

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, 2017. 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 of resources by \$2.8 billion. Of this amount, \$233 million is reported as unrestricted net position, representing amounts which are available to meet the City's on-going obligations to citizens and creditors.
- The City's overall net position increased by \$57 million in 2017.
- Tacoma Power's net position for 2017 was \$830.2 million which was an increase of \$8.2 million from 2016.
- Tacoma Water's net position for 2017 was \$556.7 million which was an increase of \$7.1 million from 2016.
- Sewer's net position for 2017 was \$435.4 million which was an increase of \$13.3 million from 2016.

Overview of the Financial Statements

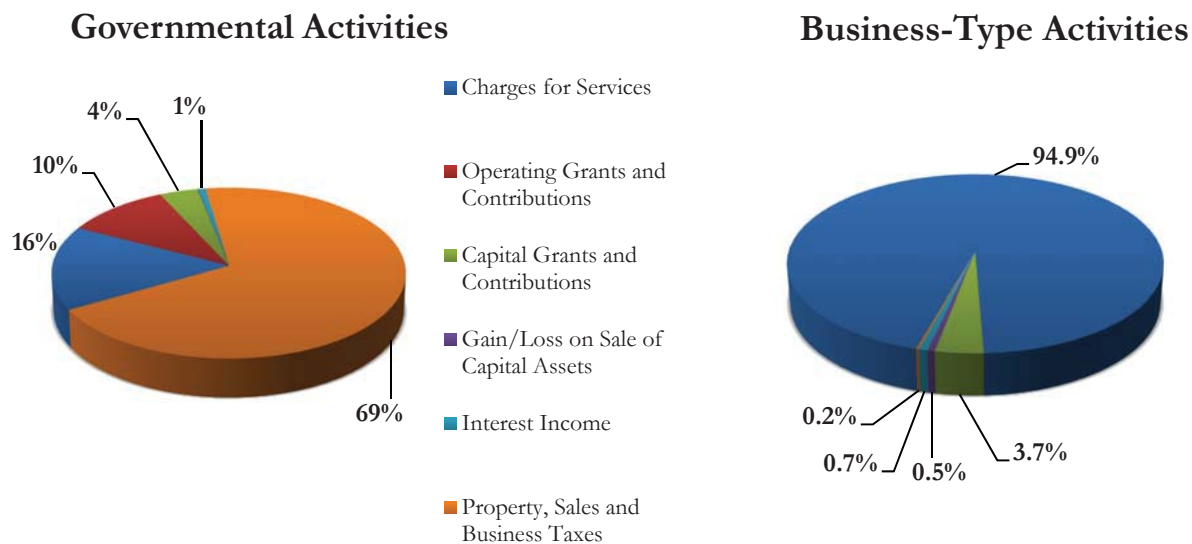
This discussion and analysis is intended to serve as an introduction to the City of Tacoma's basic financial statements. The City of Tacoma's basic financial statements consist of three components: 1) the government-wide financial statements, 2) the fund financial statements, and 3) the notes to the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

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 (GTRCCPFD), 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.

Figure 1. Comparison of Governmental and Business-Type 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.

