

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Tacoma, we offer readers of the City of Tacoma's financial statements this narrative overview and analysis of the financial activities of the City of Tacoma for the fiscal year ended December 31, 2014. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our Letter of Transmittal, which can be found on pages 1-1 to 1-4 of this report. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

Financial Highlights

- Total assets and deferred outflows of resources exceeded the City's liabilities and deferred inflows resources by \$2.7 billion. Of this amount, \$287 million were reported as unrestricted net position, amounts which are available to meet the City's on-going obligations to citizens and creditors.
- The City's net position increased by \$64 million. This increase is due to an increase in capital assets and a decrease in liabilities for Business Activities.
- Tacoma Power reported a change in net position of \$23.7 million, up \$ 5.9 million from the change in 2013.
- Tacoma Water reported change in net position of \$36.4 million, up \$ 9.0 million from the change in 2013.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the City of Tacoma's basic financial statements. The City of Tacoma's basic financial statements consist of three components: 1) the government-wide financial statements, 2) the fund financial statements, and 3) the notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the City of Tacoma's finances, and are similar to private sector financial statements. The statements also include the discretely presented component units, Tacoma Community Redevelopment Authority (TCRA), the Greater Tacoma Regional Convention Center Public Facilities District (GTRCCPF), and the Foss Waterway Development Authority (FWDA.)

The Statement of Net Position includes information on all assets and deferred outflows of resources and all liabilities and deferred inflows of resources of the City of Tacoma's general government as well as its business-type activities. The difference between the assets plus deferred outflows of resources and liabilities plus deferred inflows of resources is reported as net position. Over time, increases and decreases in net position may serve as a useful indicator of whether the financial position of the City of Tacoma is improving or deteriorating.

The Statement of Activities presents information showing how the government's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses reported in this statement for some items will only result in cash flows in future fiscal periods.

Governmental Activities

Business Activities

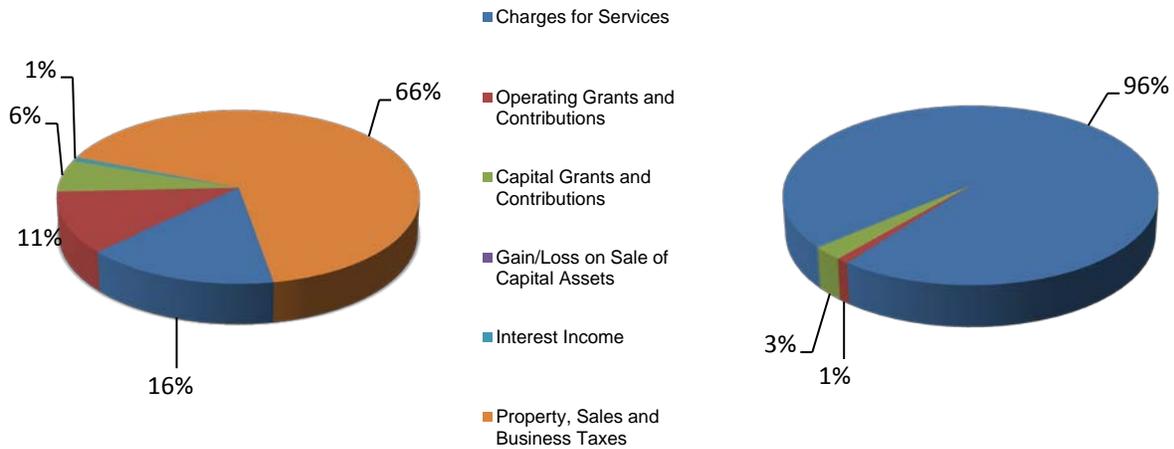


Figure 1. Comparison of Governmental and Business Activity Revenues

Both the Statement of Net Position and the Statement of Activities differentiate the functions of general government from the functions of business-type activities. Governmental activities reflect the City’s basic functions such as general government, public safety, transportation, economic environment, social services, and culture and recreation. Governmental activities are primarily supported by taxes and intergovernmental revenues. Business-type activities, primarily utilities, are intended to recover most if not all of their costs through user fees and charges for services. The government-wide financial statements can be found on pages 3-2 to 3-5 of this report.

