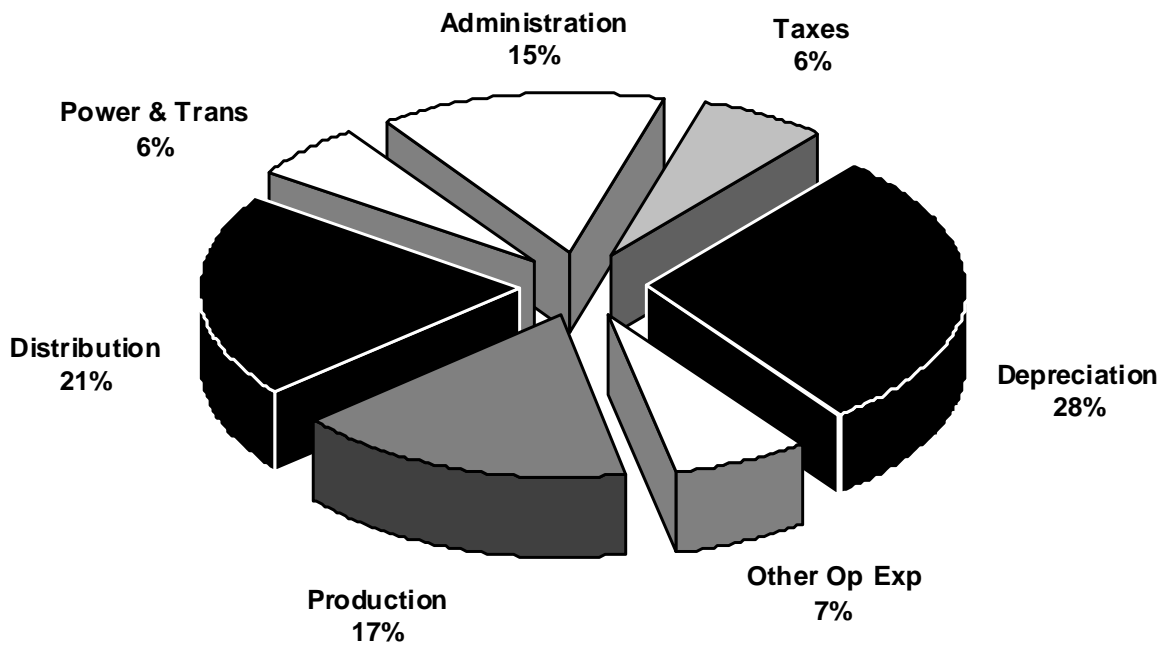
WATER SALES
Year to Date - December 2011
(\$55,877,567)



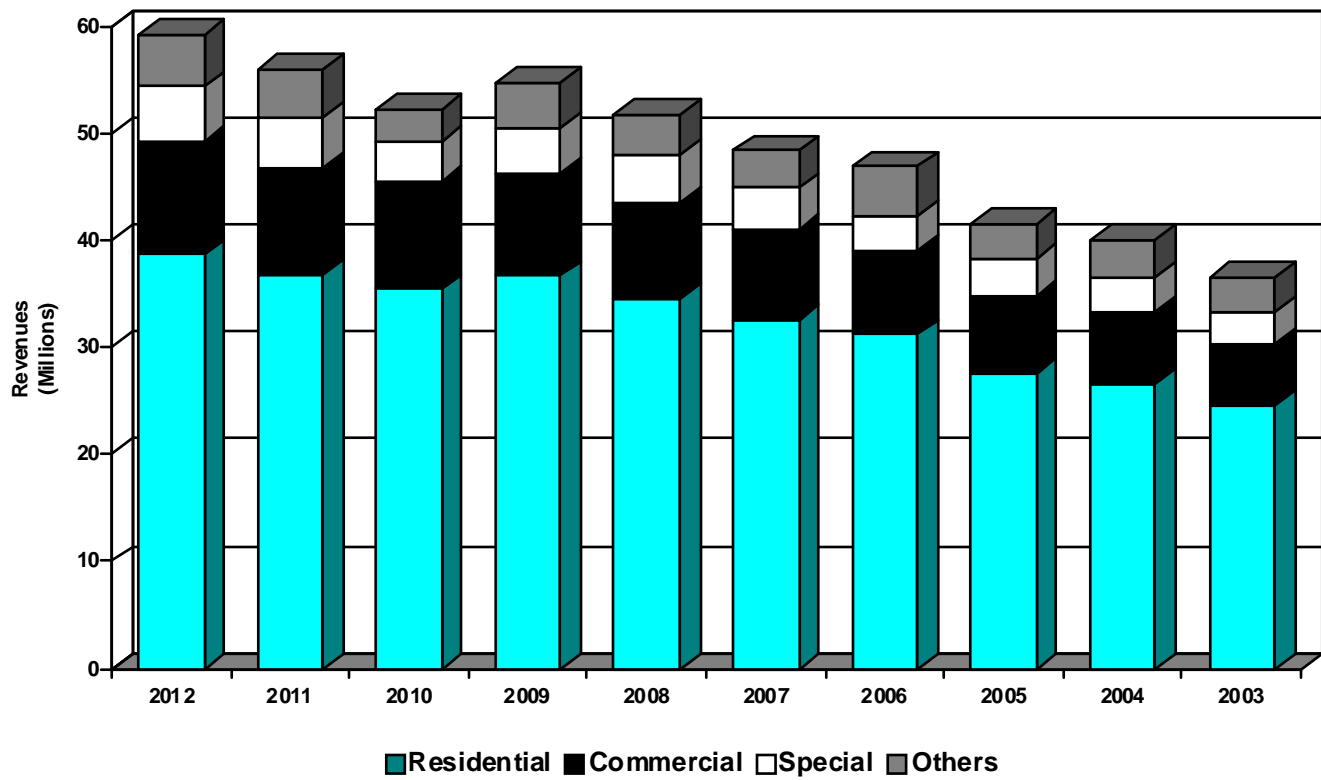
TOTAL OPERATING EXPENSES
Year to Date - December 2012
(\$51,350,381)



