



Solid Waste Management 2012 Financial Report

**City of Tacoma
Public Works
Environmental Services**

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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, Solid Waste Management
Tacoma Washington

Report on Financial Statements

We have audited the accompanying financial statements of City of Tacoma, Washington Public Works Department, Environmental Services, Solid Waste Management (the Division), which comprise the Statements of Net Position as of December 31, 2012 and 2011, and the related statements of revenue, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

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

Other Matter

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



Portland, Oregon
April 5, 2013

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Management's Discussion and Analysis

City of Tacoma, Washington
Public Works Department – Environmental Services
Solid Waste Management
Management’s Discussion and Analysis
December 31, 2012 and 2011

Introduction

The following is management’s discussion and analysis (MD&A) of the financial activities of the City of Tacoma’s Solid Waste Management Division (the Division) for the years ended December 31, 2012 and 2011. 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 which are prepared on a full accrual basis of accounting.

Financial Highlights

- Net position increased in 2012 by \$78,000 compared to an increase of \$5.2 million in 2011 and \$10.4 million in 2010.
- Operating revenues were \$56.8 million in 2012, \$57.1 million in 2011 and \$56.0 million in 2010.
- Total net position was \$23.9 million at December 31, 2012 compared to \$23.8 million and \$18.6 million at year-end 2011 and 2010, respectively.
- Cash and equity in pooled investments was \$43.2 million at December 31, 2012 compared to \$44.0 million in 2011 and \$70.9 million in 2010.

Financial Analysis – Condensed Statements of Net Position

	December 31,		
	2012	2011	2010
Current, restricted, and other assets	\$ 51,277,218	\$ 52,476,091	\$ 80,114,562
Capital assets	84,265,678	89,071,847	66,503,841
Total assets	\$ 135,542,896	\$ 141,547,938	\$ 146,618,403
Current liabilities and liabilities payable from restricted assets	\$ 14,746,242	\$ 15,852,083	\$ 17,828,301
Noncurrent liabilities	96,939,996	101,917,674	110,187,388
Total liabilities	111,686,238	117,769,757	128,015,689
Net investment in capital assets	23,087,873	28,641,409	16,809,022
Restricted for bond reserves	1,623,541	1,849,648	5,501,677
Unrestricted	(854,756)	(6,712,876)	(3,707,985)
Total net position	23,856,658	23,778,181	18,602,714
Total liabilities and net position	\$ 135,542,896	\$ 141,547,938	\$ 146,618,403

Current, restricted and other assets

Current, restricted and other assets decreased \$1.2 million in 2012 compared to a decrease of \$27.6 million in 2011. The decrease in 2012 was due to a decrease of \$771,000 in cash and equity in pooled investments and a decrease in other noncurrent assets of \$382,000. The decrease in 2011 was due to the decrease of \$23.6 million in bond construction funds primarily used for the administration building and transfer station. In addition, restricted debt service funds decreased \$4.1 million primarily as a result of calling the 2001 Revenue Refunding Bonds on December 1, 2011.

Capital Assets

Net capital assets decreased \$4.8 million in 2012 and increased \$22.6 million in 2011, due primarily to increased depreciation in 2012 and capital construction in 2011.

Current liabilities and liabilities payable from restricted assets

Total current liabilities and liabilities payable from restricted assets decreased \$1.1 million in 2012 and decreased \$2.0 million in 2011. Significant changes include:

- The accrued landfill closure and post closure current liabilities increased \$543,000 in 2012 and decreased \$908,000 in 2011 due to changes in the current portion of project costs.
- Accounts payable decreased \$1.4 million in 2012 compared to an increase of \$1.2 million in 2011 due to project year-end accruals.
- Environmental liabilities decreased \$334,000 in 2012 due to the final cash payout settlement with the EPA and the Division's environmental cleanup costs related to the Port of Tacoma's cleanup on the Lincoln Avenue project.

Noncurrent liabilities

Noncurrent liabilities consist of revenue bonds payable and related debt accounts, a capital lease obligation, noncurrent accrued landfill closure and post closure costs, noncurrent compensated absences and other post employment benefit (OPEB) obligations. Total noncurrent liabilities decreased \$5.0 million in 2012 and \$8.3 million in 2011.