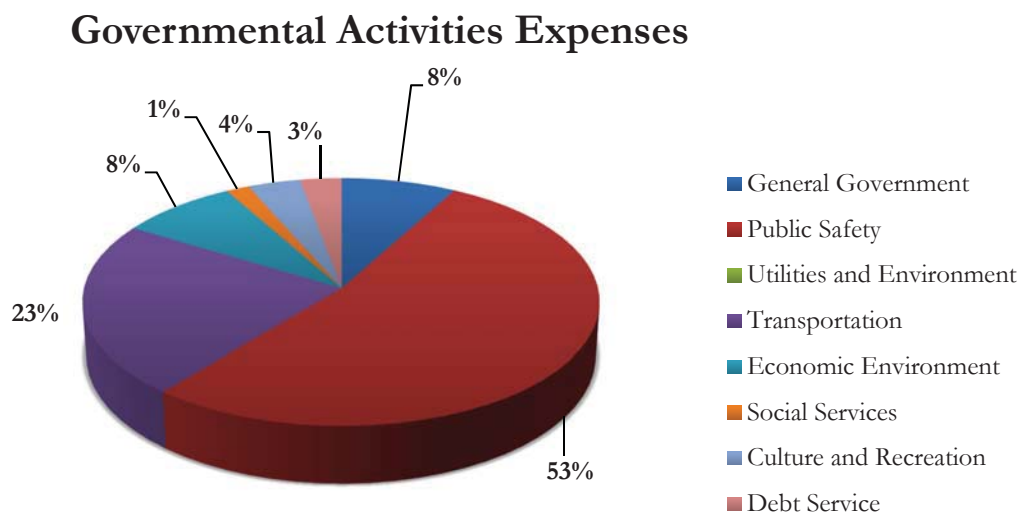
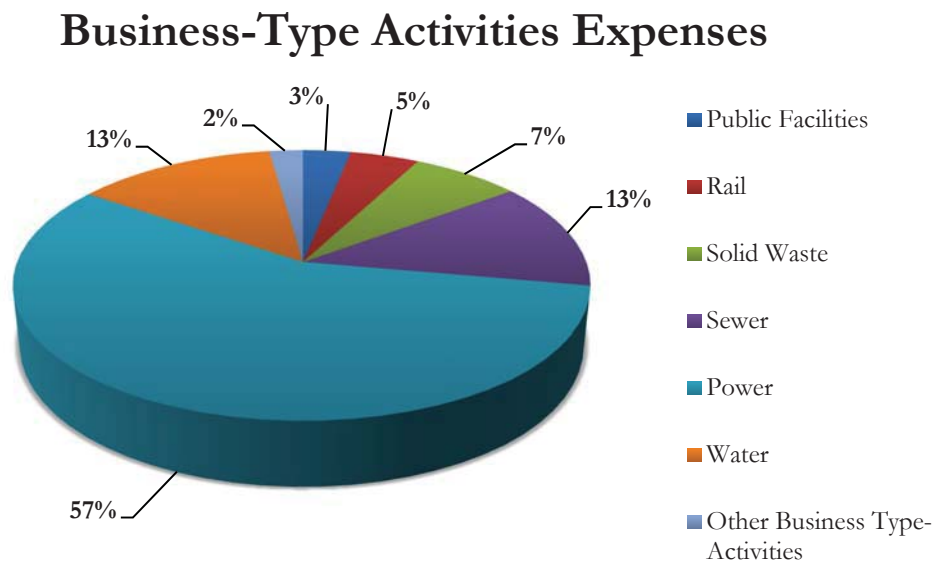
Figure 2. Governmental Activities Expenditures

Figure 3. Business-Type 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 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 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 3-90 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 4-9 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 5-115 of this report.

Other Supplementary Information

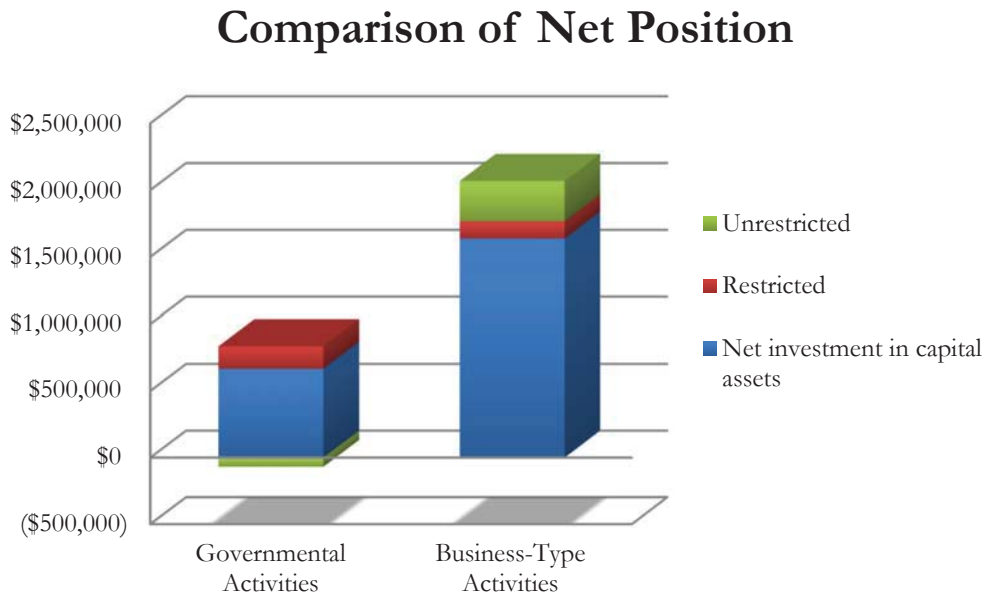
This section provides statistical information on Local Improvement District assessments. The Other Supplementary Information section can be found on pages 5-117.