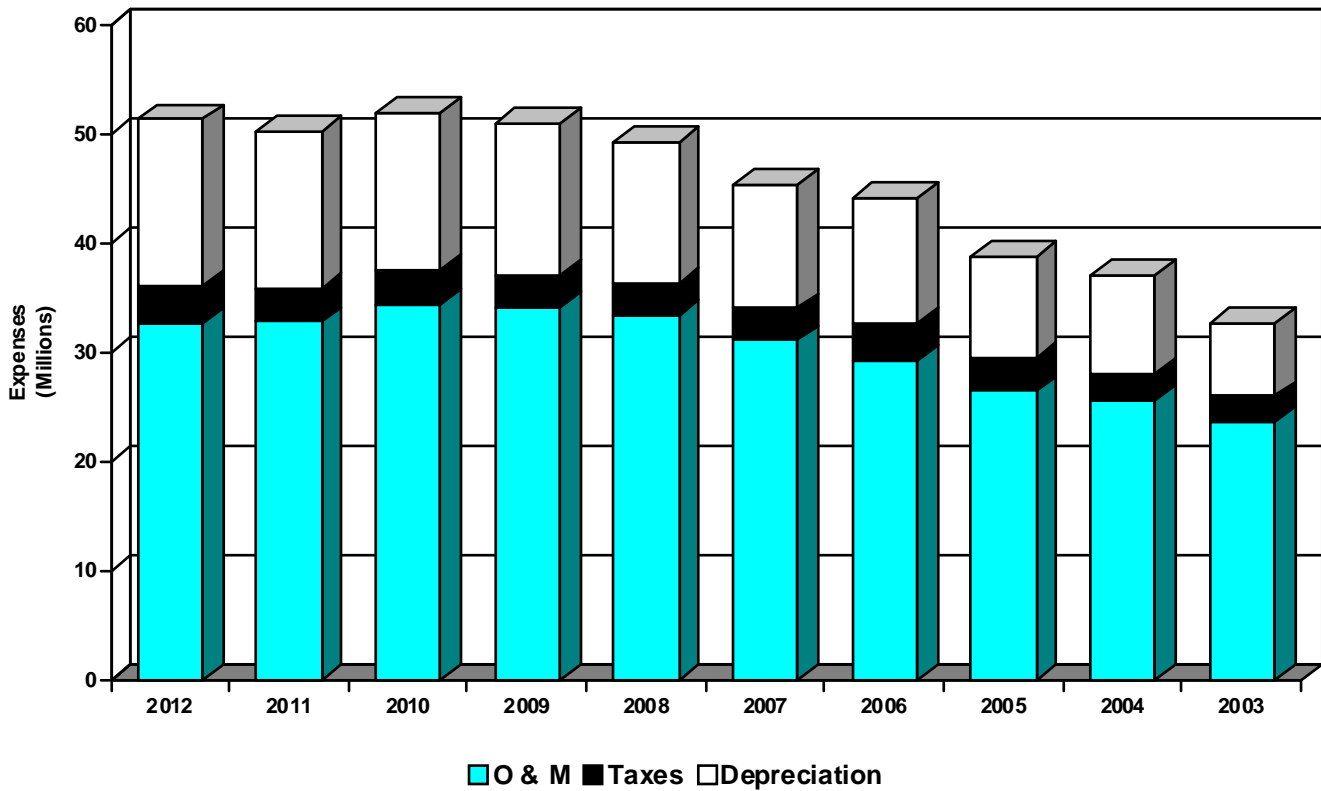
TOTAL OPERATING EXPENSES
Year to Date - December 2011
(\$50,317,808)



TEN-YEAR SUMMARY OF WATER SALES



TEN-YEAR SUMMARY OF OPERATING EXPENSES



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SUPERINTENDENT'S REPORT 2012 TACOMA WATER

Tacoma Water Management Team completed a strategic planning effort in early 2012. The adopted plan sets the direction and strategic focus for our Utility over the next many years. An updated mission and values were adopted along with a series of initiatives. The Tacoma Water Strategic Plan was presented to the Public Utility Board and provided to Tacoma Water staff during the second quarter. The plan provides us with a solid foundation by helping us understand and communicate the challenges we face. Eight initiatives were detailed to help us succeed in our mission of providing clean, reliable water now and in the future. Tacoma Water's management team also approved the approach we will use to track and report on Strategic Plan strategy and performance metric progress. A Balanced Scorecard Strategy Map was developed to provide structure for prioritization and measurement going forward. The Strategic Plan provided the basis for Tacoma Water's 2013/2014 budget request.

Summer weather in 2012 presented an interesting scenario; temperatures were similar to 2011 yet precipitation was, during late peak season, the lowest in years. Even with nice summer weather from mid July through early October, total water consumption in 2012 was similar to recent cool, wet summers. Water sales were lower than budgeted development activity, as indicated by new meter installs and residential System Development Charges, increased modestly due to construction of homes on developed lots.

Expenses were managed throughout all sections of Tacoma Water to respond to the reduced revenues resulting from poor water sales. Approximately 20 positions were held vacant, equipment was surplussed and not replaced and inventory turnover was improved and the economic recovery remained sluggish.

Four-year labor contracts for Tacoma Water's unionized staff were negotiated for the period of 2011 through 2014. The wage rates for the first two years will not increase implementation of the City's compensation policy regarding market rate wages will be implemented in the 2013/2014 timeframe.

In June, Tacoma Water entered into a water supply agreement with Auburn to provide 1 MGD of water supply. Auburn began purchasing water in late 2012; these sales are expected to generate in excess of \$1M annually.

Tacoma Water also renegotiated its agreement with the Cascade Water Alliance (Cascade), effective December 31, 2012. The new agreement restructures the payment obligations contained in the 2005 agreement from Cascade to Tacoma Water into a defined payment stream that totals \$119.7 million over the next 30 years. This agreement also contains provisions for the transfer of up to 10 million gallons per day of wholesale water supply capacity to Auburn, Buckley, Bonney Lake, and Sumner, which could result in significant additional water sales revenue for Tacoma reduce future water rates for all Tacoma Water customers.