- Long-term debt decreased \$2.9 million in 2012 and \$7.2 million in 2011. In addition to reclassifications to current liabilities and amortizations of premiums, refunding costs of \$541,000 in 2012 and \$855,000 in 2011 were reclassified to other non-current assets. On December 1, 2011 the \$6.1 million in outstanding 2001 Revenue Refunding Bonds were called.
- Non-current landfill closure and post closure liabilities decreased \$2.0 million in 2012 and \$1.0 million in 2011 related to work on closing the City's Landfill.

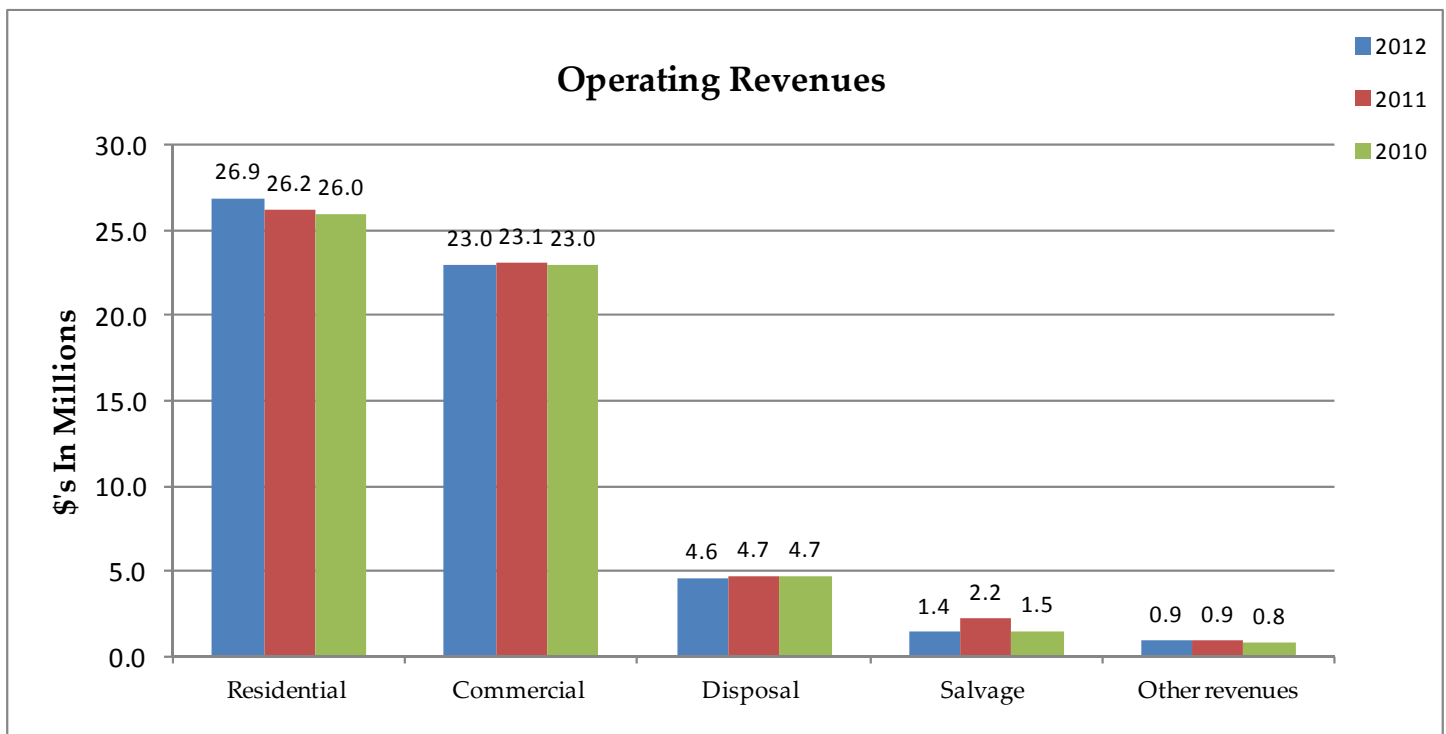
Financial Analysis - Condensed Statements of Revenues, Expenses and Changes in Net Assets