Governmental Activities Expenses

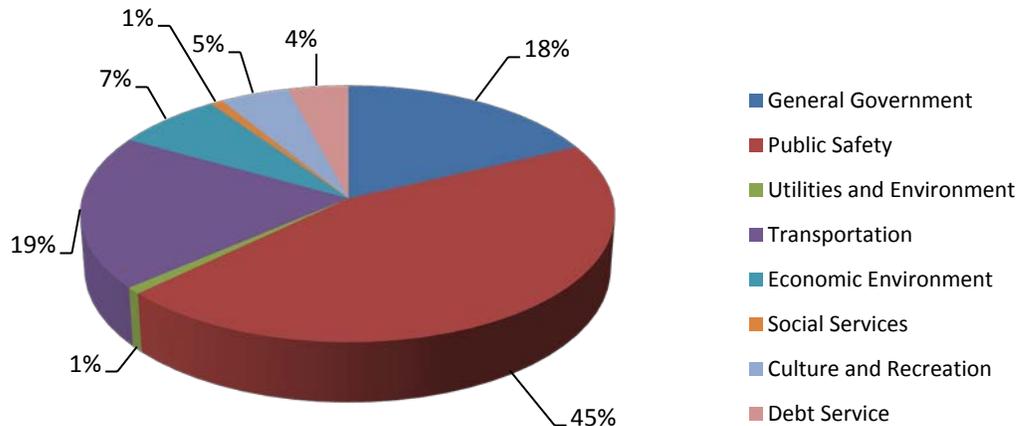


Figure 2. Governmental Activities Expenses

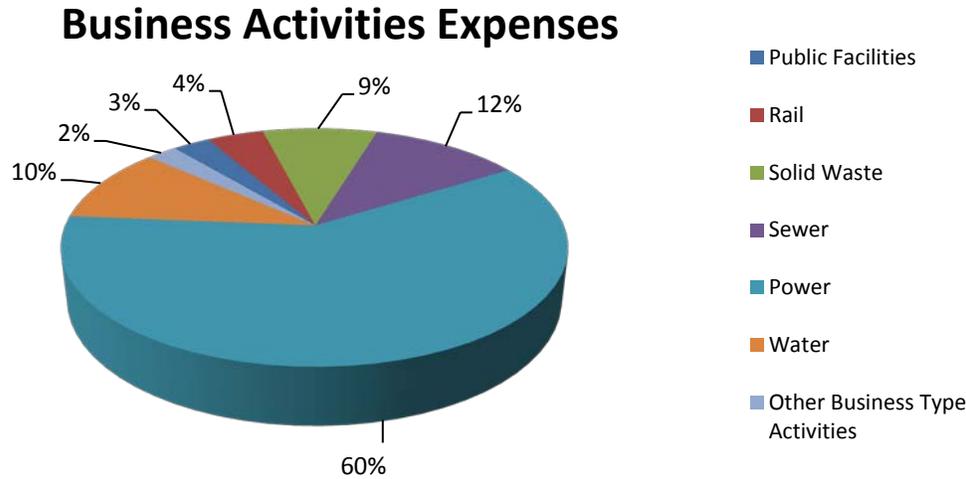


Figure 3. Business Activities Expenses

Fund Financial Statements

A fund is a grouping of related accounts used to maintain control over resources that have been segregated for specific activities or objectives. The City of Tacoma, like other local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All the funds of the City of Tacoma can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental Funds

Governmental funds are used to account for the functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near term inflows and outflows of expendable resources, as well as on balances of expendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of government-wide financial statements, it is useful to compare the information presented for the governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balance provide a reconciliation to facilitate this comparison.

The focus of the governmental fund statements is on major funds. A fund is considered major if it represents at least 10% of the assets, liabilities, revenues or expenditures of its fund category and at least 5% of the corresponding totals for the governmental and business-type activities combined. All other governmental funds are combined and presented as a single column in the respective governmental fund statements. Individual fund data for each of these combined non-major funds is provided in the form of combining statements elsewhere in this report. The Transportation Capital and Engineering fund was added to governmental activities as a major fund in 2011.

The City of Tacoma adopts a biennial budget for its General Fund. A budgetary comparison statement has been provided for the General Fund to demonstrate compliance with the budget.