In 2009, Tacoma Water removed the cost of public fire protection from rates and instead billed the applicable local governments pursuant to Washington State Supreme Court decision *Lane v. City of Seattle*. The Washington State Supreme Court decided on January 26 of 2012, in *City of Tacoma v. Bonney Lake*, that Tacoma Water should not have removed the cost of public fire protection from the 2009 – 2012 rates of customers outside City of Tacoma limits in jurisdictions where we have franchise agreements. Consistent with our understanding of the opinion, Tacoma Water did the following: continued to invoice the City of Tacoma for the cost of public fire protection inside City limits; deemed the invoices sent to the applicable outside City of Tacoma local governments for the period 2009 – 2012 uncollectable, eliminated invoice balances, and refunded as appropriate; and established a regulatory deferral per Financial Accounting Standard 71 for accounting years 2009 -2012 for recovery of uncollected costs related to outside City of Tacoma public fire protection services demonstrating intent to recover the lost revenue. Tacoma Water has proposed a “Franchise Fire Protection Rate” to recover these historical costs, as well as the ongoing costs of providing public fire protection, from those customers outside the city of Tacoma that receive the service. Tacoma Water is also actively participating in statewide efforts to accomplish additional clarity through a legislative fix.

WATER QUALITY

In 2012 the Water Quality section contributed to Tacoma Water’s continued commitment to protect public health, and to support Tacoma and the region with a high quality, reliable water supply. Highlights are briefly discussed in the following sections.

Green River Filtration Treatment

Design was completed and the Green River filtration plant moved into construction in 2012. The construction of this complex plant requires expert planning and project execution. The Tacoma Water construction management team, together with the selected General Contractor / Construction Manager, Hoffman Construction Company, are successfully delivering the project on schedule, and within budget. The project is targeted for substantial completion in December 2014, and the total project budget has reduced from \$211 million at the beginning of the year to \$195 million at year end, with over 85% of the project work under contract.

In 2012, Tacoma Water and its Regional Water Supply System (RWSS) Partners decided to incorporate Tacoma Water’s North Fork Well Field facilities into the design of the Green River Filtration Facility (GRFF) as a result of a business case evaluation (BCE) that was conducted by Tacoma Water staff and MWH Global, the design engineer for the GRFF. This is a significant decision from a treatment plant design perspective, in that it will significantly reduce expenses associated with the construction and operation of the solids handling components of the GRFF. Tacoma Water is actively engaged with Tacoma Power and Puget Sound Energy in developing a strategy to optimize energy use for these facilities once the GRFF is online.

Groundwater Treatment

Construction of groundwater treatment facilities at the Hood Street Reservoir and at the South Tacoma Pump Station began in 2012, and is well underway. This project will enhance Tacoma Water's ability to serve groundwater from the South Tacoma aquifer that meets requirements for treatment to reduce lead and copper exposure, and to provide fluoridation at the Hood Street Reservoir, in accordance with the expectations of Tacoma voters and the City's ordinance.

Meeting Expectations

Customer confidence is hard-won, and easily lost. Professionalism and timeliness of response when customers have a concern is critical. In 2012 we continued measuring our success – ensuring that our customers who call with a concern about their water quality get a very rapid response. We exceeded our established goal of responding to at least 98 percent of all Water Quality calls on the same day. We continued our strong record of active system surveillance through water quality testing, and uninterrupted regulatory compliance.

Protecting and Preserving our Natural Environment

Our Watershed Management and Environmental Programs advanced the protection of critical assets in 2012 through the continued implementation of bridge and culvert evaluation and replacement projects on watershed lands, implementing additional surveillance and tracking, and improved maintenance procedures. There was continued progress meeting Tacoma Water's aggressive environmental obligations embodied in our Habitat Conservation Plan. Managing the lands and water resources with which we are entrusted is a cornerstone value at Tacoma Water, and one we share with our resource management partners.

Protection of our Green River water supply was improved in 2012 with the acquisition of 344 acres of forest land in the Sawmill Creek sub-basin. The land, which includes the largest piece of old growth timber remaining in private ownership in the Green River watershed, was purchased by an NGO (Forterra Northwest) using a Cooperative Endangered Species Conservation Fund grant administered by Washington Department of Natural Resources. The land was subsequently given to Tacoma Water in December 2012 to be managed under a conservation easement for the protection of ESA-listed species and water quality. These lands together with an adjacent parcel previously acquired from the Forterra (then Cascade Land Conservancy) and with the U.S. Forest Service's Kelly Butte Special Management Area represent a large block of contiguous habitat that provides ecological connectivity with similarly protected parcels in the I-90 Corridor and high quality ecosystem functions, such as water supply and quality to benefit Tacoma Water customers.

WATER SUPPLY

The Water Supply section made progress in 2012 on its mission of operating, maintaining and improving the infrastructure that forms Tacoma's water supply system to assure reliable supply to our customers.

Infrastructure Design and Construction

The construction of the McMillin Reservoir Replacement Project was completed. This major project represented the last of our open reservoir basins having been converted to enclosed tanks. The two new 33 million gallon covered concrete tanks, are the largest tanks of their kind in the world, and replace the three open basins that previously held up to 210 million gallons of storage. The old reservoirs had been in service for 50 to 100 years and were at the end of their useful lives. This is a significant improvement to Tacoma's supply system both from a maintenance perspective and water quality perspective. The conversion of these previously open basins to enclosed tanks has eliminated a safety hazard in that we no longer need to rechlorinate and have removed the gas chlorine from the site.

The replacement of a portion of Pipeline 1 across the Orting Valley wetlands was completed in 2012. This was phase 1 of the replacement project of the last original section of the Green River Pipeline and is located in an area vulnerable to flooding and volcanic eruption. The work to replace these remaining above ground sections of pipeline with buried sections will assure better reliability and safety of this critical line.

An extensive upgrade and modernization to the entire Supervisory Control and Data Acquisition (SCADA) system and the communication network (including 2 new microwave sites) was completed in 2012. This system-wide upgrade was the first since the system was installed in the late 1980's and will improve both the reliability and effectiveness of the operations of the water system.

Preliminary work needed to rehabilitate a section of Pipeline 2 at Woodland Avenue was completed in 2012. Several distribution mains were installed and customers originally connected to the pipeline were transferred to the new distribution mains. As a result, an extended shutdown of Pipeline 2, which is needed to accomplish the relining work, can occur without inconveniencing customers. Relining of the transmission main will occur in the 1st quarter of 2013.

Operations & Maintenance

Supply staff continued to actively participate in the development of the Division's Asset Management program.

