



*Wastewater and Surface Water
Management
2013 Financial Report*

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Independent Auditor's Report

REPORT OF INDEPENDENT AUDITORS

Honorable Mayor and City Council
City of Tacoma, Washington Public Works Department, Environmental Services,
Wastewater and Surface Water Management
Tacoma Washington

Report on Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Washington Public Works Department, Environmental Services, Wastewater and Surface Water Management (the Division), which comprise the statements of net position as of December 31, 2013 and 2012, 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, 2013 and 2012, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 11 to the financial statements, the Division adopted the accounting requirements of Governmental Accounting Standards Board Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which resulted in the restatement of previously reported amounts for the year ended December 31, 2012. Our opinion is not modified with respect to this matter.

Other Matters***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis on pages 7 through 12 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The supplemental information presented on pages 43 through 49 are not a required part of the financial statements, but are supplemental information presented for the purposes of additional analysis. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and, accordingly, we express no opinion on it.



Tacoma, Washington
April 7, 2014

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Management's Discussion and Analysis

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Management's Discussion and Analysis
December 31, 2013 and 2012

Introduction

The following is management's discussion and analysis (MD&A) of the financial activities of the City of Tacoma's Wastewater and Surface Water Management Division (the Division) for the years ended December 31, 2013 and 2012. The MD&A is designed to focus on significant financial transactions and activities and to identify changes in financial position. This information should be read in conjunction with the financial statements taken as a whole. The financial statements are prepared on a full accrual basis of accounting.

Financial Highlights

- Total net position is \$386.4 million at December 31, 2013 compared to \$369.5 million and \$362.8 million at year-end 2012 and 2011, respectively. The change in net position is \$16.9 million in 2013, \$6.6 million in 2012 and \$7.7 million in 2011.
- Total assets and deferred outflows of resources are \$606.6 million, an increase of \$12.3 million in 2013 compared to \$594.2 million, a decrease of \$5.1 million in 2012.
- Liabilities and deferred inflows of resources are \$220.2 million, a decrease of \$4.6 million in 2013 compared to \$224.8 million, a decrease of \$11.8 million in 2012.

Financial Analysis – Condensed Statements of Net Position

	December 31,		
	2013	2012 (as restated)	2011 (as restated)
Current, restricted, and other assets	\$ 96,634,377	\$ 121,015,523	\$ 147,597,911
Capital assets	508,831,233	472,068,087	449,849,304
Deferred outflows of resources	1,098,362	1,159,666	1,918,773
Total assets and deferred outflows of resources	<u>\$ 606,563,972</u>	<u>\$ 594,243,276</u>	<u>\$ 599,365,988</u>
Current liabilities and liabilities payable from restricted assets	\$ 13,474,553	\$ 13,993,493	\$ 15,782,235
Noncurrent liabilities	181,730,999	185,762,831	198,243,680
Deferred inflows of resources	25,000,000	25,000,000	22,500,000
Total liabilities and deferred inflows of resources	<u>220,205,552</u>	<u>224,756,324</u>	<u>236,525,915</u>
Net investment in capital assets	379,249,919	345,790,613	324,655,577
Restricted for bond reserves	9,573,274	8,227,353	7,516,853
Unrestricted	(2,464,773)	15,468,986	30,667,643
Total net position	<u>386,358,420</u>	<u>369,486,952</u>	<u>362,840,073</u>
Total liabilities, deferred inflows of resources, and net position	<u>\$ 606,563,972</u>	<u>\$ 594,243,276</u>	<u>\$ 599,365,988</u>

Current, restricted, and other assets

Current, restricted, and other assets decreased \$24.4 million in 2013 and \$26.6 million in 2012. The primary reason for the 2013 decrease was a \$26.0 million decrease in cash due to increased spending on capital projects of \$39.5 million funded by \$7.5 million from the 2006 Sewer Revenue Bonds and \$32.0 million from cash generated from operating activities.

In 2012, cash decreased \$27.4 million due to calling \$11.0 million remaining on the 2002 Revenue Refunding Bonds in June 2012 and \$29.8 million spending on capital projects funded by \$12.7 million from the 2006 Sewer Revenue Bonds and \$17.1 million from operating cash.

Other changes in 2013 include a \$640,000 increase in grants receivable, mainly from the Washington State Department of Ecology for the Cheney Stadium project. Prepaid expenses increased \$460,000 due to prepaid rental expenses for a 10 year lease on the Cavanaugh Building for the Tagro operation.

Deferred outflows of resources

Deferred outflows of resources is a new caption in 2013 and includes unamortized refunding costs on the 2006 and 2011 revenue bonds. There is a \$61,000 decrease in 2013 and \$759,000 in 2012. The changes during the year are due to amortizing these costs.

Current liabilities and liabilities payable from restricted assets

Total current liabilities including those payables from restricted assets decreased \$519,000 in 2013 and \$1.8 million in 2012. The 2013 changes include a \$793,000 decrease in accounts payable, a \$288,000 decrease in environmental liabilities and a \$247,000 increase in due other funds. The environmental liabilities decreased primarily due to less anticipated clean-up costs related to the Thea Foss Waterway. The 2012 changes included a \$2.5 million decrease in revenue bonds principal payable and a \$234,000 increase in accrued wages due to an additional week of payroll accruals at year-end.

Noncurrent liabilities

Noncurrent liabilities decreased \$4.0 million in 2013 and \$12.5 million in 2012. The 2013 decrease was primarily due to payments on the State Revolving Funds (SRF) loans of \$3.5 million. The 2012 decrease was the result of calling the 2002 Revenue Refunding Bonds and payments on the SRF loans.

Deferred inflows of resources

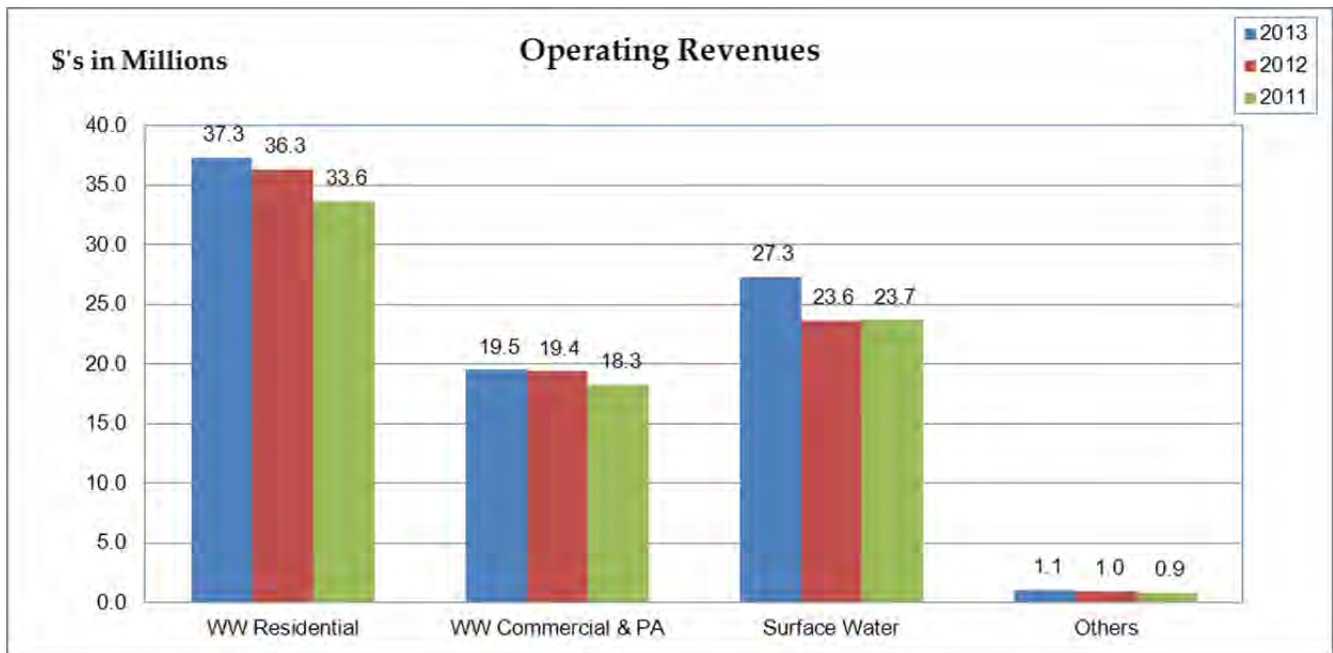
Deferred inflows of resources is a new caption in 2013 and includes rate stabilization credit. In 2012, \$2.5 million was transferred to the Rate Stabilization Fund in order to better match revenues with future expenses.

Financial Analysis - Condensed Statements of Revenues, Expenses and Changes in Net Position

	Year Ended December 31,		
	2013	2012 (as restated)	2011 (as restated)
Operating revenues	\$ 85,108,081	\$ 80,201,594	\$ 76,500,058
Operating expenses	68,772,885	68,125,720	63,859,726
Net operating income	16,335,196	12,075,874	12,640,332
Nonoperating revenues (expenses)	(5,201,731)	(4,285,494)	(3,596,910)
Income before contributions and transfers	11,133,465	7,790,380	9,043,422
Contributions	10,964,513	4,872,655	3,940,156
Transfers	1,688,834	682,025	1,060,608
Gross earnings taxes	(6,915,344)	(6,698,181)	(6,309,651)
Change in net position	16,871,468	6,646,879	7,734,535
Net position, as originally stated			
Effect of restatement			(549,900)
Net position - beginning as restated	369,486,952	362,840,073	355,655,438
Net position - ending	\$ 386,358,420	\$ 369,486,952	\$ 362,840,073