	Year Ended December 31,		
	2012	2011	2010
Operating revenues	\$ 56,807,522	\$ 57,101,949	\$ 56,033,649
Operating expenses	50,108,727	45,473,065	38,350,691
Net operating income	6,698,795	11,628,884	17,682,958
Nonoperating revenues (expenses):			
Investment income	774,934	1,698,012	1,265,537
Interest on revenue bonds	(3,344,432)	(3,214,931)	(3,896,807)
Other, net	(254,102)	(285,286)	(102,563)
Total nonoperating expenses	(2,823,600)	(1,802,205)	(2,733,833)
Net income before transfers	3,875,195	9,826,679	14,949,125
Transfers - gross earnings tax	(4,544,348)	(4,651,212)	(4,591,131)
Transfers - From other funds	747,630	-	-
Change in net position	78,477	5,175,467	10,357,994
Total net position - beginning	23,778,181	18,602,714	8,244,720
Total net position - ending	\$ 23,856,658	\$ 23,778,181	\$ 18,602,714

Operating revenues

Overall operating revenues decreased \$294,000 (1%) in 2012 and increased \$1.1 million (2%) in 2011.

The following graph provides a comparison of operating revenue sources for each of the three years:

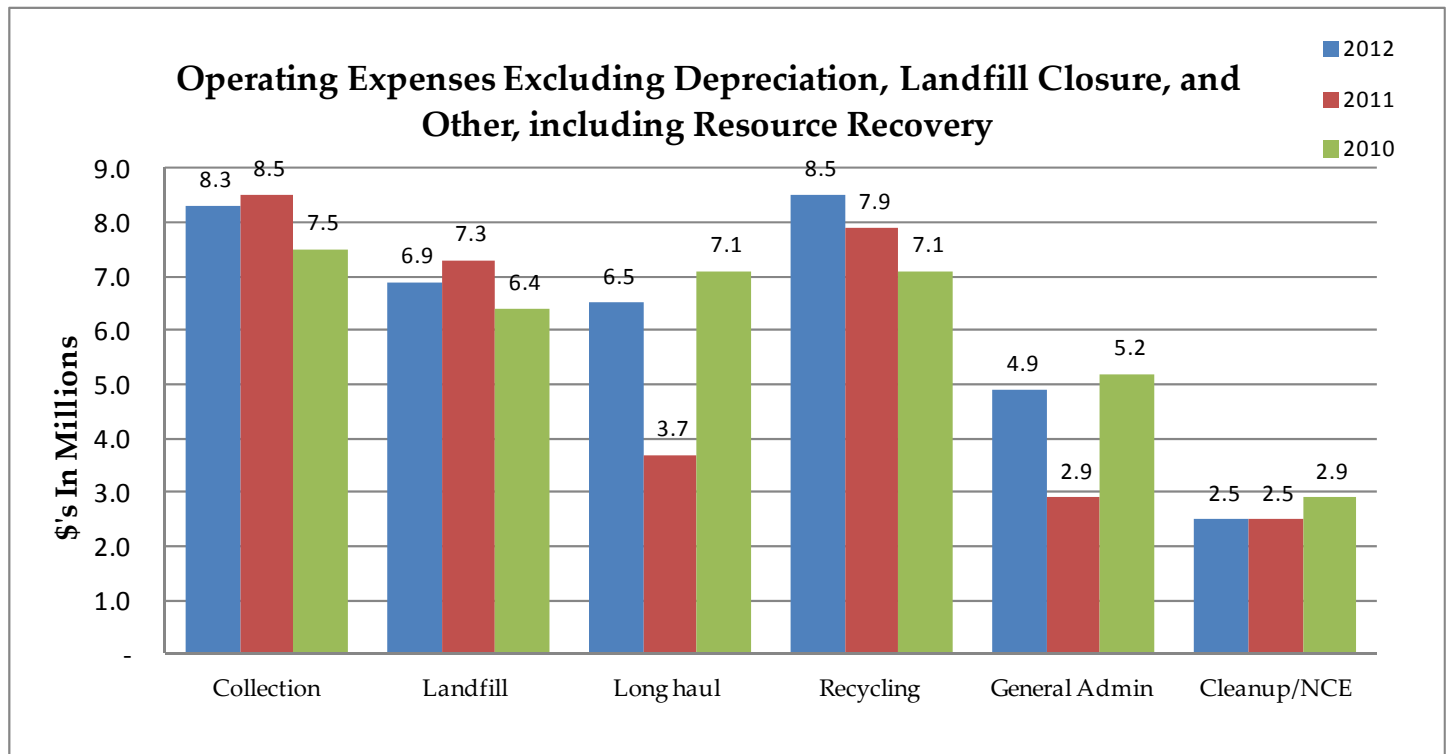


Revenues from residential customers increased \$738,000 (3%) in 2012 and \$244,000 (1%) in 2011. Although average revenue rates increased 2.8% in each of the years 2012 and 2011, overall revenues are down due to reduced volumes and residential volume based rates. Commercial collection revenues increased \$120,000 (1%) in 2011 compared to a decrease of \$627,000 (3%) in 2010.