A consolidation of reporting headquarters was accomplished in 2012. The consolidation will provide efficiencies to our operation by pooling resources at a single location, and will decrease expenses by shutting down a reporting headquarters and consolidating crews at an existing site.

A shift schedule similar to a schedule used at our Headworks facility was implemented in our Water Control Center. This allowed a downsizing of the workforce required to staff the Water Control Center from the historical 6 employees to a total of 4. This change will provide significant financial benefits to Tacoma Water, as well as provide significant benefits to the employees working the shifts.

In addition to operating and maintaining Tacoma Water's transmission and supply system, the section also coordinates operation and maintenance of the transmission system supplying the Regional Water Supply System partnership, and coordinates all activities with the US Army Corp of Engineers relating to Howard Hanson Dam. Success in these activities requires close interaction with a wide variety of stakeholders including regulators, resource agencies, tribes, project partners, interest groups and the general public.

FINANCIAL MANAGEMENT & RATES

In 2012, Tacoma Water undertook an extensive financial modeling effort in support of the 2012 strategic planning process and 2013-2014 budget development. Additionally, we rebuilt our cost of service rate model. The rate model work required involvement across all Tacoma Water Sections along with support from a rate consultant. The preliminary findings of this analytical effort have been communicated to the Public Utility Board, with additional outreach to various customer groups and review by the City Council in early 2013.

The proposed rate adjustment is scheduled for City Council consideration in late February, and implementation April 1, 2013. Tacoma Water customers will see an overall average increase of 6.0%. Another 6.0% overall increase is scheduled for January 1, 2014. The rate increase varies by customer class, based on the cost of serving each customer class.

In 2012, Tacoma Water received clarification from the City of Tacoma Tax and License Department regarding applicability of gross earnings tax on Public Fire Protection revenues. Based on the Tacoma Municipal Code, the Utility is allowed a deduction from the gross earning tax for revenue received for inside and outside City Public Fire Protection Fees, fire hydrant rentals, damage reimbursements and interest earned in the RWSS Operating Fund on behalf of the RWSS Partners. However, the Department found that 'fire service, hydrant rental' as written in the Code does not include Private Fire Protection revenue and is not an allowed deduction. Tacoma Water received a refund of \$486,956 for inside Public Fire Protection Revenues, \$348,331 for outside City Public Fire Protection Revenues, \$1,436 for Fire Hydrant Rental Revenue, \$11,604 for Damage reimbursements and \$17,797 for RWSS Interest earned by the Partners. The Utility subsequently refunded the City \$486,956 for Gross Earnings Tax collected on inside City Public Fire Protection Fees. In addition, Tacoma Water was required to pay \$181,143 for unpaid tax on Private Fire Protection revenue. Including interest, Tacoma Water received a net refund of \$241,117 at the end of 2012.

DISTRIBUTION OPERATIONS

As the economic slowdown continued in 2012 Distribution Operations continued efforts to reduce costs. Working in collaboration with Distribution Engineering, galvanized water services and mains were targeted for replacement. Customer complaints due to low pressure, inadequate flow, service disruption due to main breaks, and discolored water were the basis for targeting galvanized mains. Some of the main replacement projects were assigned to Tacoma Water crews, rather than being contracted out.

Controlling expenses continued by exploring various options for accomplishing work, and evaluating vacancies as they become available. An extensive staffing review was conducted as part of the planning process for the 13/14 biennial budget with the goal of restructuring for our future needs. As a result, Distribution Operations reduced staffing by 2 construction crews and a supervisor position, a total reduction of nine FTE's by the end of 2012.

Planner/Scheduler

Distribution Operations initiated a planner/scheduler pilot program in June of 2012. The planner/scheduler pilot involves supervisors providing their work plan by 4:00 p.m. The following morning, staff availability is reaffirmed and resources allocated to the highest priority jobs. An immediate benefit was realized in the daily morning scheduling effort as a result of teamwork, collaboration and focusing on section wide work priorities.

Leadership Program

Six employees were selected to be part of a new Tacoma Water Leadership. The program included completing the Water Division Manager role profile assessment, management feedback session, and job shadowing. Additionally training was offered to all 25 staff who applied for the Leadership Program including the six who were selected. The training sessions covered accounting, budget, and rate setting.

Fleet Improvements

To be more efficient and environmentally aware, Tacoma Water's fleet was evaluated for improvement opportunities. Automatic Vehicle Location (AVL) system technology was installed in all Tacoma Water vehicles by the end of the first quarter 2012. Weekly reports on idle times and speeding events were tracked and followed up on. Monthly averages were compiled in 2012 with the potential of establishing specific goals for 2013.

Each piece of equipment in Distribution Operations was reviewed to determine what to surplus as a result of the crew downsizing. Using replacement and surplus funds to buy down future replacement costs, a savings of \$675,000 in fleet costs will be realized in 2013/2014 and another \$800,000 will be saved in the next two biennia.

Performance Management

Several performance metrics tracked by Distribution Operations were met or exceeded reflecting significant operational efficiencies:

Reduce Labor hours on fixed fee new service installs by 20% average as compared to 2010 average labor hours. Fixed fee service install include full service installs for 3/4 x 5/8 and 1x1. The average labor hours for 2010 fixed fee jobs was 38 hrs.. The average for 2012 was 27.14 hrs.

Complete EDPR's for each represented employee within 30 days of job classification anniversary date 95% of the time. Also, each EDPR will include 3 measurable personal goals, with one goal focused on efficient operations. For 2012 99% of EDPR's for 101 employees were turned in within 30 days and with 3 measurable personal goals.

Bill all time and materials orders within 60 days after final invoice or activity 90% of the time. As of third quarter the average time for billing is 29.76 days with 90% completed within 60 days.

Respond to all Distribution Operations high priority notifications on site within less than 2 hours average. The average as of third quarter is 90 minutes.

Systematic flushing

As we are an unfiltered, river water supply, it is critical that we regularly flush our water mains. In 2012 our Unidirectional flush crews completed 2,071,233 lineal feet or 392.3 miles of distribution mains, almost 100 miles more main than was flushed in 2011, making it the sixth consecutive year of increased main flushing productivity.

Fire Hydrant Maintenance

All fire hydrants receive comprehensive maintenance every other year. Efficient routing, improved record keeping, replacement of old scissor style hydrants and a mature hydrant maintenance program has resulted in high degree of hydrant reliability and low incidence of issues.