Operating revenues

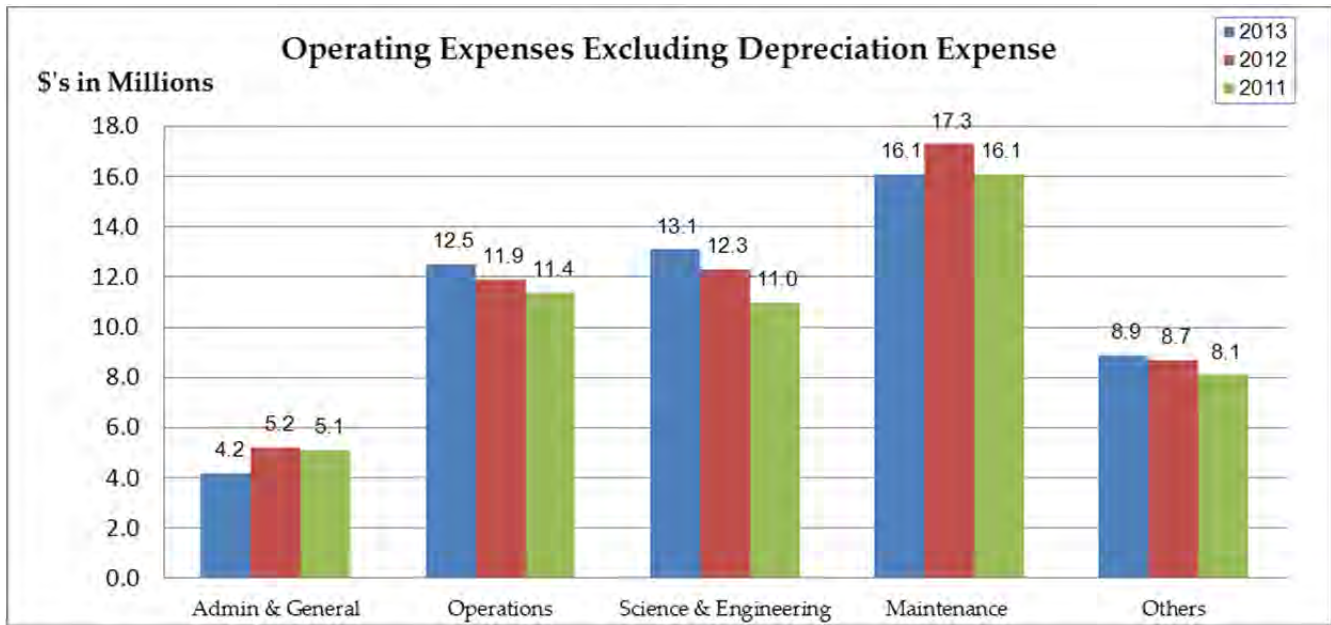
The following graph provides a comparison of operating revenues for the three years.



Operating revenues were \$85.1 million in 2013 compared to \$80.2 million in 2012 and \$76.5 million in 2011. However, the 2012 revenues before the transfer of \$2.5 million to the Rate Stabilization Fund totaled \$82.7 million. The table above reflects this change in the surface water revenues. The approved average revenue increase for Wastewater Management was 4.8% for each of the years 2013, 2012, and 2011, and for Surface Water Management was 6% for 2013 and 5.4% for each of the years 2012 and 2011. The 2013 rate increases went into effect March 1st instead of the usual January 1st resulting in less of an increase compared to the increases in 2012. In addition, wastewater residential revenues reflect the lower than planned average winter water usage as customers conserve more water.

Operating expenses

The graph below shows a three year comparison of operating expenses excluding depreciation.



2013 Activity

Operating expenses were \$68.8 million in 2013 and \$68.1 million in 2012, an increase of \$647,000.

- Administration and general costs decreased \$1.0 million (19%) primarily due to increased capitalized A&G credits of \$418,000 as a result of increased spending on capital projects and decreased bad debt expenses of \$450,000 due to reductions in older receivables. Capital lease payments decreased \$350,000 due to expensing the January 2013 payment in December 2012. There was an increase of \$174,000 in professional services resulting from the rate model and the capital management E-Builder software projects.
- Operation costs increased \$540,000 due to increased personnel related costs of \$360,000 and professional services for the Community Gardens Program.
- Science and engineering costs increased \$793,000 principally due to spending on expensed projects and more laboratory work performed for the Division.
- Maintenance costs decreased \$1.2 million primarily due to reduced material costs for maintenance and repairs as a result of the mild winter conditions, an absence of major line failures, and no major maintenance on pumps. There are capital pump replacement projects underway resulting in less maintenance expense.

2012 Activity

Operating expenses were \$68.1 million in 2012 and \$63.9 million in 2011, an increase of \$4.2 million.

- Operation costs increased \$484,000 over 2011 as a result of increased Pierce County wastewater treatment charges and a new rental cost for the Tagro Cavanaugh Building lease. Other increases include increased costs for the compensated absences accrual and chemical and gas purchased for water treatment and bio-solid dewatering.
- Science and engineering costs increased \$1.3 million (12%) mainly due to increased personnel related costs as a result of the increased number of full-time employees to 136 from 88 in 2011. The increase in staff resulted from the transfer in from the Public Works Department the Construction Division, which employed 27, and other staff to fill vacancies.
- Maintenance costs increased \$1.1 million as a result of more work performed on expense projects, including the Electronic Operation and Management manual project, than on capital projects compared to 2011. Other increases include increased costs of materials and parts used for Treatment Plant #1 upgrades and repairs and outside service contracts, including the Digester #5 painting.
- Other operating expenses increased \$673,000 mainly due to increased assessment charges from IT and Customer Service.

Nonoperating revenues (expenses)

Nonoperating revenues and expenses consist principally of investment income, rental income, operating grant revenues, and interest expense. Net expenses of \$5.2 million were reported in 2013, an increase of \$916,000 (21%) from the net expenses of \$4.3 million in 2012. Significant changes include:

- Investment income decreased \$1.9 million (89%) to \$237,000 from \$2.2 million in 2012: 1) the mark to market adjustment decreased investment revenue by \$457,000, and 2) the investment earnings were \$1.5 million lower because of the reduced cash balance due to increased spending on capital projects.
- There is no operating grant revenue in 2013 compared to \$332,000 in 2012.
- Revenue bond related costs decreased \$889,000 due to calling the 2002 Revenue Refunding Bonds in 2012.
- Other nonoperating expenses decreased \$414,000 due to decreased losses on disposal of assets.

Contributions

The Division recorded \$1.0 million of donated lines in 2013 compared to \$3.6 million in 2012 and \$3.4 million in 2011. Transfers from the City's General Fund account for \$8.4 million for land designated as "Open Space" recorded as contributions.

Transfers

Capital related transfers were \$1.9 million; \$1.5 million from Public Works for the Pacific Avenue Streetscape Project and \$314,000 from Public Assembly Facilities for land designated as "Open Space". Operating related transfers out of \$168,000 were for radio replacements compared to the transfers in from other funds of \$682,000 in 2012 for radio and public liability assessments.

Capital Assets

Capital assets increased \$36.8 million compared to \$22.2 million in 2012. (See Note 3.)

2013 Activity

Capital assets increased \$36.8 million over the prior year. Land increased \$8.9 million mainly due to recording "Open Space" land transferred to Surface Water. Machinery and equipment increased \$10.1 million primarily due to the capitalization of the Lincoln & Marine View Drive Pump Station and High Purity Oxygen Generation Facility projects. Transmission lines and other improvements increased \$27.5 million: 4,146 feet of donated lines were recorded for \$1.0 million, 66,452 feet of old lines were retired at the historical cost of \$255,000, and 76,156 feet of new replacement lines and extended sewer lines were recorded for \$18.7 million. Other improvements include the Pacific Avenue Streetscape Project recorded for the value of \$4.0 million of which \$1.5 million was grant funded. Accumulated depreciation increased \$13.8 million and construction in progress increased \$3.4 million.

2012 Activity

Capital assets increased \$22.2 million over the prior year. Buildings increased \$4.4 million mainly due to the capitalization of the Eductor Decant Facility. Machinery and equipment increased \$5.9 million due to the capitalization of the Salmon Beach Lower Pump for \$2.9 million and various purchases of equipment and vehicles. Transmission lines increased \$20.7 million: 13,800 feet of donated lines were recorded at \$3.6 million and 37,963 feet of old pipe lines were retired at historical cost of \$146,000 and replaced with 67,500 feet of new and extended sewer lines for \$17.1 million. Accumulated depreciation increased \$12.5 million and construction in progress increased \$3.4 million.

Debt Administration

At December 31, 2013, the Division had \$152.7 million outstanding in long-term debt: \$59.2 million of this is junior lien debt consisting of SRF loans and \$93.5 million is senior parity bond debt. This compares to \$156.6 million in 2012 and \$171.5 million in 2011. The rating agencies maintained the Division's underlying credit ratings on parity bonds of Aa2, AA+, and AA+ from Moody's, Standard & Poor's, and Fitch respectively.

Debt Service Coverage

The bond coverage ratio is calculated by dividing net revenue by debt service as defined by bond covenants. The SRF loans are junior lien debt and excluded from the debt service in the bond coverage ratio calculation. However, 100% of the capital lease obligation on the Urban Waters building was included as parity debt although 20% is expected to be received from the Solid Waste Division.

The bond coverage ratio is 4.46 at the end of 2013 from a ratio of 2.75 at the end of 2012 and 2.94 at the end of 2011. A bond coverage ratio of 1.3 is required by bond covenants for the Division.

Summary

This Management Discussion and Analysis should be read in conjunction with the accompanying financial statements and notes. This report is prepared by our Financial Services Team. Moss Adams LLP independently audited the financial statements and notes. Environmental Services and Finance are jointly responsible for the information contained in this report, including the financial statements and notes.