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 \$2.8 billion at December 31, 2017. 81.3% of the total net position reflects the City's investment in capital assets 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. 8.2% of the City's net position is unrestricted, meaning they are available for meeting the City's ongoing obligations. The remaining 10.5% of net position is restricted for other purposes such as debt redemption and new capital construction. Governmental activities represent 27.0% of total net position and business-type activities represent 73.0% 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 December 31						
(Amounts expressed in thousands)	Governmental Activities		Business-Type Activities		Total	
	2017	2016	2017	2016	2017	2016
Current and other assets	\$ 401,122	\$ 316,348	\$ 856,424	\$ 877,669	\$ 1,257,546	\$ 1,194,017
Capital assets	806,327	819,394	2,822,014	2,824,020	3,628,341	3,643,414
Total assets	\$ 1,207,449	\$ 1,135,742	\$ 3,678,438	\$ 3,701,689	\$ 4,885,887	\$ 4,837,431
Deferred Outflow of Resources	\$ 37,607	\$ 21,512	\$ 75,168	\$ 77,892	\$ 112,775	\$ 99,404
Current and other liabilities	\$ 43,991	\$ 33,204	\$ 114,463	\$ 116,117	\$ 158,454	\$ 149,321
Long-term liabilities outstanding	391,050	332,361	1,441,943	1,518,894	1,832,993	1,851,255
Total liabilities	\$ 435,041	\$ 365,565	\$ 1,556,406	\$ 1,635,011	\$ 1,991,447	\$ 2,000,576
Deferred Inflows of Resources	\$ 43,788	\$ 39,876	\$ 129,096	\$ 119,281	\$ 172,884	\$ 159,157
Net Position:						
Net investment in capital assets	\$ 666,530	\$ 673,093	\$ 1,636,652	\$ 1,613,805	\$ 2,303,182	\$ 2,286,898
Restricted	168,280	113,897	129,836	124,289	298,116	238,186
Unrestricted	(68,583)	(35,177)	301,616	287,195	233,033	252,018
Total net position	\$ 766,227	\$ 751,813	\$ 2,068,104	\$ 2,025,289	\$ 2,834,331	\$ 2,777,102

In 2017, the City's total net position increased by \$57 million, which was a 2% increase in fund balance from 2016.

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

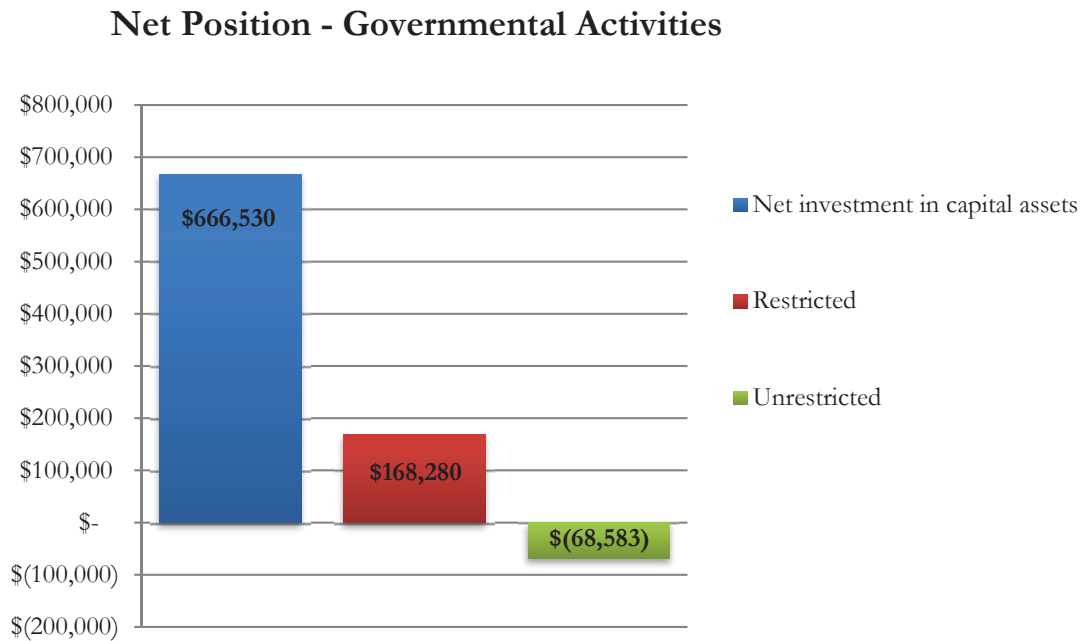


Figure 6. Composition of Net Position—Business-Type Activities (Amounts expressed in thousands)