The basic governmental fund financial statements can be found on pages 3-6 to 3-9 of this report.

Proprietary Funds

There are two types of proprietary funds, internal service and enterprise, both of which the City of Tacoma uses. Internal service funds are used to accumulate and allocate costs internally among the City of Tacoma's various functions. Because these services primarily benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements. There are two exceptions with the Self Insurance and Utility Fleet funds which only services utilities funds and are included within business type activities. Enterprise funds account for various utilities which provide services such as power, water, sewer, and solid waste collection. The service area for these utilities is generally broader than the corporate limits of the City. The activities in these funds are primarily supported by user fees and are presented as business-type activities in the government-wide financial statements. The Solid Waste fund was added to business activities as a major fund in 2012. The basic proprietary fund financial statements can be found on pages 3-10 to 3-21 of this report.

Fiduciary Funds

Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the City of Tacoma's programs. The accounting used by the fiduciary funds is similar to that used for proprietary funds. The basic fiduciary fund statements can be found on pages 3-22 to 3-23 of this report.

Notes to the Financial Statements

The notes to the financial statements provide additional information that is essential for a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 3-24 to 3-83 of this report.

Required Supplementary Information

In addition to the basic financial statements and accompanying notes, this report also contains certain required supplementary information (RSI) concerning the City of Tacoma's budget. Required supplementary information can be found on pages 4-1 to 4-5 of this report.

Combining Statements – Non-Major funds

The combining statements referred to earlier in connection with Non-Major governmental funds, internal service funds, and fiduciary funds can be found on pages 5-1 to 5-109 of this report.

Other Supplementary Information

This section provides schedules of capital assets used in the operations of Governmental Funds and statistical information on Local Improvement District assessments. The Other Supplementary Information section can be found on pages 5-112 to 5-114.

Statistical Section

This section provides financial trends, revenue and debt capacity, and demographic and economic information about the City's operations. The Statistical Section can be found on pages 6-1 to 6-36 of this report.

Government-wide Financial Analysis

As noted earlier, net position may serve as a useful indicator of a government's financial position. The City's total assets exceeded total liabilities by \$2.7 billion at December 31, 2014. 82% of the total net position reflects the City's investment in capital less any outstanding debt used to acquire those assets. The City uses these capital assets to provide services to its citizens; thus, they do not represent resources available for future spending. 11% of the City's net position is unrestricted, meaning they are available for meeting the City's ongoing obligations. The remaining 7% of net position is restricted for other purposes such as debt redemption and new capital construction. Governmental activities represent 27% of total net position and business activities represent 73% of total net position.

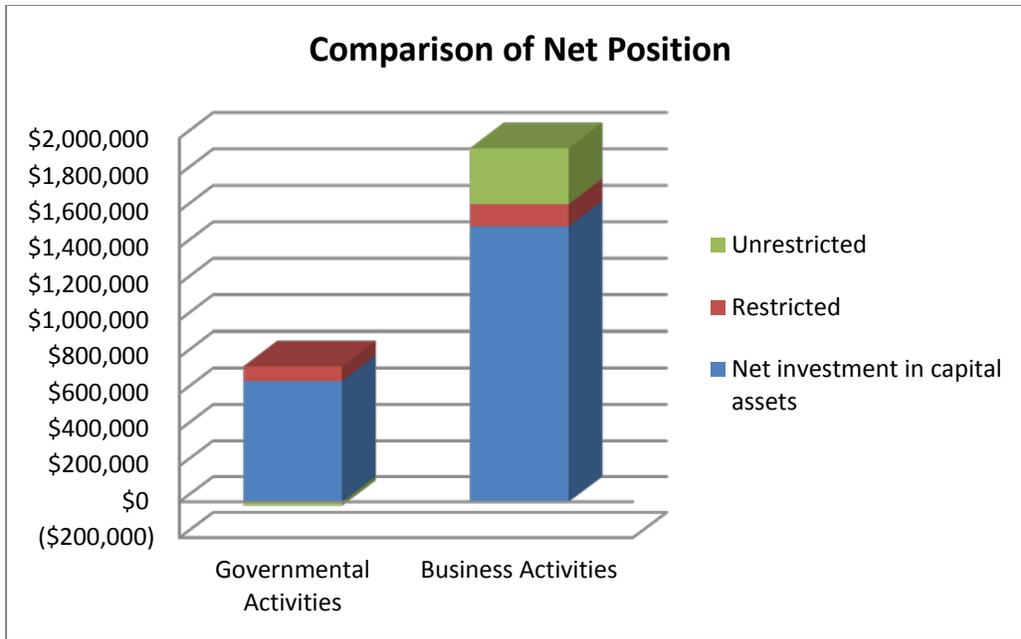


Figure 4. Comparison of Net Position, By Activity Type (Amounts expressed in thousands)