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Financial Statements

**City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Net Position**

	December 31,	
	2013	2012 (as restated)
ASSETS		
Current assets:		
Cash and equity in pooled investments:		
Operating Fund	\$ 35,770,595	\$ 55,606,656
Rate Stabilization Fund	25,000,000	25,000,000
Total cash and equity in pooled investments	60,770,595	80,606,656
Accounts receivable	9,630,374	9,426,226
Allowance for uncollectible accounts	(4,355,891)	(4,178,448)
Unbilled revenue	5,900,000	5,610,000
Due from other funds	108,426	15,259
Inventory	894,085	856,445
Prepaid expenses	573,806	113,475
Grants receivable	1,086,120	446,390
Notes and contracts receivable	174,063	158,776
Total current assets	74,781,578	93,054,779
Restricted cash and equity in pooled investments:		
Bond reserve and debt service accounts	9,938,025	8,592,104
Customer deposits - detention ponds	104,678	110,262
Construction accounts	8,293,031	15,789,446
Total restricted cash and equity in pooled investments	18,335,734	24,491,812
Capital assets:		
Land and easements	19,255,327	10,321,617
Buildings	151,293,170	151,378,623
Buildings - capital lease	30,272,000	30,272,000
Machinery and equipment	152,561,487	142,498,431
Transmission lines and other improvements	333,647,503	306,140,187
Computer software	7,831,714	7,165,274
Less: accumulated depreciation	(207,463,950)	(193,705,228)
Assets in service, net of accumulated depreciation	487,397,251	454,070,904
Construction in progress	21,433,982	17,997,183
Total capital assets	508,831,233	472,068,087
Other noncurrent assets	3,517,065	3,468,932
Total assets	605,465,610	593,083,610
DEFERRED OUTFLOWS OF RESOURCES		
Unamortized bond refunding costs	1,098,362	1,159,666
Total deferred outflows of resources	1,098,362	1,159,666
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	\$ 606,563,972	\$ 594,243,276

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

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Net Position

	December 31,	
	2013	2012 (as restated)
LIABILITIES		
Current liabilities:		
Accounts payable	\$ 3,624,854	\$ 4,417,408
Accrued wages payable and compensated absences	1,545,050	1,329,062
Accrued taxes payable	689,760	648,165
Due other funds	1,320,027	1,072,811
Due other governmental units	490,971	510,233
Unearned revenue	187,889	179,057
State Revolving Loan interest payable	269,220	285,128
Current portion of long-term debt		
- State Revolving Loans	3,596,773	3,532,270
Current portion of capital lease obligation	602,000	578,000
Environmental liabilities	678,580	966,346
Total current liabilities	13,005,124	13,518,480
Current liabilities payable from restricted assets:		
Deposit payable - detention ponds	104,678	110,262
Bond interest payable	364,751	364,751
Total current liabilities payable from restricted assets	469,429	475,013
Noncurrent liabilities:		
Long-term debt - revenue bonds	93,502,552	93,821,885
Long-term debt - State Revolving Loans	55,632,692	59,229,464
Capital lease obligation	27,444,000	28,046,000
Compensated absences	2,684,113	2,444,362
Net OPEB obligation	1,967,642	1,671,120
Environmental liabilities	500,000	550,000
Total noncurrent liabilities	181,730,999	185,762,831
Total liabilities	195,205,552	199,756,324
DEFERRED INFLOWS OF RESOURCES		
Rate stabilization	25,000,000	25,000,000
Total deferred inflows of resources	25,000,000	25,000,000
NET POSITION		
Net investment in capital assets	379,249,919	345,790,613
Restricted for bond reserves	9,573,274	8,227,353
Unrestricted	(2,464,773)	15,468,986
Total net position	386,358,420	369,486,952
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND NET POSITION		
	\$ 606,563,972	\$ 594,243,276

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

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Revenues, Expenses, and Changes in Net Position

	Year Ended December 31,	
	2013	2012 (as restated)
OPERATING REVENUES		
Wastewater residential	\$ 37,259,592	\$ 36,262,815
Wastewater commercial and public authorities	19,466,323	19,386,726
Surface Water	27,331,797	23,562,104
Other revenues	1,050,369	989,949
Total operating revenues	<u>85,108,081</u>	<u>80,201,594</u>
OPERATING EXPENSES		
Administration and general	4,214,786	5,235,291
Operations detail:		
Customer service	862,430	851,483
Plant #1	5,736,608	5,476,073
Wastewater treatment by other	2,370,876	2,207,265
Plant #3	901,610	1,037,447
Biosolids (Tagro)	2,593,671	2,352,692
Operations	<u>12,465,195</u>	<u>11,924,960</u>
Science & engineering detail:		
Engineering	6,059,530	5,958,679
Construction support	782,840	797,218
Laboratory	1,965,436	2,007,966
Environmental Compliance	3,513,436	3,315,126
Private development	51,029	42,655
Natural Resource Damage Consent Decree (NRDA)	48,268	16,827
Detention Ponds	6,657	25,811
Expense construction	666,837	137,054
Science & engineering	<u>13,094,033</u>	<u>12,301,336</u>
Maintenance detail:		
Pumping	1,928,577	2,225,449
Transmission	7,818,498	8,041,286
Plant #1	4,946,791	5,517,146
Parts	111,757	308,572
Administration	460,081	480,156
Plant #3	611,665	485,968
Holding basins	9,311	34,078
Biosolids (Tagro)	206,990	173,948
Maintenance	<u>16,093,670</u>	<u>17,266,603</u>
Total divisional operating expenses	<u>45,867,684</u>	<u>46,728,190</u>

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

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Revenues, Expenses, and Changes in Net Position

	Year Ended December 31,	
	2013	2012 (as restated)
OPERATING EXPENSES (Continued)		
Other expenses detail:		
Insurance	\$ 452,258	\$ 425,628
Taxes	1,447,144	1,498,450
IT services	3,199,112	3,001,590
Customer service	3,825,873	3,797,599
Other	8,924,387	8,723,267
Depreciation	13,980,814	12,674,263
Total operating expenses	68,772,885	68,125,720
Net operating income	16,335,196	12,075,874
NONOPERATING REVENUES (EXPENSES)		
Investment income	237,027	2,160,833
Rental income	382,151	375,391
Operating grant revenue	-	331,870
Bond interest expense, net of capitalized interest	(3,225,467)	(3,562,670)
Interest on long-term debt - State Revolving Loans	(1,121,650)	(1,185,215)
Interest on capital lease	(1,508,988)	(1,531,292)
Amortization of premium, discount, and refunding costs	258,029	(294,000)
Other nonoperating revenues	144,848	201,075
Other nonoperating expenses	(367,681)	(781,486)
Total nonoperating expenses	(5,201,731)	(4,285,494)
CHANGE IN NET POSITION		
Net position before capital contributions and transfers	11,133,465	7,790,380
Contributions:		
Cash	106,657	27,158
Capital related grants	1,242,302	1,082,398
Donated fixed assets	9,615,554	3,763,099
Transfers capital related	1,856,869	-
Transfers operating related	(168,035)	682,025
Transfers - gross earnings taxes	(6,915,344)	(6,698,181)
CHANGE IN NET POSITION	16,871,468	6,646,879
NET POSITION, AS ORIGINALLY STATED		363,621,979
EFFECT OF RESTATEMENT		(781,906)
NET POSITION - BEGINNING AS RESTATED	369,486,952	362,840,073
NET POSITION - ENDING	\$ 386,358,420	\$ 369,486,952

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

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Cash Flows

	Year Ended December 31,	
	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	\$ 84,390,428	\$ 80,498,342
Payments to suppliers	(25,252,908)	(24,034,126)
Payments to employees	(28,611,590)	(27,720,786)
Taxes paid	(1,435,574)	(1,475,146)
Net cash from operating activities	<u>29,090,356</u>	<u>27,268,284</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Gross earning taxes paid	(6,885,318)	(6,671,263)
Debt service related to environmental cleanup	(1,915,194)	(1,915,194)
Operating grants received	580	677,894
Transfers	(168,035)	682,025
Net cash from noncapital financing activities	<u>(8,967,967)</u>	<u>(7,226,538)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets	(38,788,292)	(30,805,346)
Principal payments on revenue bonds	-	(10,965,000)
Principal payments on State Revolving Loans	(3,532,269)	(3,469,009)
Capital lease obligation	(2,086,988)	(2,088,961)
Interest expense, net of capitalized interest	(2,447,908)	(2,904,827)
Net cash from capital and related financing activities	<u>(46,855,457)</u>	<u>(50,233,143)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment income	237,027	2,160,833
Rental income	382,151	375,391
Other investing proceeds	121,751	201,075
Net cash from investing activities	<u>740,929</u>	<u>2,737,299</u>
Net change in cash and equity in pooled investments	(25,992,139)	(27,454,098)
Cash and equity in pooled investments - beginning	105,098,468	132,552,566
Cash and equity in pooled investments - ending	<u>\$ 79,106,329</u>	<u>\$ 105,098,468</u>

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

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Cash Flows

	Year Ended December 31,	
	2013	2012
Reconciliation of cash and equity in pooled investments to balance sheets:		
Operating funds	\$ 60,770,595	\$ 80,606,656
Restricted funds	18,335,734	24,491,812
	\$ 79,106,329	\$ 105,098,468
Reconciliation of operating income to net cash from operating activities:		
Operating income	\$ 16,335,196	\$ 12,075,874
Adjustments to reconcile operating income to net cash from operating activities:		
Depreciation expense	13,980,814	12,674,263
Low income assistance	(119,105)	(73,922)
Change in assets, liabilities, and deferred inflows of resources:		
Accounts receivable, net of allowance	(26,705)	104,631
Unbilled revenue	(290,000)	(1,510,000)
Notes and contract receivable	(63,420)	(8,891)
Due from other funds	(93,167)	110,444
Due from other governmental units	-	17,000
Inventory	(37,640)	168,597
Prepaid expenses	(460,331)	(13,190)
Accounts payable	(792,553)	129,301
Accrued wages and compensated absences	455,739	876,895
Accrued taxes payable	11,570	24,048
Deposits payable	(5,584)	(24,488)
Due other funds	247,216	(16,210)
Due other governmental units	(19,262)	4,012
Unearned revenue	8,832	11,310
Rate stabilization	-	2,500,000
Environmental liability	(337,766)	(100,000)
Net OPEB obligation	296,522	318,610
Total adjustments	12,755,160	15,192,410
	\$ 29,090,356	\$ 27,268,284
Significant non-cash transactions:		
Capital and Related Financing Activities		
Donated fixed assets	\$ 9,615,554	\$ 3,763,099
Transfers capital related	1,856,869	-
	\$ 11,472,423	3,763,099

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

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Notes to Financial Statements

City of Tacoma, Washington
Environmental Services Department
Wastewater & Surface Water Management
Notes to Financial Statements
Years Ended December 31, 2013 and 2012

NOTE 1 OPERATIONS

OPERATIONS OF THE WASTEWATER AND SURFACE WATER MANAGEMENT DIVISION - The Wastewater and Surface Water Management Division (the Division) is presented as an enterprise fund within the Environmental Services Department under the provisions of the City of Tacoma's (the City) Charter and is included in the City's Comprehensive Annual Financial Report.