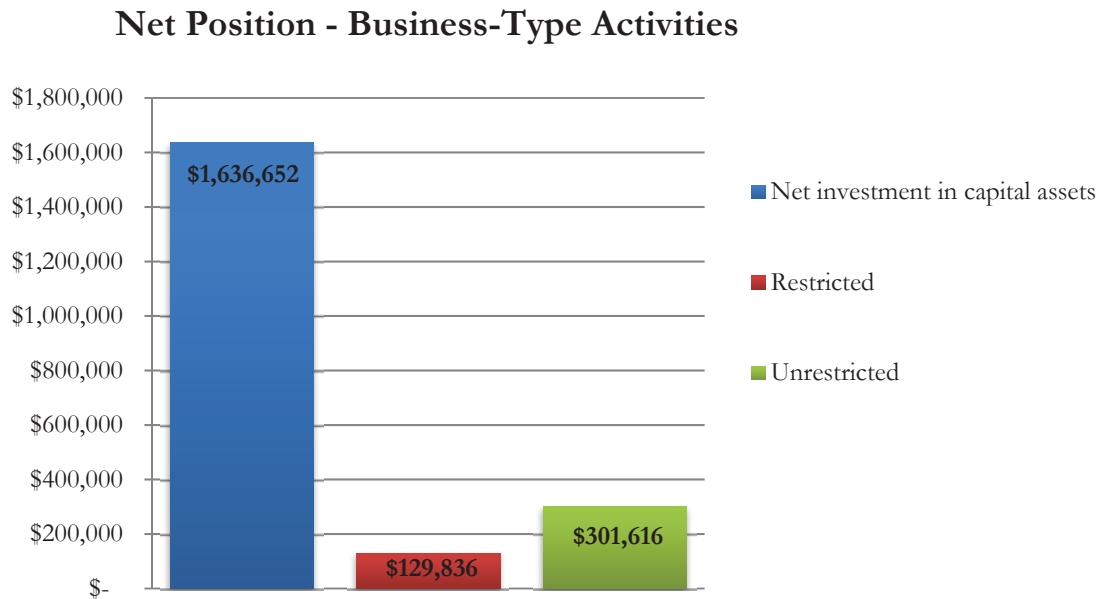


Table 2. Changes in Net Position

City of Tacoma, Washington Changes in Net Position							
<i>(Amounts expressed in thousands)</i>							
	Governmental Activities		Business-Type Activities		Total		
	2017	2016	2017	2016	2017	2016	
Revenues:							
Program revenues							
Charges for services	\$ 48,562	\$ 62,782	\$ 791,542	\$ 761,282	\$ 840,104	\$ 824,064	
Operating grants and contributions	31,791	33,903	208	8,392	31,999	42,295	
Capital grants and contributions	11,549	7,392	30,528	21,413	42,077	28,805	
General revenues	-	-	-	-	-	-	
Property taxes	74,479	78,886	-	-	74,479	78,886	
Other taxes	135,558	122,310	1,702	-	137,260	122,310	
Other	2,427	2,316	10,241	7,005	12,668	9,321	
Total revenue	304,366	307,589	834,221	798,092	1,138,587	1,105,681	
Expenses:							
General government	\$ 24,436	\$ 74,293	\$ -	\$ -	\$ 24,436	\$ 74,293	
Public safety	162,416	175,131	-	-	162,416	175,131	
Utilities and environment	-	1	-	-	-	1	
Transportation	69,741	60,881	-	-	69,741	60,881	
Social services	4,908	4,983	-	-	4,908	4,983	
Economic Environment	25,102	36,759	-	-	25,102	36,759	
Culture and recreation	11,187	15,258	-	-	11,187	15,258	
Debt Service	8,837	8,670	-	-	8,837	8,670	
Public assembly facilities	-	-	23,243	20,986	23,243	20,986	
Rail	-	-	33,579	31,571	33,579	31,571	
Solid waste	-	-	52,938	66,661	52,938	66,661	
Waste water	-	-	95,960	92,958	95,960	92,958	
Water	-	-	97,540	95,869	97,540	95,869	
Power	-	-	420,368	404,566	420,368	404,566	
Other business-type funds	-	-	16,326	16,721	16,326	16,721	
Total expenses	306,627	375,976	739,954	729,332	1,046,581	1,105,308	
Increase/(Decrease) in net position before transfers	(2,261)	(68,387)	94,267	68,760	92,006	373	
Transfers	51,452	48,973	(51,452)	(48,973)	-	-	
Increase/(Decrease) in net position	49,191	(19,414)	42,815	19,787	92,006	373	
Net position--January 1	751,813	771,777	2,025,289	2,006,164	2,777,102	2,777,941	
Prior Period Adjustments	1,169	(1,048)	-	(662)	1,169	(1,710)	
Change in accounting principle	(35,946)	498	-	-	(35,946)	498	
Net position--January 1	717,036	771,227	2,025,289	2,005,502	2,742,325	2,776,729	
Net position--December 31	\$ 766,227	\$ 751,813	\$ 2,068,104	\$ 2,025,289	\$ 2,834,331	\$ 2,777,102	