Table 1. Summary Statement of Net Position

**Statement of Net Position
For the Year Ended December 31, 2014**

(Amounts expressed in thousands)	Governmental Activities		Business Activities		Total	
	2014	2013	2014	2013	2014	2013
Current and other assets	\$ 276,795	\$ 272,098	\$ 931,897	\$ 977,710	\$ 1,208,692	\$ 1,249,808
Capital assets	828,035	847,508	2,723,738	2,626,269	3,551,773	3,473,777
Total assets	\$ 1,104,830	\$ 1,119,606	\$ 3,655,635	\$ 3,603,979	\$ 4,760,465	\$ 4,723,585
Deferred Outflow of Resources	\$ 4,226	\$ 4,226	\$ 13,898	\$ 19,146	\$ 18,124	\$ 23,372
Current and other liabilities	\$ 108,802	\$ 105,258	\$ 183,202	\$ 187,620	\$ 292,004	\$ 292,878
Long-term liabilities outstanding	232,123	247,675	1,427,425	1,442,574	1,659,548	1,690,249
Total liabilities	\$ 340,925	\$ 352,933	\$ 1,610,627	\$ 1,630,194	\$ 1,951,552	\$ 1,983,127
Deferred Inflows of Resources	\$ 39,117	\$ 39,731	\$ 114,575	\$ 114,575	\$ 153,692	\$ 154,306
Net Position:						
Net investment in capital assets	\$ 669,951	\$ 681,794	\$ 1,515,858	\$ 1,508,950	\$ 2,185,809	\$ 2,190,744
Restricted	79,630	74,670	121,369	112,925	200,999	187,595
Unrestricted	(20,567)	(25,296)	307,104	256,481	286,537	231,185
Total net position	\$ 729,014	\$ 731,168	\$ 1,944,331	\$ 1,878,356	\$ 2,673,345	\$ 2,609,524

In 2014, the City's net position increased by \$64 million. This is due to an increase in capital assets and a decrease in liabilities for governmental and business activities. The 2013 fund balances were restated in the fund balance categories.

Net Position - Governmental Activities

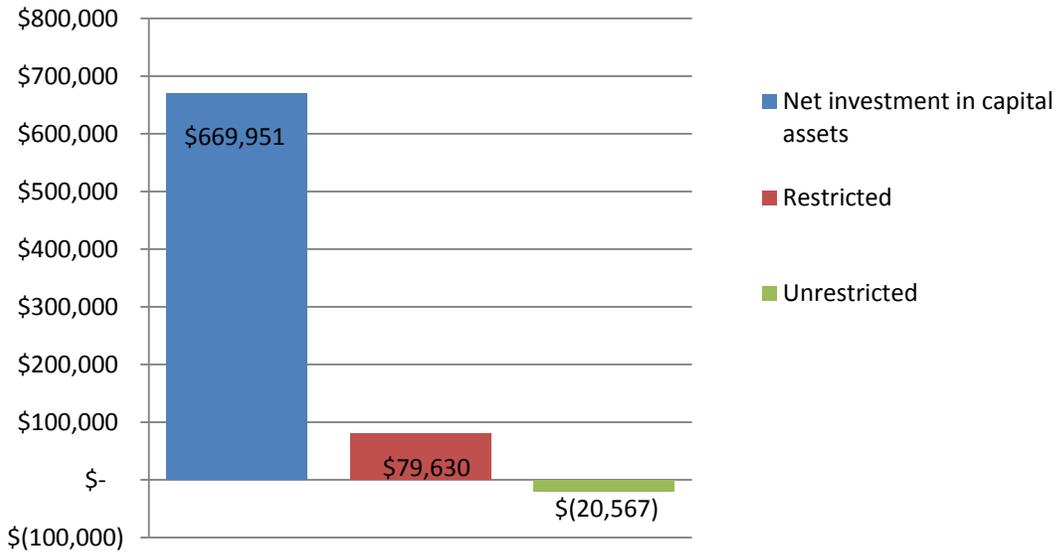


Figure 5. Composition of Net Position--Governmental Activities (Amounts expressed in thousands)