The Division is responsible for the planning, design, construction, operation, and maintenance of the wastewater and surface water facilities owned by the City. In addition to providing wastewater service within the City, the Division provides sewage treatment and disposal services by contract to the towns of Fife, Ruston, and Fircrest, and portions of Pierce County.

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 gross earnings tax to the City. These transactions are required to be arms-length transactions by law.

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 March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities* effective for financial statements periods beginning after December 15, 2012. This statement provides guidance for reclassifying certain items as deferred outflows of resources or deferred inflows of resources and further requires reclassification of certain items previously recorded as assets and liabilities to be presented as expenses or revenues. The Division adopted this new pronouncement in the current year and has restated amounts of effected items within the financial statements as of December 31, 2012. The specific accounts impacted by the restatement are detailed in Note 11.

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.

Wastewater & Surface Water Management 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 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 TIP in the Washington 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 TIP held in qualified public depositories at December 31, 2013 and 2012 is entirely covered by the Federal Deposit Insurance Corporation (FDIC) and the Washington State Public Deposit Protection Commission (PDPC).

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's Investment Policy allows for authorized investments up to 60 months to maturity. One method 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. The minimum legal requirement is AAA for bankers acceptance notes, and fixed rate callable and non-callable agency securities, and A for fixed rate non-callable municipal securities. The Bank Certificates of Deposit (CD) and Demand Deposit Accounts (DDA) are protected by the FDIC insurance up to \$250,000. All CD and DDA deposits not covered by FDIC are covered by the Washington State PDPC. The PDPC is a statutory authority established under the Revised Code of Washington (RCW) 39.58. The State Treasurers LGIP is authorized by RCW 43.250 and operates like a 2A7 fund and is collateralized by short term legal investments. Detailed disclosure information is available in the City of Tacoma's CAFR.

Concentration risk disclosure is required for all investments in a single issuer that is 5% or more of the total of the City's investments. Detailed disclosure information is available in the City of Tacoma's CAFR.

Custodial credit risk is the risk of unauthorized transactions by the custodian of investments. The City policy states that all security transactions will be settled "delivery versus payment" by the City's safekeeping bank.

ACCOUNTS RECEIVABLE AND UNBILLED REVENUE - 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 UNCOLLECTIBLE 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.

Wastewater & Surface Water Management Notes to Financial Statements Continued

INTERFUND AND INTERGOVERNMENTAL TRANSACTIONS - Unsettled transactions between entities at year end are recorded as due to or due from either other funds or other governmental units as appropriate.

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

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

BOND PREMIUM AND REFUNDING COSTS - Bond premium is amortized over the life of the bonds using the weighted average of the bonds outstanding. Bond refunding costs are amortized on a straight-line basis over the applicable bond period.

CAPITAL ASSETS AND DEPRECIATION - Capital assets consist of utility plant and are stated at original cost, which includes both direct costs of construction or acquisition and indirect costs. The cost of capital assets contributed is recorded at donated fair value. The cost of maintenance and repairs is charged to expense as incurred while the costs of improvements, additions and major renewals that extend the life of an asset are capitalized.

Assets are capitalized when costs exceed \$5,000 and the useful life exceeds one year.

Depreciation is recorded using the straight-line method based upon estimated useful lives of the assets. The original cost of property together with removal cost, less salvage, is charged to accumulated depreciation at such time as property is retired and removed from service.

The estimated useful lives range as follows:

	Years
Collection and Transmission Mains	75
Structures and Improvements	50
Land Improvements	25
Intangible Plant	7 - 20
Equipment	3 - 20

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.

Wastewater & Surface Water Management Notes to Financial Statements Continued

CONTRIBUTED CAPITAL - Capital grants and contributed capital assets are recorded as capital contributions.

COMPENSATED ABSENCES - The City has two different policies for compensated absences. The City's original policy allows employees to accrue vacation based on the number of years worked with a maximum accrual equal to the amount earned in a two-year period. These employees also accrue one day of sick leave per month without any ceiling on the maximum accrued. The City implemented a new policy in 1998 allowing employees to earn PTO (personal time off) without distinction between vacation and sick leave. Employees who worked for the City prior to the change could choose to stay with the original policy or opt to convert to the new policy.

The amount of PTO earned is based on years of service. The maximum accrual for PTO is 960 hours, and upon termination, employees are entitled to compensation for unused PTO at 100%. The liability and expense for accumulated unused PTO is adjusted each year based on each employee's current compensation level.

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 for earned vacation is computed at 100% and earned sick leave is computed at 10%, which is considered the amount vested. The liability and expense for accumulated unused vacation and sick leave is adjusted each year based on each employee's current compensation level.

Liability and expense for compensated absences are recorded including 100% of compensated time earned based on each employee's current compensation level.

RATE STABILIZATION FUND - The Division has established a rate stabilization account to better match revenues and expenses which may reduce volatility in rates. Amounts deposited into the account are excluded from the Statement of Revenues, Expenses and Changes in Net Position in accordance with regulated operations. Revenue will be recognized in subsequent periods when it is withdrawn in accordance with rate decisions.

OPERATING REVENUES - Revenues are derived from providing wastewater and surface water services. Wastewater services include the collection and treatment of wastewater to produce clean water and biosolids that are then used to produce TAGRO, planting soil amendments. Wastewater rates are based on volume of flow and strength. Total suspended solids (TSS) and biological oxygen demand (BOD) are strength determinants. Customers are billed on bi-monthly or monthly billing cycles.

Surface water services include flooding and erosion control, pollution prevention and control, environmental cleanup and restoration, and street drainage. Surface water rates are based on the area of the parcels and level of development with reductions for direct discharge and approved detention systems.

The rate structure is designed to meet the Division's needs and obligations on a cost-of-service basis while adhering to legal requirements. These legal requirements include computing rates on a reasonable basis, charging rates uniformly within classes, and using the revenues for utility and regulatory purposes. In addition, there may be laws imposed by the State, City Charter or to meet grant or bond requirements.

Wastewater & Surface Water Management Notes to Financial Statements Continued

The City has a parity bond ordinance that it will establish, maintain and collect rates or charges in connection with the ownership and operation of the utility that will be fair and nondiscriminatory and adequate to provide gross revenues sufficient for 1) the payment of the principal and interest on all parity bonds and all amounts that the City is obligated to set aside in the bond fund, 2) the proper operation and maintenance of the utility, 3) the payment of any and all amounts that the City may now or hereafter become obligated to pay from gross revenues.

NON-OPERATING REVENUES AND EXPENSES – The Division reports transactions not directly related to primary services as non-operating revenues and expenses. Significant items include investment and rental income and interest expense.

TAXES - The City charges the Division a gross earnings tax at the rate of 8.0%. In addition, the Division pays a 3.852% public utility tax to the State on wastewater collection revenues and the 1.5% business and occupation tax, which was changed from 1.8% effective July 1, 2013, to the State on wastewater transmission and treatment and surface water service revenues. The Division is exempt from payment of federal income tax.

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

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

Restricted for bond reserves are restricted when constraints placed on 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 are not “net investment in capital assets” or “restricted for bond reserves”.

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

ENVIRONMENTAL REMEDIATION COSTS - The Division recognizes environmental obligations and accruals for expected pollution remediation outlays which are recorded when one of the five obligating events occurs and are adjusted as further information develops or circumstances change.

The five obligating events are applied when the Division is: 1) compelled to take action because of an imminent endangerment, 2) the Division is in violation of a pollution prevention-related permit or license, 3) the Division is named or evidence indicates that it will be named by a regulator as a responsible party or potentially responsible party, 4) named in a lawsuit to compel participation in pollution remediation or 5) the Division commences or legally obligates itself to commence pollution remediation.

Costs related to environmental remediation are charged to operating expense when the liability is recognized; outlays are capitalized when goods and services are acquired under specific circumstances. Measurement is based on the current value of the outlays for the individual remediation components using the expected cash flow technique, adjusted for recoveries from other parties and insurance.

Wastewater & Surface Water Management Notes to Financial Statements Continued

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

USE OF ESTIMATES - The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. The Division used estimates in determining reported unbilled revenues, allowance for doubtful accounts, accrued compensated absences, depreciation, Other Post Employment Benefits (OPEB), 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, weather and natural disaster-related disruptions, collective bargaining labor disputes, Environmental Protection Agency regulations, federal government regulations or orders concerning the operation, maintenance and/or licensing of facilities.

RECLASSIFICATIONS - Changes have been made to prior year account classifications as needed to conform to the current year presentation format. (See Note 11.)

NOTE 3 CAPITAL ASSETS

A summary of the balances and changes in capital assets for 2013 and 2012 follows:

	2012	Additions	Retirements	Transfers	2013
Nondepreciable:					
Land and easements	\$ 10,321,617	\$ 8,933,710	\$ -	\$ -	\$ 19,255,327
Depreciable:					
Buildings	151,378,623	165,165	(250,618)	-	151,293,170
Buildings - capital lease	30,272,000	-	-	-	30,272,000
Machinery and equipment	142,498,431	-	-	10,063,056	152,561,487
Transmission lines and other improvements	306,140,187	1,421,993	(254,736)	26,340,059	333,647,503
Computer software	7,165,274	666,440	-	-	7,831,714
Assets in service	647,776,132	11,187,308	(505,354)	36,403,115	694,861,201
Accumulated depreciation	(193,705,228)	(14,002,662)	243,940	-	(207,463,950)
Assets in service, net	454,070,904	(2,815,354)	(261,414)	36,403,115	487,397,251
Construction work in progress	17,997,183	39,839,914	-	(36,403,115)	21,433,982
Total capital assets	<u>\$ 472,068,087</u>	<u>\$ 37,024,560</u>	<u>\$ (261,414)</u>	<u>\$ -</u>	<u>\$ 508,831,233</u>