Tacoma's governmental activities reported a combined fund balance of \$766 million, which was an increase of \$14 million from 2016; this increase was due in a large part to an increase in tax revenues and grants received while also reducing general government and public safety expenses. The reduction in expenditures primarily reflects the decreased effect of the net pension liability on the expenditures. In addition general government expenditures decreased by \$69 million, primarily the result of moving support services (finance, legal, human resources, etc.) from the general fund to internal service funds. These expenditures are now reflected in the expenditures of the functions they support.

Business-type activities also saw a positive change, with an ending net position of \$2.07 billion. This is an increase of \$43 million over 2016.

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 was \$80.2 million which decreased by \$134 thousand or less than 1% from 2016. The general funds unassigned fund balance saw a decrease of \$1.4 million; this amount is not restricted for any specific purposes and may be used for spending at the government's discretion. Fund balance for the Transportation Capital and Engineering fund is \$3.8 million which decreased by \$2.7 million (42%) in 2017, caused by an increase in transportation expenditures of \$3.6 million. Fund balance for the Non-Major governmental funds, which include debt service funds, capital projects funds, and special revenue funds, was \$138.2 million. This increase of \$53.1 million (62%) is the result of the issuance of long-term debt of \$27.5 million and the sale of capital assets of \$4.9 million.

Fund Balances

At December 31, 2017, the City's governmental funds reported combined ending fund balances of \$222 million. Of this amount, \$5.3 million is nonspendable, either due to its form or legal constraints. \$116 million is restricted for specific programs by external constraints. \$8.9 million is committed for specific purposes as approved by City Council. \$24.1 million is assigned to specific purposes by management and the remaining \$67.7 million is unassigned.

Proprietary Fund Statements

Total net position for enterprise funds increased by \$46.0 million in 2017. Power, Water, Solid Waste and Sewer utilities make up the majority of the proprietary funds and activity in these utilities was the primary driver for the change in the net position. The Power funds net position increased by \$8.4 million, this was a 1% increase from 2016. The Water fund had an increase in their net position of \$7.1 million, a 1.3% increase from 2016. The Sewer fund had an increase in net position of \$13.4 million, or 3.2%. The Solid Waste funds net position had the largest increase of the proprietary funds at \$9.3 million, which was a 34% from 2016. This can be attributed to an average 3.4% rate increase in residential customers in 2017. Revenues from residential customers increased \$856,000 in 2017. Residential collection revenues increased due to the increases in both the number of customer accounts along with the rate increases. Commercial customer revenues increased \$1.7 million due to commercial business improvement and an increase in commercial Drop-off-Box containers. Disposal revenues increased \$1.6 million from continued increase in customer self-hauls and scale house rates increasing from \$15 to \$20 for the first 100 pounds. Salvage revenues increased by \$217,000 due to increases in both volumes and prices of salvaged materials. The non-major Enterprise funds had an ending net position of \$163.6 million which was an increase of \$7.7 million, or 5%. The total net position for internal service funds' was \$102.5 million and increased by \$2.1 million, or 2%, in 2017.