Net Position - Business Activities

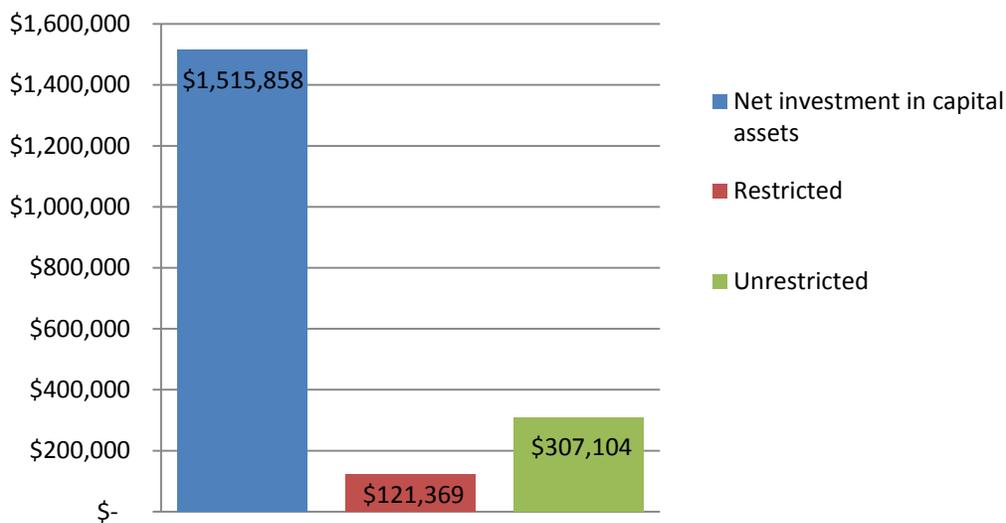


Figure 6. Composition of Net Position--Business Activities (Amounts expressed in thousands)

City of Tacoma, Washington
Changes in Net Position

(Amounts expressed in thousands)

	Governmental Activities		Business Activities		Total	
	2014	2013	2014	2013	2014	2013
Revenues:						
Program revenues						
Charges for services	\$ 41,628	\$ 37,354	\$ 785,502	\$ 739,699	\$ 827,130	\$ 777,053
Operating grants and contributions	30,378	33,925	7,968	7,438	38,346	41,363
Capital grants and contributions	15,882	19,813	19,587	25,150	35,469	44,963
General revenues						
Property taxes	64,204	62,487	-	-	64,204	62,487
Other taxes	111,945	149,374	-	-	111,945	149,374
Other	2,090	433	1,774	2,879	3,864	3,312
Total revenue	266,127	303,386	814,831	775,166	1,080,958	1,078,552
Expenses:						
General government	\$ 56,887	\$ 49,781	\$ -	\$ -	\$ 56,887	\$ 49,781
Public safety	142,097	138,368	-	-	142,097	138,368
Utilities and environment	2,580	2,477	-	-	2,580	2,477
Transportation	61,524	58,288	-	-	61,524	58,288
Social services	2,649	1,953	-	-	2,649	1,953
Economic Environment	22,856	21,255	-	-	22,856	21,255
Culture and recreation	14,823	18,832	-	-	14,823	18,832
Debt Service	13,001	14,401	-	-	13,001	14,401
Public assembly facilities	-	-	19,801	16,832	19,801	16,832
Rail	-	-	30,095	29,024	30,095	29,024
Solid waste	-	-	61,040	67,591	61,040	67,591
Waste water	-	-	80,343	81,286	80,343	81,286
Water	-	-	72,324	79,773	72,324	79,773
Power	-	-	422,265	432,321	422,265	432,321
Other business-type funds	-	-	16,005	14,979	16,005	14,979
Total expenses	316,417	305,355	701,873	721,806	1,018,290	1,027,161
Increase/(Decrease) in net position before transfers	(50,290)	(1,969)	112,958	53,360	62,668	51,391
Transfers	44,853	(2,153)	(44,853)	2,153	-	-
Increase/(Decrease) in net position	(5,437)	(4,122)	68,105	55,513	62,668	51,391
Net position--January 1	731,168	716,822	1,878,356	1,823,949	2,609,524	2,540,771
Prior Period Adjustments	3,283	18,468	(2,130)	(533)	1,153	17,935
Change in accounting principle	-	-	-	(573)	-	(573)
Net position--January 1	734,451	735,290	1,876,226	1,822,843	2,610,677	2,558,133
Net position--December 31	\$ 729,014	\$ 731,168	\$ 1,944,331	\$ 1,878,356	\$ 2,673,345	\$ 2,609,524