**Wastewater & Surface Water Management
Notes to Financial Statements Continued**

	2011	Additions	Retirements	Transfers	2012
Nondepreciable:					
Land and easements	\$ 10,116,383	\$ 159,178	\$ -	\$ 46,056	\$ 10,321,617
Depreciable:					
Buildings	146,998,199	-	(748,800)	5,129,224	151,378,623
Buildings - capital lease	30,272,000	-	-	-	30,272,000
Machinery and equipment	136,583,014	-	-	5,915,417	142,498,431
Transmission lines and other improvements	285,488,642	3,615,000	(161,692)	17,198,237	306,140,187
Computer software	7,058,551	-	-	106,723	7,165,274
Assets in service	616,516,789	3,774,178	(910,492)	28,395,656	647,776,132
Accumulated depreciation	(181,242,825)	(12,674,263)	211,860	-	(193,705,228)
Assets in service, net	435,273,964	(8,900,085)	(698,632)	28,395,656	454,070,904
Construction work in progress	14,575,340	31,586,115	-	(28,164,272)	17,997,183
Total capital assets	<u>\$ 449,849,304</u>	<u>\$ 22,686,030</u>	<u>\$ (698,632)</u>	<u>\$ 231,384</u>	<u>\$ 472,068,087</u>

NOTE 4 LONG-TERM DEBT

Long-term debt activity for the years ended December 31, 2013 and 2012 follows:

	2012	Payments	2013	Due within One Year
Revenue bonds	\$ 89,265,000	\$ -	\$ 89,265,000	\$ -
Plus: Unamortized premium	4,556,885	(319,333)	4,237,552	-
State Revolving Fund loans	62,761,734	(3,532,269)	59,229,465	3,596,773
Long-term debt	<u>\$ 156,583,619</u>	<u>\$ (3,851,602)</u>	<u>\$ 152,732,017</u>	<u>\$ 3,596,773</u>

	2011	Payments	2012	Due within One Year
Revenue bonds	\$ 100,230,000	\$ (10,965,000)	\$ 89,265,000	\$ -
Plus: Unamortized premium	5,021,992	(465,107)	4,556,885	-
State Revolving Fund loans	66,230,743	(3,469,009)	62,761,734	3,532,270
Long-term debt	<u>\$ 171,482,735</u>	<u>\$ (14,899,116)</u>	<u>\$ 156,583,619</u>	<u>\$ 3,532,270</u>

Wastewater & Surface Water Management Notes to Financial Statements Continued

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

	2013	2012
Parity bonds, senior lien:		
2006 Revenue & Refunding Bonds, with interest rates ranging from 4.5% to 5.125%, due in yearly installments of \$470,000 to \$6,890,000 between 2016 and 2036. Original par value \$55,000,000 with a call date of December 1, 2016. Purpose was to fund a portion of the capital improvement plan, refund certain maturities of the 2001 Series A bonds, and pay the costs of issuance.	\$ 54,950,000	\$ 54,950,000
2011 Refunding Bonds, with interest rates ranging from 4.00% to 5.00%, due in yearly installments of \$2,765,000 to \$4,205,000 between 2022 and 2031. Original par value \$34,315,000 with a call date of December 1, 2021. Purpose was to refund the 2001 Series A bonds and pay the costs of issuance.	34,315,000	34,315,000
Total parity bonds, senior lien	89,265,000	89,265,000
Junior lien debt:		
State Revolving Fund loans A & B, with an interest rate of 1.5% and 2.6%, respectively, due in semi annual installments of \$3,450,000 to \$4,500,000 through 2028; this debt is junior lien and is secured by net operating revenue. The original amount issued totaled \$75,178,000 to reimburse a portion of costs related to the Central Treatment Plant Upgrade project.	58,802,532	62,315,644
State Revolving Fund loan 2011, with an interest rate of 2.9% in semi-annual installments of \$16,017 through 2030; this debt is junior lien and is secured by net operating revenue. The original amount issued totaled \$473,806 to reimburse a portion of costs related to surface water line retrofit projects.	426,933	446,090
Total junior lien debt	59,229,465	62,761,734
Total outstanding debt	148,494,465	152,026,734
Less:		
Current portion	(3,596,773)	(3,532,270)
Current portion payable from restricted assets	-	-
Plus: Unamortized premium	4,237,552	4,556,885
Total long-term debt	\$ 149,135,244	\$ 153,051,349

**Wastewater & Surface Water Management
Notes to Financial Statements Continued**

Annual debt service requirement to maturity follows:

	Principal	Interest on Debt	Total Debt Service
2014	\$ 3,596,773	\$ 5,450,070	\$ 9,046,843
2015	3,662,544	5,384,298	9,046,842
2016	6,349,611	5,317,231	11,666,842
2017	6,548,001	5,117,842	11,665,843
2018	6,757,742	4,910,601	11,668,343
2019-2023	36,599,167	21,215,685	57,814,852
2024-2028	39,523,830	15,200,896	54,724,726
2029-3033	25,751,797	9,013,007	34,764,804
2034-2036	19,705,000	2,028,338	21,733,338
	<u>\$ 148,494,465</u>	<u>\$ 73,637,968</u>	<u>\$ 222,132,433</u>

The carrying amounts of the State Revolving Fund loans approximate the fair value since such loans are exclusive and have not market.

The Division's current underlying credit ratings are Aa2, AA+, and AA+ from Moody's, Standard and Poor's, and Fitch, respectively.

Defeased and outstanding bonds constitute a contingent liability of the Division only to the extent that cash and investments presently in the control of the refunding trustees are not sufficient to meet debt service requirements and therefore are excluded from the financial statements because the likelihood of additional funding requirements is considered remote. As of December 31, 2013, no bonds were defeased and outstanding.

The Division's revenue bonds are secured by net operating revenue and cash and equity in pooled investment balances in the bond construction, reserve, and debt service funds. The bonds are also subject to certain financial and non-financial covenants. Arbitrage calculations were prepared and no arbitrage was due in 2013 or 2012.

NOTE 5 CAPITAL LEASE

By Ordinance No. 27783 passed on January 20, 2009, the City approved a property agreement and project lease with TES Properties and issuance by TES Properties of \$37,840,000 aggregate principal amount of its Lease Revenue Bonds, 2009 (Bonds). TES Properties is a single purpose Washington nonprofit corporation and subordinate organization of NDC Housing and Economic Development Corporation. The Environmental Services Department determined the appropriate pro-rata share for the Environmental Services divisions to share in all revenue, costs and cash requirements based on usage of the Urban Waters building to be: Wastewater (43%), Surface Water (37%) and Solid Waste (20%).

Wastewater & Surface Water Management Notes to Financial Statements Continued

The three divisions have included their pro-rata share of the capital lease and lease obligation for the building in their respective financial statements. The building has a useful life of 50 years and the lease agreement is for 29 years which exactly matches the debt service schedule of the Bonds. The land on which the building was constructed has been transferred to TES Properties and reclassified on the divisions' statements of net position in other noncurrent assets. All assets revert to the City at the end of the lease.

The future payments of the lease obligation as of December 31, 2013 total \$65,251,869. The Division's portion of the future lease payments is presented in the following table:

Years	Capital Lease Payments
2014	\$ 2,087,865
2015	2,087,865
2016	2,086,905
2017	2,088,985
2018	2,089,945
2019-2023	10,439,165
2024-2028	10,443,425
2029-3033	10,439,490
2034-2038	10,437,850
	52,201,495
Less interest	24,105,495
Principal	\$ 28,096,000

The sub-lease agreements for the space in the Urban Waters building include agreements with two tenants: the University of Washington Tacoma (UWT) and the Puget Sound Partnership (PSP). Both are for ten year periods effective in 2010 with the possibility of five year extensions. The revenue are shared across the utilities on the same prorated basis as the building lease. The UWT agreement provides revenue of \$293,640 per year, adjusted annually for inflation, and the PSP agreement provides a total of \$1,615,000 in revenue spread over the ten year lease period.

NOTE 6 INSURANCE

The major risks to the Division are flooding, recontamination, 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.

The City of Tacoma has established a Self-insurance Fund (the Fund) to insure the Division and other divisions within the City for certain losses arising from personal and property damage claims by third parties. The Division participates in the City's self-insurance program for claims that arise during the normal course of business. Environmental and tax claims generally are paid for out of revenue of the Division and not from the Fund. The Division is required to make payments to the Fund to cover claims incurred by the Division and administrative expenses of the Fund. The Division's premium payments totaled \$211,399 for 2013 and 2012. The Division only recognizes expense for premium payments because the risk of loss transfers to the Fund.

Wastewater & Surface Water Management Notes to Financial Statements Continued

The City maintains an excess general liability policy with limits of \$15 million, subject to a self-insured retention of \$3 million and a \$30 million dollar aggregate. The City has an excess policy to cover extraordinary workers' compensation claims with Statutory Limits and with a \$1 million self-insured retention plus a \$250,000 of total loss each 12 month policy period. The City has a property insurance policy with a limit of \$500 million replacement cost (\$50,000 deductible per occurrence). The City carries property coverage with a maximum single occurrence limit of \$500,000,000 with a sublimit of \$150,000 deductible per occurrence, with exceptions. This policy renews July 1st of each year. The Division's cost for these policies \$240,859 in 2013 and \$214,230 in 2012.

NOTE 7 TACOMA EMPLOYEES' RETIREMENT SYSTEM (TERS OR THE SYSTEM)

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.

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 - The System is a cost-sharing multiple-employer, defined benefit retirement plan covering substantially all employees of the City of Tacoma, with the exception of police officers, firefighters, Tacoma Rail employees who are covered by state or federal retirement plans. Employees of the Tacoma-Pierce County Health Department, as well as certain employees of the Pierce Transit and the Law Enforcement Support Agency who established membership in the System when these agencies were still City of Tacoma departments, are also members. It is administered in accordance with RCW Chapter 41.28 and Chapter 1.30 of the Tacoma Municipal Code. There are 2,119 retirees and beneficiaries currently receiving benefits, 434 vested terminated members entitled to future benefits and 2,881 active members of the Tacoma Employees' Retirement System, as of December 31, 2013.

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 value policies. No investment in any one corporation or organization exceeded five percent of net assets 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 their beneficiaries. The System also provides death and disability retirement.

Wastewater & Surface Water Management Notes to Financial Statements Continued

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:

<u>Applicable Period</u>	<u>Employer Rate</u>	<u>Member Rate</u>	<u>Total Rate</u>
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

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, 2013, 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.