Meters

Changes in the availability of Compound, Turbine and Fire service meters, and new Federal Regulations relating to acceptable levels of lead in potable water products has lead Tacoma Water to investigate new meter technologies. A team of stakeholders identified metering options to respond to these changes and our business needs. The team used Asset Management principles considering life cycle costs in the evaluation process and started bench and field tests of several meters. A business case evaluation was been completed and meters will continue to be tested before a final decision is made.

ASSET AND INFORMATION MANAGEMENT (FORMERLY RESOURCE PLANNING)

Asset Management

Tacoma Water continued to make Asset Management progress in 2012. Some noteworthy accomplishments from the 2012 work plan include: initiating failure modes assessment for both the Treatment & Monitoring and Pump Station strategic asset management plans (SAMPs); holding a 2-day Asset Management workshop attended by 23 Tacoma Water employees; launching an Asset Management Forum to bring SAMP leads together; participating in development of the Balanced Scorecard strategy map; and enhancing our economic model by creating a multiple asset decision tool which allows multiple assets to be brought together to analyze the benefit of a project.

Information Management

Much work related to information management was conducted in 2012 to ready the organization for the future. The importance of Information Management was recognized by making it an initiative in our Strategic Plan. In addition, staff worked collaboratively across Tacoma Public Utilities and with Tacoma Power in particular to develop and support a new governance model for IT projects including the creation of a Project Management Office. Specific to Tacoma Water, an IT Roadmap was adopted as part on the Information Management initiative in our Strategic Plan with a supported budget

request for 13/14. We are well positioned to improve our GIS system in the coming years with a study completed in December 2012 along with completing the mapping of pipelines 1 and 5 and publishing them in our MapGuide System.

Federal Way Franchise

The Public Utility Board authorized acceptance of a new Tacoma Water franchise with the City of Federal Way. It is a 10 year franchise with the option of a 10 year extension to operate within its jurisdiction. Tacoma Water and the City of Federal Way began franchise negotiation in 2009 in anticipation of franchise expiration in June of that year. Following months of negotiation and given the uncertainty at that time regarding public fire protection we agreed to a one-year extension of the franchise to allow for resolution of public fire protection questions. The one-year extension was ultimately not enough and agreement was reached to continue to use the 1999 franchise until after resolution of the public fire protection matter in court. Negotiation of the proposed franchise picked up from where we left off in 2009 and contains a section providing public fire protection resolution for Tacoma Water in Federal Way. The terms of the franchise are generally favorable and will result in improved coordination and ability to serve our customers within City of Federal Way limits.

DISTRIBUTION ENGINEERING

Infrastructure

Distribution Engineering worked on many large water main replacement projects in 2012, throughout Tacoma and the greater service area. The Replacement Program constructed 10.3 miles of distribution main in 2012. Development of our strategic asset management plan for distribution mains has helped us with prioritization of replacements and identification of necessary funding levels to reliably sustain the distribution system and the work accomplished in 2012.

New Service/Development Support

Staffing at the Water Permit Counter was reduced in recognition of continuing slow development activity. Private development in 2012 shifted from primarily commercial over the past two years to over 90 percent residential. Residential meter installs on existing service stubs increased to 443, which is more than double 2011. Water main construction was completed on 12 private contracts in 2012, resulting in 2.44 miles of new main. Tacoma Water supported the area's economic development strategy and strengthened its partnership with Tacoma/Pierce County Economic Development Board with a successful effort to attract Carlisle Construction Materials to our service area. The Point Ruston development continued in 2012, with completion of all on-site water mains, as well as a signed Operations and Maintenance agreement.

Water Efficiency

The Water Conservation team was reassigned to Distribution Engineering midyear to consolidate customer program activities. Tacoma's Water Conservation Program had another busy year with great accomplishments and new endeavors. "Energy and Water Saving Kits" were direct mailed to 6,000 customers through a partnership with Tacoma Power. Included in the kits were items such as showerheads, faucet aerators, and water conservation literature. The "Know Your H2O" campaign continues to be a draw with customers and visible in the community with general advertising, vehicle wraps, an informational guidebook for customers, and 15-second TV spots. Tacoma Water chaired a committee through the Partnership for Water Conservation that produced a report "Cooperative Conservation: A Report of the Implementation of Washington's Water Use Efficiency Rule." The report demonstrates progress towards greater water efficiency among water suppliers in Washington since the adoption of the Water Use Efficiency Rule in 2007. A Home Water Use Review pilot project was offered to customers and provided a free residential water audit. Tacoma Water is a participant on the national Residential End Uses of Water study being led by the Water Research Foundation. The study will examine and quantify the "end uses" of water including all the places where water is used in a single-family home such as toilets, showers, clothes washers, faucets, lawn watering, etc.

Linda McCrea
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.

APPENDIX E
FORM OF OPINION OF BOND COUNSEL

City of Tacoma, Washington

Re: City of Tacoma, Washington,
\$64,795,000 Regional Water Supply System Revenue Refunding Bonds, 2013

We have served as bond counsel to the City of Tacoma, Washington (the “City”), in connection with the issuance of the above-referenced Regional Water Supply System Revenue Refunding Bonds, 2013 (the “Bonds”), and in that capacity have examined such law and such certified proceedings and other documents as we have deemed necessary to render this opinion. As to matters of fact material to this opinion, we have relied upon representations contained in the certified proceedings and other certifications of public officials furnished to us, without undertaking to verify the same by independent investigation.

The Bonds are issued by the City pursuant to Ordinance No. 28137 (the “Bond Ordinance”) to provide the funds to refund a portion of the outstanding bonds, fund the Reserve Account, if necessary, and pay the costs of issuance of the Bonds, all as set forth in the Bond Ordinance.

For as long as any of the Bonds are outstanding, the City irrevocably has pledged to set aside from the Revenues of the Regional System and to pay into the “Regional Water Supply System Bond Fund” (the “Bond Fund”) the various amounts required by the Bond Ordinance to be paid into and maintained in such Bond Fund within the times provided by the Bond Ordinance. Revenues of the Regional System include Gross Revenues of the City’s Water System and Participants’ Payments under the Project Agreement for the Second Supply Project, subject to the prior payment of Operating Expenses, and all money and investments held in the Bond Fund. The Bonds are special limited obligations of the City and are not obligations of the State of Washington or any political subdivision thereof other than the City, and neither the full faith and credit nor the taxing power of the City or the State of Washington is pledged to the payment of the Bonds.