Table 2. Changes in Net Position

The governmental activities net position decreased by \$2.2 million in 2014 due to a decrease in assets and deferred outflows of resources by \$14.7 million and also a decrease of liabilities and deferred inflows of resources of \$12.5 million.

Business activities net position increased by \$66 million in 2014 due to an increase in assets and deferred outflows of \$46 million and a decrease of \$20 million in liabilities and deferred inflows of resources.

Information on significant outstanding claims can be found in Note 9.

Financial Analysis of the City's Fund Statements

The City prepares fund statements for governmental funds and for proprietary funds.

Governmental Fund Statements

Fund balance for the City's General Fund had no significant change. Fund balance for the Transportation Capital and Engineering fund increased by \$7.9 million in 2014 from a decrease in liabilities. Fund balance for the Non-Major governmental funds, which include debt service funds, capital projects funds, and special revenue funds, decreased by \$4.7 million from an increase in liabilities.

Fund Balances

At December 31, 2014, the City's governmental funds reported combined ending fund balances of \$164 million. Of this amount, \$16.9 million is nonspendable, either due to its form or legal constraints. \$79.6 million is restricted for specific programs by external constraints. \$1.2 million is committed for specific purposes as approved by City Council. \$23.7 million is assigned to specific purposes by management and the remaining \$42.6 million is unassigned.

Proprietary Fund Statements

Total net position for the enterprise funds increased by \$64.9 million in 2014. The Power, Water, Solid Waste and Sewer utilities make up the majority of the proprietary funds. Activity in these utilities was the primary driver for the change in the net position. The Power fund had an increase in net position of \$23.7 million from a decrease in liabilities. The Water fund had a significant increase in their net position of \$36.4 million due to an increase in capital construction. The Sewer fund had an increase in net position of \$10 million from an increase in revenues. The Solid Waste fund had no significant change in net position. The non-major Enterprise funds had a decrease in net position of \$4.9 million from a decrease in revenues and slight increase in increase liabilities. The total net position for internal service funds' increased by \$2.8 million in 2014. This is the result of an increase of \$3.4 million in assets while also having an increase of liabilities of about \$500 thousand.

General Fund Budgetary Highlights

In 2014, the City made budgetary adjustments as part of the 2013-2014 Mid-Biennium Budget Amendment. Budget revisions included a \$4.1 million reduction in the General Fund to move appropriations to the Transportation Benefit District Fund in 2013. At mid biennium, a \$2.1 million increase to the General Fund was made for various expenditures and an additional increase of \$2.1 million was made in 2014 for various grants and contributions. At biennium-end 2014, the General Fund revenues came in under budget by \$39.7 million and expenditures came in under budget by \$19.9 million. \$42 million in transfers were made into the General Fund along with \$1.3 million in other financing sources which made the net change in fund balance increase by \$23.5 million. Transfers increased due to the re-classification of Gross Earnings Taxes from Taxes to Transfers in 2014. The City's budget is a two year biennium budget which begins every odd year.

Capital Assets, Infrastructure, Bond Debt Administration

Capital Assets

The City of Tacoma's capital assets net of accumulated depreciation for its governmental and business type activities as of December 31, 2014 is \$3.6 billion. This investment in capital assets includes land, construction in process, property, plant and equipment, and infrastructure. The vast majority of this amount represents assets held by the City's various utilities and infrastructure.

The following table summarizes the City's investment in capital assets.