Schedule of Funding Progress (\$ in millions):

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (a)</u>	<u>Actuarial Accrued Liabililty (AAL) (b)</u>	<u>Unfunded AAL (UAAL) (c) = (b)-(a)</u>	<u>Funded Ratio (d) = (a) / (b)</u>	<u>Covered Payroll (e)</u>	<u>UAAL as of Percentage of Covered Payroll (f) = (c) / (e)</u>
1/1/2011	\$ 1,075	\$ 1,133	\$ 58	94.9%	\$ 220	26.5%
1/1/2012	\$ 1,068	\$ 1,186	\$ 117	90.1%	\$ 219	53.4%
1/1/2013	\$ 1,187	\$ 1,307	\$ 120	90.9%	\$ 211	56.7%

Both the City and employees made 100% of the required contributions. The City's required contributions for the years ended December 31st were:

2011	\$ 20,850,233
2012	\$ 20,919,787
2013	\$ 21,188,984

Wastewater & Surface Water Management Notes to Financial Statements Continued

ACTUARIAL METHODS AND SIGNIFICANT ACTUARIAL ASSUMPTIONS

Valuation Date	January 1, 2013
Actuarial Cost Method	Entry Age
Amortization Method	Level Percentage of the System's Projected Payroll
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	7.50%
Projected Salary Increases	4.00%
Includes Inflation at	3.00%
Postretirement Benefit Increases	2.125%

NOTE 8 OTHER POST EMPLOYMENT BENEFITS

PLAN DESCRIPTION - The City charges some early retirees not yet eligible for Medicare a health premium based on the claims experience of active employees and retirees rather than based on the claims experience of retirees only. This difference is a benefit to the retirees, since health claims costs generally increase with age. GAAP requires that the portion of age-adjusted expected retiree health claims costs that exceed the premium charged to retirees be recognized as a liability for accounting purposes. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and are subject to continual revision as results are compared to past expectation and new estimates are made about the future.

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

ANNUAL OPEB COST AND NET OPEB OBLIGATION - The Present Value of Benefits (PVB) is the present value of projected benefits discounted at the valuation interest rate (3.75%).

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

For inactive employees, the AAL is equal to the present value of benefits. For active employees, the actuarial present value of the projected benefits of each individual is allocated as a level percentage of expected salary for each year of employment between entry age (defined as age at hire) and assumed exit (until maximum retirement age). The portion attributed to service between entry age and the valuation date is the actuarial accrued liability.

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

The Annual Required Contribution (ARC) is the amount the City is required to report as an expense for the year 2013 under GASB 45. The ARC is equal to the Normal Cost plus an amount to amortize the Unfunded Actuarial Accrued Liability (UAAL) on a closed basis of 30 years, beginning January 1, 2007. The amortization period for 2013 is 24 years.

Wastewater & Surface Water Management Notes to Financial Statements Continued

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. The City has a Net OPEB Obligation as of December 31, 2013 as the City has not set aside funds for OPEB.

EXCISE TAX FOR HIGH COST OR “CADILLAC” HEALTH PLANS IN 2018 AND BEYOND – An excise tax for high cost health coverage or “Cadillac” health plans was included in the Affordable Care Act (ACA) passed into law in March 2010. The provision levies a 40% tax on the value of health plan costs that exceed certain thresholds for single coverage or family coverage. The 2018 annual thresholds for qualified retirees aged 55-64 are \$11,850 for single coverage and \$30,950 for a family plan. If, between 2010 and 2018, the cost of health care insurance rises more than 55%, the threshold for the excise tax will be adjusted.

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

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

SUMMARY OF CHANGES – As of January 1, 2011 (the date of the prior valuation), the AAL was \$248,571,791. The expected value as of January 1, 2013, based on the 2011 valuation, was \$260,708,000. The total AAL of \$251,839,846 was 3% lower than expected primarily due to lower than expected medical costs partially offset by the new excise tax for “Cadillac” health plans, demographic experience and assumptions, and economic assumptions.

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

	<u>January 1, 2011</u>	<u>January 1, 2013</u>
Total membership:		
Active employees	3,675	3,335
Terminated vested employees	363	394
Retired employees & Dependents	790	846
Total	<u>4,828</u>	<u>4,575</u>
Annual Benefit Payments	\$ 9,569,648	\$ 9,887,335
Discount rate	4.00%	3.75%
Present Value of Benefits	\$ 319,550,419	\$ 326,742,538
Actuarial Accrued Liability	\$ 248,571,791	\$ 251,839,846
Assets	\$ -	\$ -
Unfunded Actuarial Accrued Liability	<u>\$ 248,571,791</u>	<u>\$ 251,839,846</u>
Normal Cost	\$ 5,559,351	\$ 5,484,587
Annual Required Contribution	\$ 19,734,041	\$ 20,058,760

Wastewater & Surface Water Management Notes to Financial Statements Continued

The following table shows the total value of the benefits provided, the member paid premiums and the City paid benefits as of December 31, 2013.

Value of Subsidy at 3.75% Interest Rate	Total Value of Benefits	Member Paid Premiums	City Paid Benefits
Present Value of Benefits	\$ 488,143,650	\$ 161,401,112	\$ 326,742,538
Actuarial Accrued Liability	\$ 331,339,973	\$ 79,500,127	\$ 251,839,846
Normal Cost	\$ 11,227,919	\$ 5,743,332	\$ 5,484,587
Annual Benefit Payments	\$ 13,500,240	\$ 3,612,905	\$ 9,887,335

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, 2013.

	City	Division
Determination of Annual Required Contribution:		
Normal Cost at Year-end	\$ 5,484,587	\$ 308,092
Amortization of UAAL	14,574,173	114,129
Annual Required Contribution	<u>\$ 20,058,760</u>	<u>\$ 422,221</u>
Determination of Net OPEB Obligation:		
Annual Required Contribution	\$ 20,058,760	\$ 422,221
Interest on prior year Net OPEB Obligation	1,742,601	62,667
Adjustments to ARC	(2,272,594)	(67,720)
Annual OPEB Cost	<u>19,528,767</u>	<u>417,168</u>
Actual benefits paid	9,887,334	120,646
Increase in Net OPEB Obligation	9,641,433	296,522
Net OPEB Obligation - beginning of year	<u>46,469,368</u>	<u>1,671,120</u>
Net OPEB Obligation - end of year	<u>\$ 56,110,801</u>	<u>\$ 1,967,642</u>

FUNDED STATUS AND FUNDING PROGRESS -

The following table shows the annual OPEB cost and net OPEB obligation for three years. This table is based upon a 4.00% interest rate for 2011 and 2012 and 3.75% for 2013.

Year Ended	Annual OPEB Cost		Benefits Paid		Net OPEB Obligation	
	City	Division	City	Division	City	Division
12/31/2011	\$ 19,596,420	\$ 470,786	\$ 9,569,648	\$ 124,293	\$ 36,393,620	\$ 1,352,510
12/31/2012	\$ 19,469,178	\$ 469,633	\$ 9,393,431	\$ 151,023	\$ 46,469,368	\$ 1,671,120
12/31/2013	\$ 19,528,767	\$ 417,168	\$ 9,887,334	\$ 120,646	\$ 56,110,801	\$ 1,967,642

As of January 1, 2013, the most recent actuarial valuation date, the Plan was zero percent funded. Based upon a 3.75% interest rate, the actuarial accrued liability for benefits was \$251.8 million, and the actuarial value of assets was zero, resulting in an Unfunded Actuarial Accrued Liability of \$251.8 million.

Wastewater & Surface Water Management Notes to Financial Statements Continued

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

The portion of the actuarial present value allocated to a valuation year is called the normal cost. The portion of this actuarial present value not provided for at a valuation date by the sum of (a) the actuarial value of the assets, and (b) the actuarial present value of future normal costs is called the UAAL. In determining the ARC, the UAAL is amortized as a level percentage of expected payrolls for non-LEOFF 1 groups. For LEOFF 1, the UAAL is amortized as a level dollar amount. The amortization period was 30 years in 2007 and is now 24 years.

Actuarial Methods and Significant Actuarial Assumptions:

Valuation DateJanuary 1, 2013
 Census DateJanuary 1, 2013
 Actuarial Cost Method:Entry Age
 Amortization Method:Combination of level percentage and level dollar amount, see note above.
 Remaining Amortization Period:24 years, closed
 Demographic Assumptions:Demographic assumptions regarding retirement, disability, and turnover are based upon pension valuations for the various pension plans.

Actuarial Assumptions:

Discount Rate.....3.75% for pay-as-you-go funding
 Medical Cost Trend.....2013 8.9%
 2014 6.5%
 2015 5.8%
 2020 6.0%
 2030 5.9%
 2040 5.6%

The medical cost rate is assumed to continue grading downward until achieving the ultimate rate of 4.8% in 2083 and beyond. The first year trend reflects assumed increases based on ACA fees. These trend rates assume that, over time, deductibles and out-of-pocket maximums will be periodically increased as medical trends increase. The trends above do not reflect increases in costs due to the excise tax.

Economic Assumptions – Discount Rate (Liabilities).....3.75%

Wastewater & Surface Water Management Notes to Financial Statements Continued

Demographic Assumptions.....Eligibility:

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

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

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

NOTE 9 ENVIRONMENTAL LIABILITIES

COMMENCEMENT BAY NATURAL RESOURCE DAMAGES - The City has resolved federal, state, and tribal natural resource damage claims associated with municipal storm water discharges in Commencement Bay through a Consent Decree that became effective on December 30, 1997. The stated value of the City’s settlement is approximately \$7,700,000. Under the Consent Decree (the NRDA Consent Decree), the City agreed to undertake five restoration projects within the Commencement Bay watershed and make certain cash payments. The construction has been completed on four projects and the City made a payment to the Port of Tacoma of \$134,692 to construct the fifth project.

The City hopes to close out the Consent Decree in 2014. Ongoing monitoring and maintenance of the various projects will continue through 2014. Included in the financial statements for are liabilities of \$272,234 for 2013 and \$310,000 for 2012. Although the City resolved its NRDA liability, the City indemnified certain parties when it purchased real property along the Thea Foss Waterway in the late 1980’s and early 1990’s. The City expects that any financial obligation it may have related to these indemnities will be de minimus given the historical uses of the indemnified properties and the limited potential for releases from these properties to damage natural resources. The City’s understanding is a Thea Foss Waterway NRDA settlement between non-City parties and the Commencement Bay Natural Resource Trustees could be reached in 2014.