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

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

Under the Internal Revenue Code of 1986, as amended (the “Code”), the City is required to comply with certain requirements after the date of issuance of the Bonds in order to maintain the exclusion of the interest on the Bonds from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Bond proceeds and the facilities financed or refinanced with Bond proceeds, limitations on investing gross proceeds of the Bonds in higher yielding investments in certain circumstances and the arbitrage rebate requirement to the extent applicable to the Bonds. The City has covenanted in the Bond Ordinance to comply with those requirements, but if the City fails to comply with those requirements, interest on the Bonds could become taxable retroactive to the date of issuance of the Bonds. We have not undertaken and do not undertake to monitor the City’s compliance with such requirements.

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

1. The City is a duly organized and legally existing first-class city under the laws of the State of Washington.

2. The Bonds have been duly authorized and executed by the City and are issued in full compliance with the provisions of the Constitution and laws of the State of Washington and the ordinances of the City relating thereto.

3. The City has irrevocably bound itself to set aside and pay into the Bond Fund and the Reserve Account therein out of Revenue of the Regional System, amounts necessary to pay the principal of and interest on the Bonds as the same become due.

4. The City has pledged that the payments to be made into the Bond Fund and the Reserve Account out of Revenue of the Regional System shall be a lien and charge thereon equal in rank to the lien and charge upon such Revenue of the amounts required to pay and secure the payment of the Outstanding Parity Bonds and any regional water supply system revenue bonds of the City hereafter issued on a parity with the Bonds, and superior to all other liens and charges except the Operating Expenses of the Regional System. The City has reserved the right to issue Future Parity Bonds on the terms set forth in the Bond Ordinance.

5. Assuming compliance by the City after the date of issuance of the Bonds with applicable requirements of the Code, the interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals; however, while interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by corporations is to be taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by certain S corporations may be subject to tax, and interest on the Bonds received by foreign corporations with United States branches may be subject to a foreign branch profits tax. We express no opinion regarding any other federal tax consequences of receipt of interest on the Bonds.

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

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

Respectfully submitted,

FOSTER PEPPER PLLC

APPENDIX F

GENERAL AND ECONOMIC INFORMATION

Participants

City of Tacoma. Tacoma, the county seat of Pierce County (the “County”), is located in the west central part of Washington State near the southern tip of Puget Sound. It is the third largest city in the State with a 2012 estimated population of 199,600. The City is located 32 miles south of Seattle and 28 miles northeast of Olympia, the State capital.

City of Kent. Kent is located in southern King County, in the Green River Valley, approximately 18 miles south of Seattle and 18 miles northeast of Tacoma. State Highways Nos. 167, 181 and 516 pass through Kent, and Interstate 5 passes through the City’s west side. The City of Kent encompasses an area of approximately 29 square miles and has an estimated 2012 population of 119,100.

Covington Water District. Covington Water District is located in southeast King County, approximately 35 miles southeast of Seattle between the cities of Kent (ten miles west) and Auburn (three miles southwest). Covington Water District includes 100% of the City of Covington, approximately 60% of the City of Maple Valley and 10% of the City of Black Diamond. Covington Water District encompasses an area of approximately 55 square miles and has an estimated 2012 population of approximately 47,000.

Lakehaven Utility District. Lakehaven Utility District is one of the largest public water/sewer districts in the State and is located in southern King County and a small portion of the County. Lakehaven Utility District encompasses an area of approximately 35 square miles with a service population of approximately 112,000 people, including most of the City of Federal Way and to small portions of the cities of Auburn, Milton, Tacoma, Pacific, Des Moines and a part of unincorporated King County.

Population

The following tables show the historical population for the County, Tacoma, King County and the cities of Kent, Covington and Federal Way.

POPULATION		
CITY OF TACOMA AND PIERCE COUNTY		
Year	Tacoma	Pierce County
2012	199,600	808,200
2011	198,900	802,150
2010	198,397	795,225
2009	203,400	813,600
2008	202,700	805,400
2007	201,700	790,500
2006	199,600	773,500
2005	198,100	755,900
2004	196,800	744,000
2003	196,300	733,700

Source: Washington State Office of Financial Management estimates; U.S. Census for 2010 figure.

POPULATION
CITIES OF KENT, COVINGTON AND FEDERAL WAY AND KING COUNTY

Year	Kent	Covington	Federal Way	King County
2012	119,100	17,760	89,460	1,957,000
2011	118,200	17,640	89,370	1,942,600
2010	92,411	17,575	89,306	1,931,249
2009	88,380	17,530	88,580	1,909,300
2008	86,980	17,360	88,040	1,884,200
2007	86,660	17,190	87,390	1,861,300
2006	85,650	17,240	86,530	1,835,300
2005	84,920	16,610	85,800	1,808,300
2004	84,560	15,190	83,590	1,788,300
2003	84,210	14,850	83,500	1,779,300

Source: Washington State Office of Financial Management estimates; U.S. Census for 2010 figure.

Employment

Employment within Pierce and King Counties are described in the following tables:

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

NAICS Industry Title	Annual Average				
	2012	2011	2010	2009	2008
<u>Resident Labor Force</u>					
Employment	357,010	349,310	352,260	356,550	370,570
Unemployment	34,530	37,940	40,180	38,140	22,510
Total	391,540	387,250	392,440	394,690	393,080
Percent Of Labor Force	8.8%	9.8%	10.2%	9.7%	5.7%
 Total Nonfarm	 267,400	 265,200	 264,300	 268,500	 280,500
Total Private	210,400	207,400	205,900	210,700	223,500
Goods Producing	33,800	33,000	33,800	36,200	43,700
Mining and Logging	300	300	300	300	400
Construction	16,800	16,300	17,200	19,000	23,500
Specialty Trade Contractors	10,700	10,500	10,800	12,000	15,000
Manufacturing	16,700	16,400	16,300	16,900	19,800
Services Providing	233,600	232,100	230,500	232,200	236,700
Trade, Transportation And Utilities	55,100	54,300	53,000	53,100	55,600
Wholesale Trade	11,100	10,900	10,900	11,000	11,400
Retail Trade	31,800	31,700	31,200	31,200	32,900
Food And Beverage Stores	5,900	5,600	5,500	5,400	5,500
General Merchandise Stores	8,000	8,000	7,800	7,800	7,900
Transportation and Utilities	12,200	11,600	10,900	10,900	11,400
Information	2,700	2,800	3,000	3,100	3,700
Financial Activities	11,500	11,200	11,200	12,300	13,200
Professional And Business Services	23,900	23,900	23,500	23,900	24,900
Admin, Support, Waste Mgmt & Remed.	14,300	14,200	13,600	13,500	14,300
Administrative And Support Services	13,000	12,900	12,200	12,100	12,900
Education And Health Services	44,200	43,800	43,600	43,200	41,600
Ambulatory Health Care Services	14,500	14,300	14,000	14,000	13,600
Hospitals	11,000	10,900	10,600	10,200	9,600
Leisure And Hospitality	26,200	25,500	25,300	26,200	27,800
Food Services And Drinking Places	20,500	19,900	19,800	20,600	22,100
Other Services	13,000	12,900	12,600	12,700	13,000
Government	57,000	57,800	58,400	57,800	56,900
Federal Government	12,800	13,200	13,200	11,700	10,800
State Government	10,500	10,600	11,300	11,700	11,900
State Government Educational Services	3,700	3,700	3,700	3,600	3,800
Local Government	33,700	34,000	34,000	34,400	34,300
Local Government Educational Services	18,400	18,400	18,400	18,400	18,200

Source: Washington State Employment Security Department.

KING COUNTY
RESIDENT CIVILIAN LABOR FORCE AND EMPLOYMENT AND AVERAGE CIVILIAN
NONAGRICULTURAL WAGE AND SALARY EMPLOYMENT(I)

NAICS Industry Title (1)	Annual Average				
	2012	2011	2010	2009	2008
Resident Labor Force					
Employment	1,034,840	1,015,970	1,006,000	1,020,090	1,043,300
Unemployment	77,570	89,580	101,060	95,890	48,420
Total	1,112,410	1,105,550	1,107,060	1,115,980	1,091,720
Percent Of Labor Force	7.0%	8.1%	9.1%	8.6%	4.4%
 Total Nonfarm	1,183,600	1,154,100	1,133,300	1,152,000	1,217,600
Total Private	1,018,300	989,100	966,300	984,800	1,051,200
Goods Producing	157,100	149,600	148,200	160,400	186,500
Natural Resources and Mining	400	500	500	500	600
Construction	52,600	48,800	49,700	57,100	73,900
Construction of Buildings	14,100	13,000	13,200	15,600	20,600
Heavy & Civil Engineering Construction	5,900	5,300	5,300	5,400	6,800
Specialty Trade Contractors	32,700	30,500	31,300	36,200	46,500
Manufacturing	103,900	100,400	98,000	102,800	112,000
Durable Goods	80,100	77,200	75,200	79,000	86,200
Nondurable Goods	23,800	23,200	22,800	23,800	25,800
Services Providing	1,026,600	1,004,400	985,100	991,500	1,031,100
Trade, Transportation And Utilities	218,400	211,800	206,300	209,200	224,700
Wholesale Trade	60,900	59,200	58,000	59,700	64,000
Retail Trade	113,200	109,000	105,900	106,000	113,800
Transportation, Warehousing And Utilities	44,300	43,600	42,400	43,500	46,900
Information	80,100	80,000	79,400	80,200	79,800
Software Publishers	51,100	50,300	49,500	50,100	49,100
Wired Telecommunications Carriers	3,000	3,500	4,400	5,100	4,900
Financial Activities	67,600	67,300	67,700	71,200	77,500
Finance and Insurance	44,600	44,600	44,500	46,900	51,300
Real Estate & Rental & Leasing	23,000	22,700	23,200	24,300	26,300
Professional And Business Services	192,200	184,700	176,700	176,800	194,200
Professional, Scientific & Tech Services	101,200	98,400	93,400	92,900	98,800
Mgmt of Companies & Enterprises	25,400	23,500	22,200	22,700	24,600
Admin, Support, Waste Mgmt & Remed.	65,600	62,900	61,000	61,100	70,800
Education And Health Services	145,200	142,200	138,100	137,700	133,300
Educational Services	23,900	23,600	23,000	22,700	22,300
Ambulatory Health Care Services	49,400	48,200	47,400	46,400	44,600
Hospitals	28,300	27,900	26,500	26,500	25,300
Nursing & Residential Care Facilities	19,900	19,400	18,400	18,400	17,900
Social Assistance	23,700	23,200	22,900	23,700	23,300
Leisure And Hospitality	114,700	111,100	108,800	108,100	113,400
Arts, Entertainment & Recreation	21,800	21,800	21,800	21,400	22,300
Accommodation	12,900	12,900	12,600	12,800	13,600
Food Services And Drinking Places	80,000	76,500	74,400	74,000	77,400
Other Services	43,000	42,300	41,200	41,200	41,900
Government	165,300	164,900	167,000	167,200	166,400
Federal Government	20,700	21,200	21,900	22,100	21,600
State Government	55,500	55,000	55,800	55,800	55,600
Local Government	89,200	88,800	89,300	89,300	89,200

Source: Washington State Employment Security Department.

PIERCE COUNTY MAJOR EMPLOYERS

Employer	Type of Business	Number of Employees
Joint Base Lewis McChord	Military	56,624
Local Public School Districts (K-12)	Education	13,352
Multicare Health System	Health Services	6,547
Washington State	Public Sector	6,488
Franciscan Health System	Health Services	5,704
Pierce County Government	Government/Public Offices	2,872
Washington State Higher Education	Education	2,632
City of Tacoma (excluding Tacoma Public Utilities)	Government/Public Offices	2,222
Emerald Queen Casino	Casino Gambling	2,200
Wal-Mart	Retail	1,785
The Boeing Company (Frederickson Site)	Aerospace	1,700
Tacoma Public Utilities	Public Utility	1,332
Costco	Wholesale	1,185
US Postal Service	Government/Public Offices	1,100
State Farm Insurance Companies	Insurance	1,070
Washington State National Guard	Military	1,050
Comcast Cable	Cable Televisions Services	1,018

Source: Economic Development Board of Tacoma-Pierce County, 2012.