General Fund Budgetary Highlights

The City's budget is a two year biennium budget which begins every odd year, with 2017 being the start of the 2017-2018 biennium budget. The 2017-2018 adopted budget included funding for deferred maintenance such as \$5 million to cover the replacement for the City's fleet vehicles, bonds to cover the updating of the Tacoma Dome, and infrastructure investments to repair and maintain city streets.

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, 2017 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.

Table 3. Schedule of Capital Assets

City of Tacoma, Washington Schedule of Capital Assets						
(Amounts expressed in thousands)	Governmental Activities		Business-Type Activities		Total	
	2017	2016	2017	2016	2017	2016
	\$	\$	\$	\$	\$	\$
Land	36,380	35,335	164,293	163,451	200,673	198,786
Construction in progress	30,800	57,538	53,807	57,691	84,607	115,229
Property, plant and equipment	275,701	255,700	4,428,165	4,338,447	4,703,866	4,594,147
Infrastructure	1,410,490	1,373,328	-	-	1,410,490	1,373,328
Less accumulated depreciation	(947,044)	(902,507)	(1,824,251)	(1,735,569)	(2,771,295)	(2,638,076)
	<u>\$ 806,327</u>	<u>\$ 819,394</u>	<u>\$ 2,822,014</u>	<u>\$ 2,824,020</u>	<u>\$ 3,628,341</u>	<u>\$ 3,643,414</u>

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, 2017 was \$1.8 billion. Approximately 87% of the bonded debt is related to utilities with repayment pledged by specific revenue sources generated by the utilities. Of the remaining 13% 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.

Table 4. Schedule of Long Term Liabilities

City of Tacoma, Washington Schedule of Long Term Liabilities						
(Amounts expressed in thousands)	Governmental Activities		Business-Type Activities		Total	
	2017	2016	2017	2016	2017	2016
	\$	\$	\$	\$	\$	\$
Bonded debt and loans	196,081	182,106	1,317,775	1,396,763	1,513,856	1,578,869
Capital leases	-	-	-	-	-	-
Claims and judgments	33,784	27,183	-	-	33,784	27,183
Accrued landfill liability	-	-	18,080	21,118	18,080	21,118
Net OPEB Obligation	69,698	62,495	21,656	20,181	91,354	82,676
Net Pension Obligation	10,093	9,662	-	-	10,093	9,662
Pension Liability	27,989	25,948	64,891	60,636	92,880	86,584
Compensated absences	19,181	24,967	19,541	60,636	38,722	45,163
	<u>\$ 356,826</u>	<u>\$ 332,361</u>	<u>\$ 1,441,943</u>	<u>\$ 1,559,334</u>	<u>\$ 1,798,769</u>	<u>\$ 1,851,255</u>

The City's debt rating for 2017 is as follows:

Bond	Moody's	S&P	Fitch
GO	Aa2	AA	AA
LTGO	Aa2	AA	AA
Solid Waste	A1	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 5.4% which is a decrease of 0.6% from 2016.
- Sales tax revenue was \$71.6 million in 2017, which is a \$12.7 million increase over 2016 sales tax revenues.
- Taxable property values have increased by \$2.4 billion over 2016, which is an 11.6% increase.

City of Tacoma voters passed Proposition A and Proposition 3 in November 2015, which went into effect March 1st, 2016 and has increase both sales and property taxes in order to fund the repair and maintenance of roads, crosswalks and sidewalks. This will be accomplished through methods including pothole repair, street resurfacing, fixing sidewalk approaches and building missing sidewalks. Proposition A will raise sales tax by 1/10 of 1% over a period of 10 years. Proposition 3 will authorize an additional 1.5% earning tax on natural gas, electric and phone companies, and an increase in the regular property tax levy of \$.20 per \$1,000 of assessed value. The propositions together will provide an estimated \$17-18 million per year over the next ten years, with \$4.5 million from Proposition A and \$13 million from Proposition 3 per year. The City has also committed \$30 million and with matching grants the amount raised should total \$325 million. The City's tax and license department joined with the cities of Seattle, Bellevue and Everett as part of a program called FileLocal. This new website allows businesses to pay both B&O tax and business license fees online. This program is expected to bring in over \$3.8 million in extra revenue over the 2017-2018 biennium.

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.