Salvage revenues decreased \$866,000 in 2012 due to fluctuations in both volumes and prices of salvaged materials. In 2011 salvage revenues continue to increase, \$681,000. This represents increased recycling effort and sales of recycling materials.

Operating expenses

The following graph provides a three year comparison of operating expenses for the major cost center groups.



2012 Activity

Operating expenses were \$50.1 million in 2012, an increase of \$4.6 million (10%). Significant changes in operating costs include the following:

- Collection expenses include both commercial and residential collection. These costs decreased \$208,000 (2%) in 2012; including a decrease of \$286,000 related to labor costs.
- Landfill expenses include costs to maintain the landfill and process the disposal of solid waste; specifically, this includes public receiving, the scale-house, and on-site transfer. Costs decreased \$404,000 in 2012 due to lower labor cost related to closing the landfill in 2013.
- Landfill closure and post closure liability adjustments increased \$1.3 million in 2012 .
- Long haul includes both the transfer and disposal of solid waste to the site in Pierce County. Long haul expenses increased \$2.8 million (75%) in 2012 after the decrease of \$3.4 million in 2011.
- Recycling expenses increased \$581,000 (7%) in 2012 due primarily to increases in recycling activity. The increase included \$100,000 for labor costs and \$481,000 for internal services provided from other departments.
- General administration expenses increased \$2.0 million in 2012. Significant changes include \$1.6 million decrease in capitalized administration and general (A&G costs) to capital projects, and an increase of \$238,000 in labor costs. Capitalized A&G costs were \$1.8 million in 2011.

2011 Activity

Operating expenses were \$45.5 million in 2011, an increase of \$7.1 million (19%). Significant changes in operating costs include the following:

- Collection expenses increased \$1.0 million (13%) included \$219,000 related to labor costs and \$765,000 related to Fleet services, including a \$208,000 increase in fuel cost.
- Landfill expenses include costs to maintain the landfill and process the disposal of solid waste; specifically, this includes public receiving, the scale-house, on-site transfer, and environmental systems. Costs increased \$12.3 million.
 - Landfill closure and post closure liability adjustments costs increased by \$2.1 million.

- Landfill costs excluding the liability adjustments totaled \$7.3 million. The \$934,000 increase in 2011 was due to utilizing the City's landfill as opposed to the Pierce County landfill.
- Long haul expenses decreased \$3.4 million (48%). These decreases are due to the Division discontinuing the transfer of solid waste to the Pierce County landfill and instead using the remaining capacity at the City's landfill.
- Recycling expenses increased \$813,000 (11%) due primarily to increases in recycling sales activity.
- General administration expenses decreased \$2.3 (44%) million. Significant changes include \$1.8 million capitalized administration and general (A&G costs) to capital projects.

Nonoperating revenues (expenses)

Investment earnings were \$775,000 in 2012 and \$1.7 million in 2011, a decrease of \$923,000 primarily due to a loss in the GASB 31 mark to market adjustment; \$22,000 in 2012 compared to \$531,000 in 2011. Additionally, 2012 investment income was \$351,000 less than in 2011. These decreases in 2012 were primarily the result of lower interest rates and decreases in the cash and equity investment pool balances from the prior year.

Interest paid net of capitalized interest on revenue bonds was \$3.3 million, an increase \$130,000 in 2012 compared to 2011. Bond interest decreased \$400,000 due to calling the 2001 Revenue and Refunding Bonds in 2011 and capitalized interest expense decreased \$571,000 due to reduced capital spending in 2012. Interest expense on revenue bonds decreased \$682,000 in 2011 compared to 2010.

Contributions

The General Fund transferred \$901,000 to the Division to refund a portion of assessments for the Radio and Third-Party Liability funds.

Capital Assets

As the end of 2012, the Division's total capital assets, net of accumulated depreciation is \$84.3 million compared to \$89.1 million in 2011 and \$66.5 million in 2010. (See Note 3 for detailed activity.)