PUGET SOUND AREA(1) MAJOR EMPLOYERS

Firm/Organization	Product or Service	Number of Employees (1)
The Boeing Company	Aerospace	82,000 (2)
Joint Base Lewis-McChord	Military	56,000
Navy Region Northwest	Military	46,376 (3)
Microsoft	Technology	40,376
University of Washington	Education	26,978
Wal-Mart Stores, Inc.	Retail	18,011
Fred Meyer Stores	Retail	14,300
King County Government	Government/Public Offices	13,448
Providence Health & Services	Healthcare	12,225
United States Postal Service	Postal Service	11,998
Starbucks Corp.	Retail	10,166
Swedish	Healthcare	9,825
City of Seattle	Government/Public Offices	9,631
MultiCare Health System	Healthcare	9,103
Franciscan Health System	Healthcare	8,518
Costco Wholesale Corp.	Wholesale	8,267
Group Health Cooperative	Healthcare	8,225
Nordstrom Inc.	Retail	8,189
Alaska Air Group, Inc.	Airline	6,606

(1) Does not include part-time or seasonal employment figures.

(2) From Boeing, as of December 31, 2011.

(3) Includes Whidbey Naval Air Station and Everett Naval Air Station.

Source: Puget Sound Business Journal Book of Lists, 2012.

Personal and Per Capital Income

Historic personal income and per capital income levels for Pierce County, King County and the State of Washington are shown below:

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

Year	Pierce County		King County		State of Washington	
	Total Personal Income (\$000)	Per Capita Income	Total Personal Income (\$000)	Per Capita Income	Total Personal Income (\$000)	Per Capita Income
2011(1)	\$ 33,117,849	\$ 40,992	\$ 113,922,436	\$ 57,837	\$ 299,685,263	\$ 43,878
2010	31,625,073	39,761	106,401,739	54,927	283,367,864	42,024
2009	31,228,180	39,208	103,120,593	53,933	276,727,871	41,504
2008	32,198,440	40,996	109,927,858	58,628	289,433,693	44,106
2007	30,164,757	39,049	106,693,888	57,735	272,624,864	42,192
2006	27,915,787	36,567	99,609,451	54,641	252,091,288	39,570
2005	25,579,464	34,190	89,432,163	49,815	230,057,261	36,766
2004	23,905,533	32,299	89,382,811	50,348	222,421,768	35,998
2003	22,789,755	31,050	80,128,451	45,439	206,983,236	33,909
2002	21,933,684	30,125	78,430,459	44,596	200,492,998	33,126

(1) Last available data.

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

Taxable Retail Sales

Taxable retail sales reflect only those sales subject to retail sales tax. Historic taxable retail sales for the City of Tacoma and Pierce County and the Cities of Kent and Federal Way and King County are shown below:

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

Year	Pierce County	City of Tacoma
2012 (1)	\$ 2,484,930	\$ 931,712
2011	10,428,907	3,826,546
2010	10,547,025	3,849,214
2009	10,359,977	3,803,604
2008	11,621,810	4,288,739
2007	12,449,284	4,665,527
2006	12,068,965	4,536,401
2005	11,177,879	4,218,012
2004	10,055,822	3,832,668
2003	9,448,120	3,708,718

(1) Through the first quarter of 2012. The taxable retail sales for Pierce County for the first quarter of 2011 was \$2,432,448,662 and \$909,779,399 for the City of Tacoma.

Source: Washington State Department of Revenue.

KING COUNTY AND CITIES OF KENT AND FEDERAL WAY⁽¹⁾
TAXABLE RETAIL SALES
(\$000)

Year	King County	Kent	Federal Way
2012 (1)	\$ 9,652,698	\$ 374,522	\$ 274,283
2011	40,846,119	1,608,647	1,216,636
2010	39,275,353	1,549,393	1,195,495
2009	39,594,904	1,556,361	1,208,587
2008	45,711,920	2,165,011	1,354,503
2007	47,766,339	2,626,702	1,474,686
2006	43,993,479	2,589,371	1,401,412
2005	40,463,997	2,321,255	1,290,165
2004	37,253,104	2,263,708	1,190,030
2003	35,370,831	2,005,341	1,179,841

(1) Through the first quarter of 2012. The taxable retail sales for the first quarter of 2011 for King County was \$9,131,182,690, \$363,517,949 for the City of Kent and \$275,465,312 for the City of Federal Way.

Source: Washington State Department of Revenue.

Building Permits

The total number and value of new building permits in Pierce County and King County are listed below:

PIERCE COUNTY NEW RESIDENTIAL BUILDING PERMIT VALUES

Year	Single-Family		Multi-Family	
	Total Permits	Total Value	Total Units	Total Value
2012	2,007	\$513,727,095	472	\$ 48,284,707
2011	1,487	358,523,919	1,072	119,788,982
2010	1,703	396,954,508	192	22,130,123
2009	1,240	242,118,582	804	79,995,681
2008	1,795	339,876,617	543	64,271,436
2007	3,537	718,169,188	1,490	176,217,591
2006	4,839	864,902,045	1,062	131,476,813
2005	5,402	928,758,256	1,204	141,101,681
2004	4,348	676,867,250	1,438	140,259,564
2003	4,400	643,284,106	752	60,428,746

Source: U.S. Census Bureau.

KING COUNTY BUILDING PERMIT ACTIVITY

Year	Single-Family		Multi-Family	
	Total Permits	Total Value	Total Units	Total Value
2012	3,719	\$1,082,990,642	7,343	\$1,070,032,832
2011	2,607	734,032,262	3,273	421,062,010
2010	2,537	692,929,762	3,371	318,012,250
2009	1,975	529,224,279	1,156	134,440,538
2008	3,026	865,838,017	7,414	1,008,233,396
2007	5,198	1,504,067,269	10,207	1,246,161,883
2006	5,767	1,620,644,028	8,300	1,023,393,178
2005	6,330	1,740,291,588	5,703	556,297,096
2004	6,947	1,684,139,845	4,998	451,908,793
2003	6,354	1,543,557,962	3,503	309,101,770

Source: U.S. Census Bureau.