HYLEBOS WATERWAY CONSENT DECREE - In 2003 the City of Tacoma – General Government entered a Consent Decree settlement with EPA to resolve any liability it may have had for sediment contamination in the Hylebos Waterway. The majority of the City’s potential liability was attributed to municipal storm water discharges. Under the terms of its settlement, the City paid \$459,663 to “cash-out” its liability. This amount included a 50 percent premium, which obligated the City to pay a small percentage (i.e., 0.4397%) of any cost overruns if the remedial action work exceeded the project estimate of \$56,056,407 to complete such work. On January 11, 2012 the City was notified by the Hylebos Performing Party Group that the cost of the Hylebos Waterway remedial action project totaled \$110,991,511. This number has since been adjusted downward, setting the City’s share of cost overruns at \$233,029. The City also anticipates making an additional payment to the Hylebos Performing Party Group for around \$63,317, which would fully and finally resolve the City’s liability for any post-2012 costs overruns under its 2003 Hylebos Waterway Consent Decree settlement with EPA. The City recorded an expense and liability of \$306,346 as of December 31, 2013.

FOSS CONSENT DECREE – The City has an obligation under the Foss Consent Decree for continued monitoring until at least 2016. The results of this monitoring may result in additional cleanup efforts in the future. Obligations for future monitoring costs of \$600,000 in 2013 and \$900,000 in 2012 have been recognized in the financial statements as environmental liabilities.

Wastewater & Surface Water Management Notes to Financial Statements Continued

NOTE 10 COMMITMENTS AND CONTINGENCIES

LITIGATION AND CLAIMS - Because of the nature of its activities, the Division is subject to various pending and threatened legal actions which arise in the ordinary course of business. The Division believes, based on the information presently known, the ultimate liability for any legal actions, individually or in the aggregate, taking into account established accruals for estimated liabilities, will not be material to the financial position of the Division, but could be material to results of operations or cash flows for a particular annual period. No assurance can be given, however, as to the ultimate outcome with respect to any particular claim.

NOTE 11 RECLASSIFICATION AND RESTATEMENT OF PRIOR YEAR

ITEMS PREVIOUSLY REPORTED AS ASSETS AND LIABILITIES – The Division restated the 2012 financial statements and reclassified certain 2012 account balances to conform to the 2013 presentation in accordance with the GASB 65 pronouncement. The Division now presents sections titled Deferred Outflows of Resources and Deferred Inflows of Resources on its Statements of Net Position with the appropriate items reported. The Division expensed bond issuance costs previously deferred and amortized. The following table shows the restatement of the prior year:

	2012 As Reported	Reclassification	Accounting Restatement	2012 As Restated
Statements of net position:				
Assets				
Other noncurrent assets	\$ 5,333,065	\$ (1,159,666)	\$ (704,467)	\$ 3,468,932
Deferred outflows of resources				
Unamortized bond refunding costs	-	1,159,666	-	1,159,666
Net position				
Net investment in capital assets	346,183,615	-	(377,027)	345,806,588
Unrestricted	15,780,451	-	(327,440)	15,453,011
Current liabilities				
Rate stabilization	25,000,000	(25,000,000)	-	-
Deferred inflows of resources				
Rate stabilization	-	25,000,000	-	25,000,000
Statements of revenues, expenses, and changes in net position:				
Amortization of premium, discount, and refunding costs	(371,439)		77,439	(294,000)
Net position - beginning	363,621,979	-	(781,906)	362,840,073

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Unaudited Supplemental Information

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Net Position

	Wastewater		Surface Water	
	December 31,		December 31,	
	2013	2012 (as restated)	2013	2012 (as restated)
ASSETS				
Current assets:				
Cash and equity in pooled investments:				
Operating Fund	\$ 20,697,586	\$ 41,975,283	\$ 15,073,009	\$ 13,631,373
Rate Stabilization Fund	17,000,000	17,000,000	8,000,000	8,000,000
Total cash and equity in pooled investments	37,697,586	58,975,283	23,073,009	21,631,373
Accounts receivable	6,347,319	6,057,767	3,283,055	3,368,459
Allowance for uncollectible accounts	(2,444,929)	(2,279,264)	(1,910,962)	(1,899,184)
Unbilled revenue	3,750,000	3,772,000	2,150,000	1,838,000
Due from other funds	64,552	4,481	43,874	10,778
Inventory	894,085	856,445	-	-
Prepaid expenses	541,120	108,700	32,686	4,775
Grants receivable	-	23,097	1,086,120	423,293
Notes and contracts receivable	174,063	158,776	-	-
Total current assets	47,023,796	67,677,285	27,757,782	25,377,494
Restricted cash and equity in pooled investments:				
Bond reserve and debt service accounts	6,448,596	5,295,899	3,489,429	3,296,205
Customer deposits - detention ponds	-	-	104,678	110,262
Construction accounts	848,582	1,842,281	7,444,449	13,947,165
Total restricted cash and equity in pooled investments	7,297,178	7,138,180	11,038,556	17,353,632
Capital assets:				
Land and easements	7,488,228	7,398,663	11,767,099	2,922,954
Buildings	148,827,640	148,875,580	2,465,530	2,503,043
Buildings - capital lease	16,271,200	16,271,200	14,000,800	14,000,800
Machinery and equipment	148,005,835	137,950,376	4,555,652	4,548,055
Transmission lines and other improvements	188,175,061	172,989,966	145,472,442	133,150,221
Computer software	4,646,282	4,317,823	3,185,432	2,847,451
Less: accumulated depreciation	(168,441,556)	(158,031,097)	(39,022,394)	(35,674,131)
Assets in service, net of accumulated depreciation	344,972,690	329,772,511	142,424,561	124,298,393
Construction in progress	15,697,075	14,809,335	5,736,907	3,187,848
Total capital assets	360,669,765	344,581,846	148,161,468	127,486,241
Other noncurrent assets	2,246,011	2,197,878	1,271,054	1,271,054
Total assets	417,236,750	421,595,189	188,228,860	171,488,421
DEFERRED OUTFLOWS OF RESOURCES				
Unamortized bond refunding costs	327,852	346,151	770,510	813,515
Total deferred outflows of resources	327,852	346,151	770,510	813,515
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	\$ 417,564,602	\$ 421,941,340	\$ 188,999,370	\$ 172,301,936

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Net Position

	Wastewater		Surface Water	
	December 31,		December 31,	
	2013	2012 (as restated)	2013	2012 (as restated)
LIABILITIES				
Current liabilities:				
Accounts payable	\$ 1,972,677	\$ 3,911,894	\$ 1,652,177	\$ 505,514
Accrued wages payable and compensated absences	1,073,029	944,605	472,021	384,457
Accrued taxes payable	458,516	450,383	231,244	197,782
Due other funds	718,333	603,904	601,694	468,907
Due other governmental units	490,971	510,233	-	-
Unearned revenue	129,087	123,169	58,802	55,888
State Revolving Loan interest payable	269,220	285,128	-	-
Current portion of long-term debt				
- State Revolving Loans	3,577,053	3,513,113	19,720	19,157
Current portion of capital lease obligation	323,575	310,675	278,425	267,325
Environmental liabilities	-	-	678,580	966,346
Total current liabilities	<u>9,012,461</u>	<u>10,653,104</u>	<u>3,992,663</u>	<u>2,865,376</u>
Current liabilities payable from restricted assets:				
Deposit payable - detention ponds	-	-	104,678	110,262
Bond interest payable	122,880	122,880	241,871	241,871
Total current liabilities payable from restricted assets	<u>122,880</u>	<u>122,880</u>	<u>346,549</u>	<u>352,133</u>
Noncurrent liabilities:				
Long-term debt - revenue bonds	30,816,817	30,892,282	62,685,735	62,929,603
Long-term debt - State Revolving Loans	55,225,479	58,802,531	407,213	426,933
Capital lease obligation	14,751,150	15,074,725	12,692,850	12,971,275
Compensated absences	2,025,564	1,878,064	658,549	566,298
Net OPEB obligation	1,516,485	1,243,142	451,157	427,978
Environmental liabilities	-	-	500,000	550,000
Total noncurrent liabilities	<u>104,335,495</u>	<u>107,890,744</u>	<u>77,395,504</u>	<u>77,872,087</u>
Total liabilities	<u>113,470,836</u>	<u>118,666,728</u>	<u>81,734,716</u>	<u>81,089,596</u>
DEFERRED INFLOWS OF RESOURCES				
Rate stabilization	17,000,000	17,000,000	8,000,000	8,000,000
Total deferred inflows of resources	<u>17,000,000</u>	<u>17,000,000</u>	<u>8,000,000</u>	<u>8,000,000</u>
NET POSITION				
Net investment in capital assets	257,152,125	238,176,952	122,097,794	107,613,661
Restricted for bond reserves	6,325,716	5,173,019	3,247,558	3,054,334
Unrestricted	23,615,925	42,924,641	(26,080,698)	(27,455,655)
Total net position	<u>287,093,766</u>	<u>286,274,612</u>	<u>99,264,654</u>	<u>83,212,340</u>
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND NET POSITION	<u>\$ 417,564,602</u>	<u>\$ 421,941,340</u>	<u>\$ 188,999,370</u>	<u>\$ 172,301,936</u>

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Revenues, Expenses, and Changes in Net Position