2012 Activity

- Land increased \$196,000 due to the purchase of land to be used for constructing a retaining water pond at the City's landfill.
- Construction work-in-process was capitalized to the following building assets: \$500,000 to the transfer station, \$280,000 to the landfill administrative building, and \$139,000 to the Urban Water's building. Buildings also decreased \$180,000 due to the demolition of a building on the Urban Water's property to clear the land for a parking lot.
- Landfill infrastructure additions include \$57,000 for a parking lot and completion of the Gas Extraction System project for \$378,000.
- Machinery and equipment decreased a net \$537,000 due to purchases of vehicles for \$721,000, containers for \$1.1 million and disposals of \$1.9 million for vehicles and \$516,000 for containers.

2011 Activity

Projects completed in 2011 include the Landfill Administration Building for \$10.1 million, the Transfer Station Facility for \$26.7 million and the EPS Recycling Facility for \$350,000. Machinery and equipment increased a net \$334,000 including purchases of vehicles for \$1.1 million and purchases of containers for \$721,000. Disposals include \$1.3 million for vehicles and \$201,000 for containers. Construction work in progress decreased \$10.5 million as a result of \$37.2 million in projects completed and transferred to assets.

Debt Administration

At December 31, 2012, the Division had \$65.5 million in long-term debt of which \$2.6 million is due within one year. This compares to long-term debt of \$68.2 million in 2011 and \$76.9 million in 2010. The bonds have underlying ratings of A2 by Moody's Investors Service, AA by Standard & Poor's, and AA- by Fitch, Inc. (See Note 4).

Debt Service Coverage

The bond coverage ratio is 2.76 at the end of 2012. This compares to 2.83 in 2011 and 2.15 in 2010. Bond coverage calculations are based on bond covenants. A bond coverage ratio of 1.25 is required by bond covenants for the Division.

Summary

This Management's 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, as well as the financial statements and notes.

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Financial Statements

**City of Tacoma
Environmental Services Department
Solid Waste Management
Statement of Net Position**

	December 31,	
ASSETS	2012	2011
Current assets:		
Cash and equity in pooled investments	\$ 29,929,817	\$ 25,124,357
Rate stabilization cash in pooled investments	4,650,000	4,650,000
Accounts receivable	6,837,345	6,895,808
Allowance for uncollectible accounts	(3,671,549)	(3,510,395)
Unbilled revenue	3,065,000	2,800,000
Due from other funds	25,550	117,116
Due from other governmental units	143,024	142,014
Total current assets	40,979,187	36,218,900
Restricted cash and equity in pooled investments:		
Bond reserve and debt service accounts	2,112,422	2,005,771
Customer deposits	63,865	54,314
Bond construction funds	3,691,786	9,384,668
Reserve for landfill closure	2,780,404	2,780,404
Total restricted cash and equity in pooled investments	8,648,477	14,225,157
Capital assets:		
Land	3,104,443	2,908,178
Buildings	63,892,674	63,150,344
Building - capital lease	7,568,000	7,568,000
Landfill infrastructure	62,460,597	62,025,839
Machinery and equipment	40,672,137	41,209,519
Computer software	4,368,980	4,212,330
Less: accumulated depreciation	(98,044,445)	(93,612,961)
Assets in service net of depreciation	84,022,386	87,461,249
Construction in progress	243,292	1,610,598
Total capital assets	84,265,678	89,071,847
Other noncurrent assets	1,649,554	2,032,034
TOTAL ASSETS	\$ 135,542,896	\$ 141,547,938

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

City of Tacoma
Environmental Services Department
Solid Waste Management
Statement of Net Position

	December 31,	
LIABILITIES	2012	2011
Current liabilities:		
Accounts payable	\$ 1,843,714	\$ 3,251,624
Accrued wages payable	543,292	497,816
Compensated absences	114,671	243,986
Accrued taxes payable	613,743	679,732
Due other funds	685,152	723,247
Deferred revenue	212,453	165,930
Customer deposits	-	21,287
Deferred credit - rate stabilization	4,650,000	4,650,000
Current portion of long-term debt	2,387,917	2,154,167
Current portion of capital lease obligation	144,499	139,416
Environmental liabilities	-	334,037
Total current liabilities	11,195,441	12,861,242
Liabilities payable from restricted assets:		
Deposits payable	61,920	54,314
Bond interest payable	271,798	283,547
Current portion of long-term debt	217,083	195,833
Current portion of landfill closure	3,000,000	2,457,147
Total liabilities payable from restricted assets	3,550,801	2,990,841
Noncurrent liabilities:		
Long-term debt - revenue bonds	62,860,169	65,807,497
Capital lease obligation	7,011,502	7,156,001
Compensated absences	1,032,037	1,087,692
Net OPEB obligation	1,100,674	911,469
Accrued landfill closure and post closure costs	24,935,614	26,955,015
Total noncurrent liabilities	96,939,996	101,917,674
Total liabilities	111,686,238	117,769,757
NET POSITION		
Net investment in capital assets	23,087,873	28,641,409
Restricted for bond reserves	1,623,541	1,849,648
Unrestricted	(854,756)	(6,712,876)
Total net position	23,856,658	23,778,181
TOTAL LIABILITIES AND NET POSITION	\$ 135,542,896	\$ 141,547,938