City of Tacoma, Washington
Schedule of Capital Assets

(Amounts expressed in thousands)	Governmental Activities		Business Activities		Total	
	2014	2013	2014	2013	2014	2013
Land	\$ 27,102	\$ 28,201	\$ 158,046	\$ 158,386	\$ 185,148	\$ 186,587
Construction in progress	84,113	84,083	266,764	180,780	350,877	264,863
Property, plant and equipment	219,833	214,192	3,844,414	3,739,727	4,064,247	3,953,919
Infrastructure	1,316,313	1,303,768	-	-	1,316,313	1,303,768
Less accumulated depreciation	(819,326)	(782,736)	(1,545,486)	(1,452,624)	(2,364,812)	(2,235,360)
	<u>\$ 828,035</u>	<u>\$ 847,508</u>	<u>\$ 2,723,738</u>	<u>\$ 2,626,269</u>	<u>\$ 3,551,773</u>	<u>\$ 3,473,777</u>

Table 3. Schedule of Capital Assets

Additional information on the City's capital assets can be found in Notes 1-D5 and 4-C of the Notes to the Financial Statements.

Outstanding Debt

The City's debt at December 31, 2014 was \$1.8 billion. Approximately 83% of the bonded debt is related to utilities with repayment pledged by specific revenue sources generated by the utilities. Of the remaining 17% bonded debt, debt is either secured by voter approved special levies or general government resources. Additional information on the City of Tacoma's long-term debt can be found in Note 4-F and Note 12 of the Notes to the Financial Statements.

City of Tacoma, Washington
Schedule of Long Term Debt

(Amounts expressed in thousands)	Governmental Activities		Business Activities		Total	
	2014	2013	2014	2013	2014	2013
Bonded debt and loans	\$ 206,664	\$ 225,653	\$ 1,392,059	\$ 1,403,305	\$ 1,598,723	\$ 1,628,958
Capital leases	-	-	34,305	35,058	34,305	35,058
Claims and judgments	22,830	24,236	-	1,178	22,830	25,414
Accrued landfill liability	-	-	26,724	25,691	26,724	25,691
Net Pension Obligation	9,608	9,643	-	-	9,608	9,643
Other Post Employment Benefits	49,703	42,145	16,408	13,952	66,111	56,097
Compensated absences	16,218	17,310	19,147	18,944	35,365	36,254
	<u>\$ 305,023</u>	<u>\$ 318,987</u>	<u>\$ 1,488,643</u>	<u>\$ 1,498,128</u>	<u>\$ 1,793,666</u>	<u>\$ 1,817,115</u>

Table 4. Schedule of Long Term Debt

The City's debt rating for 2014 is as follows:

Bond	Moody's	S&P	Fitch
GO	Aa3	AA	A+
LTGO	A1	AA	A
Solid Waste	A2	AA	AA-
Sewer	Aa2	AA+	AA+
Water	Aa2	AA	--
RWSS	Aa2	AA	--
Power	Aa3	AA	AA-
Convention Center Revenue	A2	A	A+

Economic Factors

The following economic factors currently affect the City of Tacoma:

- The unemployment rate for the City of Tacoma is currently 6.1% which is a decrease of 1.3% from 2013.
- Taxable property value has increased by \$1.3 billion over 2013, which is a 7.8% increase.
- Housing prices and sales have continued to improve and show gains over the prior year.
- The Transportation Benefit District, which was created in 2012 to collect motor vehicle license fees, has been collecting revenues as projected. The 2015-2016 biennium budget is \$4.1 million.

During the current fiscal year, the unassigned fund balance in the general fund was \$48.3 million, up \$5.2 million from 2013. There is still a projected deficit of \$6 million for the 2015-2016 biennium. The City will continue to evaluate revenues and expenditures during the 2015-2016 budget preparation to produce a balanced budget.

Other Considerations

In response to the slow economic recovery, the City has taken steps to reduce discretionary spending. General government activities took significant expenditure reductions to bring levels of service to those that are affordable and sustainable. Revenue growth is limited by several citizen initiatives that limit the growth of property tax collections.

Requests for Information

This financial report is designed to provide a general overview of the City's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City of Tacoma Finance Department, 747 Market Street Room 132, Tacoma, Washington 98402.