	Wastewater		Surface Water	
	Year Ended December 31,		Year Ended December 31,	
	2013	2012	2013	2012
OPERATING REVENUES				
Wastewater residential	\$ 37,259,592	\$ 36,262,815	\$ -	\$ -
Wastewater commercial and public authorities	19,466,323	19,386,726	-	-
Surface Water	-	-	27,331,797	23,562,104
Other revenues	826,395	637,085	223,974	352,864
Total operating revenues	<u>57,552,310</u>	<u>56,286,626</u>	<u>27,555,771</u>	<u>23,914,968</u>
OPERATING EXPENSES				
Administration and general	2,763,162	2,923,891	1,451,624	2,311,400
Operations detail:				
Customer service	655,889	611,294	206,541	240,189
Plant #1	5,736,608	5,476,073	-	-
Wastewater treatment by other	2,370,876	2,207,265	-	-
Plant #3	901,610	1,037,447	-	-
Biosolids (Tagro)	2,593,671	2,352,692	-	-
Operations	<u>12,258,654</u>	<u>11,684,771</u>	<u>206,541</u>	<u>240,189</u>
Science & engineering detail:				
Engineering	2,348,048	2,784,606	3,711,482	3,174,073
Construction support	469,546	636,929	313,294	160,289
Laboratory	1,267,664	1,487,253	697,772	520,713
Environmental Compliance	1,372,807	1,590,938	2,140,629	1,724,188
Private development	-	-	51,029	42,655
Natural Resource Damage Consent Decree (NRDA)	-	-	48,268	16,827
Detention Ponds	-	-	6,657	25,811
Expense construction	366,898	-	299,939	137,054
Science & engineering	<u>5,824,963</u>	<u>6,499,726</u>	<u>7,269,070</u>	<u>5,801,610</u>
Maintenance detail:				
Pumping	1,676,856	1,864,055	251,721	361,394
Transmission	4,869,019	4,882,104	2,949,479	3,159,182
Plant #1	4,946,791	5,517,146	-	-
Parts	111,757	308,572	-	-
Administration	460,081	480,156	-	-
Plant #3	611,665	485,968	-	-
Holding basins	-	-	9,311	34,078
Biosolids (Tagro)	206,990	173,948	-	-
Maintenance	<u>12,883,159</u>	<u>13,711,949</u>	<u>3,210,511</u>	<u>3,554,654</u>
Total divisional operating expenses	<u>33,729,938</u>	<u>34,820,337</u>	<u>12,137,746</u>	<u>11,907,853</u>

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Revenues, Expenses, and Changes in Net Position

	Wastewater		Surface Water	
	Year Ended December 31,		Year Ended December 31,	
	2013	2012	2013	2012
OPERATING EXPENSES (Continued)				
Other expenses detail:				
Insurance	\$ 407,202	\$ 381,777	\$ 45,056	\$ 43,851
Taxes	1,040,616	1,099,509	406,528	398,941
IT services	2,065,618	1,844,253	1,133,494	1,157,337
Customer service	1,893,345	1,835,675	1,932,528	1,961,924
Other	5,406,781	5,161,214	3,517,606	3,562,053
Depreciation	10,558,559	9,925,613	3,422,255	2,748,650
Total operating expenses	<u>49,695,278</u>	<u>49,907,164</u>	<u>19,077,607</u>	<u>18,218,556</u>
Net operating income	<u>7,857,032</u>	<u>6,379,462</u>	<u>8,478,164</u>	<u>5,696,412</u>
NONOPERATING REVENUES (EXPENSES)				
Investment income	107,572	1,392,546	129,455	768,287
Rental income	205,406	201,772	176,745	173,619
Operating grant revenue	-	100,000	-	231,870
Bond interest expense, net of capitalized interest	(647,932)	(974,381)	(2,577,536)	(2,588,289)
Interest on long-term debt - State Revolving Loans	(1,108,773)	(1,171,792)	(12,876)	(13,423)
Interest on capital lease	(811,080)	(823,070)	(697,908)	(708,223)
Amortization of premium, discount, and refunding costs	57,166	(570,422)	200,863	276,422
Other nonoperating revenues	144,382	70,355	466	130,720
Other nonoperating expenses	(294,845)	(452,698)	(72,836)	(328,787)
Total nonoperating expenses	<u>(2,348,104)</u>	<u>(2,227,690)</u>	<u>(2,853,627)</u>	<u>(2,057,804)</u>
CHANGE IN NET POSITION				
Net position before capital contributions and transfers	5,508,928	4,151,772	5,624,537	3,638,608
Contributions:				
Cash	-	1,347	106,657	25,811
Capital related grants	-	-	1,242,302	1,082,398
Donated fixed assets	145,725	1,423,037	9,469,829	2,340,062
Transfers capital related	(2,000)	-	1,858,869	-
Transfers operating related	(118,781)	507,353	(49,254)	174,672
Transfers - gross earnings taxes	(4,714,718)	(4,572,794)	(2,200,626)	(2,125,387)
CHANGE IN NET POSITION	<u>819,154</u>	<u>1,510,715</u>	<u>16,052,314</u>	<u>5,136,164</u>
NET POSITION, AS ORIGINALLY STATED		285,016,581		78,605,398
EFFECT OF RESTATEMENT		(252,684)		(529,222)
NET POSITION - BEGINNING AS RESTATED	<u>286,274,612</u>	<u>284,763,897</u>	<u>83,212,340</u>	<u>78,076,176</u>
NET POSITION - ENDING	<u>\$ 287,093,766</u>	<u>\$ 286,274,612</u>	<u>\$ 99,264,654</u>	<u>\$ 83,212,340</u>

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Cash Flows

	Wastewater		Surface Water	
	Year Ended December 31,		Year Ended December 31,	
	2013	2012	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES				
Receipts from customers	\$ 57,135,187	\$ 54,989,715	\$ 27,255,241	\$ 25,508,627
Payments to suppliers	(19,261,435)	(16,945,489)	(5,991,473)	(7,088,637)
Payments to employees	(20,482,002)	(20,007,400)	(8,129,588)	(7,713,386)
Taxes paid	(1,049,562)	(1,074,213)	(386,012)	(400,933)
Net cash from operating activities	<u>16,342,188</u>	<u>16,962,613</u>	<u>12,748,168</u>	<u>10,305,671</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Gross earning taxes paid	(4,697,638)	(4,531,543)	(2,187,680)	(2,139,720)
Debt service related to environmental cleanup	-	-	(1,915,194)	(1,915,194)
Operating grants received	-	100,000	580	577,894
Transfers	(118,781)	507,353	(49,254)	174,672
Net cash from noncapital financing activities	<u>(4,816,419)</u>	<u>(3,924,190)</u>	<u>(4,151,548)</u>	<u>(3,302,348)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Acquisition and construction of capital assets	(26,671,217)	(23,199,973)	(12,117,075)	(7,605,373)
Principal payments on revenue bonds	-	(7,675,500)	-	(3,289,500)
Principal payments on State Revolving Loans	(3,513,112)	(3,450,399)	(19,157)	(18,610)
Capital lease obligation	(1,121,755)	(1,122,815)	(965,233)	(966,146)
Interest expense, net of capitalized interest	(1,772,647)	(2,188,787)	(675,261)	(716,040)
Net cash from capital and related financing activities	<u>(33,078,731)</u>	<u>(37,637,474)</u>	<u>(13,776,726)</u>	<u>(12,595,669)</u>
CASH FLOWS FROM INVESTING ACTIVITIES				
Investment income	107,572	1,392,548	129,455	768,285
Rental income	205,406	201,772	176,745	173,619
Other investing proceeds	121,285	70,353	466	130,722
Net cash from investing activities	<u>434,263</u>	<u>1,664,673</u>	<u>306,666</u>	<u>1,072,626</u>
Net change in cash and equity in pooled investments	<u>(21,118,699)</u>	<u>(22,934,378)</u>	<u>(4,873,440)</u>	<u>(4,519,720)</u>
Cash and equity in pooled investments - beginning	66,113,463	89,047,841	38,985,005	43,504,725
Cash and equity in pooled investments - ending	<u>\$ 44,994,764</u>	<u>\$ 66,113,463</u>	<u>\$ 34,111,565</u>	<u>\$ 38,985,005</u>

Supplemental (Unaudited)

City of Tacoma, Washington
Environmental Services Department
Wastewater and Surface Water Management
Statements of Cash Flows

	Wastewater		Surface Water	
	Year Ended December 31,		Year Ended December 31,	
	2013	2012	2013	2012
Reconciliation of cash and equity in pooled investments to balance sheets:				
Operating funds	\$ 37,697,586	\$ 58,975,283	\$ 23,073,009	\$ 21,631,373
Restricted funds	7,297,178	7,138,180	11,038,556	17,353,632
	<u>\$ 44,994,764</u>	<u>\$ 66,113,463</u>	<u>\$ 34,111,565</u>	<u>\$ 38,985,005</u>
Reconciliation of operating income to net cash from operating activities:				
Operating income	\$ 7,857,032	\$ 6,379,462	\$ 8,478,164	\$ 5,696,412
Adjustments to reconcile operating income to net cash from operating activities:				
Depreciation expense	10,558,559	9,925,613	3,422,255	2,748,650
Low income assistance	(80,157)	(52,476)	(38,949)	(21,447)
Change in assets, liabilities, and deferred inflows of resources:				
Accounts receivable, net of allowance	(123,887)	82,672	97,182	21,958
Unbilled revenue	22,000	(1,072,000)	(312,000)	(438,000)
Notes and contract receivable	(63,420)	(8,891)	-	-
Due from other funds	(60,071)	185,624	(33,096)	(75,180)
Due from other governmental units	-	-	-	17,000
Inventory	(37,639)	168,597	-	-
Prepaid expenses	(432,420)	(12,919)	(27,910)	(272)
Accounts payable	(1,939,217)	458,769	1,146,663	(329,466)
Accrued wages and compensated absences	275,924	620,554	179,815	256,341
Accrued taxes payable	(8,944)	26,040	20,514	(1,992)
Deposits payable	-	-	(5,584)	(24,488)
Due other funds	114,429	24,142	132,787	(40,351)
Due other governmental units	(19,262)	4,012	-	-
Unearned revenue	5,918	7,741	2,914	3,569
Rate stabilization	-	-	-	2,500,000
Environmental liability	-	-	(337,766)	(100,000)
Net OPEB obligation	273,343	225,673	23,179	92,937
Total adjustments	<u>8,485,156</u>	<u>10,583,151</u>	<u>4,270,004</u>	<u>4,609,259</u>
	<u>\$ 16,342,188</u>	<u>\$ 16,962,613</u>	<u>\$ 12,748,168</u>	<u>\$ 10,305,671</u>
Significant non-cash transactions:				
Capital and Related Financing Activities				
Donated fixed assets	\$ 145,725	\$ 1,423,037	\$ 9,469,829	\$ 2,340,062
Transfers capital related	-	-	1,856,869	-
	<u>\$ 145,725</u>	<u>\$ 1,423,037</u>	<u>\$ 11,326,698</u>	<u>\$ 2,340,062</u>

Supplemental (Unaudited)

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