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

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City of Tacoma
Environmental Services Department
Solid Waste Management
Statements of Revenues, Expenses, and Changes in Net Position

	Year End December 31,	
	2012	2011
OPERATING REVENUES		
Residential collection	\$ 26,947,597	\$ 26,209,307
Commercial collection	23,046,935	23,120,799
Disposal revenues	4,563,482	4,662,287
Salvage revenue	1,358,164	2,224,626
Other operating revenue	891,344	884,930
Total operating revenues	<u>56,807,522</u>	<u>57,101,949</u>
OPERATING EXPENSES		
Collection	8,275,088	8,483,151
Landfill	6,921,880	7,325,498
Landfill closure and post closure adjustment	1,258,777	2,056,384
Long haul	6,478,638	3,703,535
Recycling	8,472,020	7,890,874
Tacoma cares/NCE	2,451,490	2,520,799
General administration	4,929,576	2,899,551
Other	4,466,250	4,492,974
Depreciation	6,855,008	6,100,299
Total operating expenses	<u>50,108,727</u>	<u>45,473,065</u>
Net operating income	<u>6,698,795</u>	<u>11,628,884</u>
NONOPERATING REVENUES (EXPENSES)		
Investment income	774,934	1,698,012
Rental income	125,341	123,949
Operating grants	251,468	247,352
Interest on revenue bonds, net of capitalized interest	(3,344,432)	(3,214,931)
Interest on capital lease	(388,163)	(388,608)
Amortization of premium, discount issuance, and refunding costs	(40,153)	(134,227)
Other revenues	39,750	20,966
Other expenses	(242,345)	(154,718)
Total nonoperating expenses	<u>(2,823,600)</u>	<u>(1,802,205)</u>
CHANGE IN NET POSITION		
Net position before transfers	3,875,195	9,826,679
Transfers - gross earnings taxes	(4,544,348)	(4,651,212)
Transfers - from other funds	900,630	-
Transfers - Fleet Equipment Fund	(153,000)	-
CHANGE IN NET POSITION	<u>78,477</u>	<u>5,175,467</u>
TOTAL NET POSITION - BEGINNING	<u>23,778,181</u>	<u>18,602,714</u>
TOTAL NET POSITION - ENDING	<u>\$ 23,856,658</u>	<u>\$ 23,778,181</u>

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

**City of Tacoma, Washington
Environmental Services Department
Solid Waste Management
Statements of Cash Flows**

	Year Ended December 31,	
	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	\$ 56,270,615	\$ 56,810,216
Payments to suppliers	(27,143,646)	(21,738,477)
Payments to employees	(17,838,581)	(17,593,612)
Taxes paid	(1,007,521)	(991,519)
Net cash from operating activities	10,280,867	16,486,608
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Gross earnings taxes paid	(4,582,951)	(4,639,504)
Fund transfer from other funds	900,630	-
Debt service related to environmental cleanup	(331,104)	(175,804)
Operating grants received	291,820	176,338
Net cash from noncapital financing activities	(3,721,605)	(4,638,970)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets	(2,367,800)	(28,686,091)
Principal payments on revenue bonds	(2,350,000)	(8,305,000)
Interest paid on revenue bonds	(3,025,106)	(3,077,569)
Capital lease obligation	(527,579)	(522,108)
Proceeds from sale of capital assets	39,750	17,072
Net cash from capital and related financing activities	(8,230,735)	(40,573,696)
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment income received	774,934	1,698,012
Rental income	125,341	123,949
Other, net	(22)	(38,535)
Net cash from investing activities	900,253	1,783,426
Net change in cash and equity in pooled investments	(771,220)	(26,942,632)
Cash and equity in pooled investments beginning	43,999,514	70,942,146
Cash and equity in pooled investments ending	\$ 43,228,294	\$ 43,999,514

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

City of Tacoma, Washington
Environmental Services Department
Solid Waste Management
Statements of Cash Flows

	Year Ended December 31,	
	2012	2011
Reconciliation of cash and equity in pooled investments to balance sheets:		
Operating funds	\$ 34,579,817	\$ 29,774,357
Restricted funds	8,648,477	14,225,157
	\$ 43,228,294	\$ 43,999,514
Reconciliation of operating income to net cash from operating activities:		
Operating income	\$ 6,698,795	\$ 11,628,884
Adjustments to reconcile operating income to net cash from operating activities:		
Depreciation expense	6,855,008	6,100,299
Low income assistance	(76,334)	(93,908)
Change in assets and liabilities:		
Accounts receivable, net of allowance	219,617	90,285
Unbilled revenue	(265,000)	300,000
Due from other funds	91,566	(104,034)
Due from other governmental units	(41,362)	(50,329)
Accounts payable	(1,407,910)	1,187,269
Accrued wages and compensated absences	(139,493)	39,909
Accrued taxes payable	(27,387)	5,588
Environmental liabilities	(334,037)	(605,215)
Deposits payable	(13,681)	6,678
Due other funds	(38,095)	(241,355)
Deferred revenue	46,523	(27,793)
Net OPEB obligation	189,205	206,000
Closure and post-closure liability	(1,476,548)	(1,955,670)
Total adjustments	3,582,072	4,857,724
Net cash from operating activities	\$ 10,280,867	\$ 16,486,608

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
Solid Waste Management
Notes to Financial Statements
Years Ended December 31, 2012 and 2011

NOTE 1 SUMMARY OF OPERATIONS

OPERATIONS OF THE SOLID WASTE MANAGEMENT DIVISION - The Solid Waste Management Division (the Division) is presented as an enterprise fund within the Department of Public Works under the provisions of the City of Tacoma Charter and is included in the City's Comprehensive Annual Financial Report (CAFR).

The Division provides mandatory solid waste collection and disposal services for residential and commercial entities located within the City. The population is approximately 200,000 and covers an area of 49 square miles. Disposal methods include recycling, long-haul to an outside landfill, and disposal in the City owned landfill.

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

CASH AND EQUITY IN POOLED INVESTMENTS - The Division's fund cash balances are a "deposit" with the City Treasurer's Tacoma Investment Pool (TIP) for the purpose of maximizing interest earnings through pooled investment activities. Cash and equity in pooled investments in the TIP are reported at fair value and changes in unrealized gains and losses are recorded in the Statements of Revenues, Expenses and Changes in Net Position. Interest earned on such pooled investments is allocated daily to the participating funds based on each fund's daily equity in the TIP.

The TIP operates like a demand deposit account in that all City departments, including the Division, have fund balances which are their equity in the TIP. Accordingly, balances are considered to be cash equivalents.

The City of Tacoma Investment Policy permits legal investments as authorized by state law including Certificates of Deposit with qualified public depositories (as defined in Chapter 39.58 RCW), obligations of the U.S. Treasury, Government Sponsored Agencies and Instrumentalities, bonds issued by Washington State and its Local Governments with an A or better rating, general obligation bonds issue by any State or Local Government with an A or better rating, Bankers' Acceptances, Commercial Paper, Repurchase and Reverse Repurchase agreements, and the Washington State Local Government Investment Pool (LGIP).

Solid Waste Management

Notes to Financial Statements Continued

Daily liquidity requirement to meet the City's daily obligations is maintained by investing a portion of the City's 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 City's TIP held in qualified public depositories at December 31, 2012 and 2011 is entirely covered by the Federal Deposit Insurance Corporation (FDIC) and the Washington State Public Deposit Protection Commission (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 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 and Demand Deposit Accounts are protected by the FDIC insurance up to \$250,000. All CS 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 Comprehensive Annual Financial Report (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 DOUBTFUL ACCOUNTS - A reserve has been established for uncollectible accounts receivable based on historical write-off trends and knowledge of specific circumstances that indicate collection of an account may be unlikely. Generally accounts receivable are considered past due after 30 days.

INTERDIVISION TRANSACTIONS - Unsettled transactions between funds at year end are recorded as due to or due from other funds.

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

Solid Waste Management

Notes to Financial Statements Continued

BOND PREMIUM, ISSUANCE COSTS AND LOSS ON REFUNDING - Bond premium, discount and issuance costs are amortized over the life of the bonds using the weighted average of the bonds outstanding. Losses on refunding are amortized on a straight-line basis over the applicable bond period.

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.

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
Structures and Improvements	20 - 50
Resource Recovery Facility	5 - 50
Vehicles	5 - 10
Containers and Equipment	5 - 10
Other Assets	3 - 10

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.

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

Solid Waste Management

Notes to Financial Statements Continued

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.

OPERATING REVENUE - Revenues are derived from providing solid waste services to both residential and commercial customers. Residential rates are based on the size of the garbage container and include services for recycling, yard waste and costs for other special programs. Commercial rates are based on the garbage container type and frequency of collection with additional charges for recycling services. Customers are billed on bi-monthly or monthly billing cycles.

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.

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 to 1) pay the cost of maintenance and operation of the utility, 2) to make all payments required to be made for the parity bonds, 3) to make all payments required to be made on any other junior debt, 4) to pay municipal taxes and payments to the City in lieu of taxes, and 5) to prepay debt, invest in improvement projects to utility assets, make payments to the Solid Waste Rate Stabilization Fund, or other lawful City purposes including payment of legal claims and judgments against the utility.

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 8.00%. The Division also pays business and occupation taxes to the State, 1.80% on service revenues and 0.47% on rental revenues. The Division is exempt from payment of federal income tax.

Solid Waste Management

Notes to Financial Statements Continued

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

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

Restricted net position is 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".

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.

LANDFILL CLOSURE AND POST-CLOSURE COSTS - The Division is required to expense a portion of the estimated closure and post-closure costs in each period that the landfill accepts solid waste. The Division has been reporting a portion of these costs as a liability and as an operating expense since 1994.

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.

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 accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. The Division used estimates in determining reported unbilled revenues, allowance for doubtful accounts, accrued compensated absences, depreciation, OPEB, self-insurance liabilities and other contingencies. Actual results may differ from these estimates.

Solid Waste Management

Notes to Financial Statements Continued

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.

NOTE 3 CAPITAL ASSETS

A summary of the balances and changes in capital assets for 2012 and 2011 is as follows:

	2011	Additions	Retirements	Transfers & Adjustments	2012
Nondepreciable:					
Land	\$ 2,908,178	\$ -	\$ -	\$ 196,265	\$ 3,104,443
Depreciable:					
Buildings	63,150,344	-	(180,000)	922,330	63,892,674
Building - capital lease	7,568,000	-	-	-	7,568,000
Landfill infrastructure	62,025,839	-	-	434,758	62,460,597
Machinery and equipment	41,209,519	-	(2,409,485)	1,872,103	40,672,137
Computer software	4,212,330	-	-	156,650	4,368,980
Assets in service	181,074,210	-	(2,589,485)	3,582,106	182,066,831
Accumulated depreciation	(93,612,961)	(6,855,008)	2,423,524	-	(98,044,445)
Assets in service					
net of depreciation	87,461,249	(6,855,008)	(165,961)	3,582,106	84,022,386
Construction in progress	1,610,598	2,214,800	-	(3,582,106)	243,292
Total capital assets	<u>\$ 89,071,847</u>	<u>\$ (4,640,208)</u>	<u>\$ (165,961)</u>	<u>\$ -</u>	<u>\$ 84,265,678</u>

Solid Waste Management
Notes to Financial Statements Continued

	2010	Additions	Retirements	Transfers & Adjustments	2011
Nondepreciable:					
Land	\$ 2,908,178	\$ -	\$ -	\$ -	\$ 2,908,178
Depreciable:					
Buildings	25,985,266	-	-	37,165,078	63,150,344
Building - capital lease	7,568,000	-	-	-	7,568,000
Landfill infrastructure	62,017,969	-	-	7,870	62,025,839
Machinery and equipment	40,875,023	1,833,106	(1,498,610)	-	41,209,519
Computer software	4,078,271	108,852	-	25,207	4,212,330
Assets in service	143,432,707	1,941,958	(1,498,610)	37,198,155	181,074,210
Accumulated depreciation	(88,993,489)	(6,100,299)	1,480,827	-	(93,612,961)
Assets in service net of depreciation	54,439,218	(4,158,341)	(17,783)	37,198,155	87,461,249
Construction in progress	12,064,623	26,744,130	-	(37,198,155)	1,610,598
Total capital assets	<u>\$ 66,503,841</u>	<u>\$ 22,585,789</u>	<u>\$ (17,783)</u>	<u>\$ -</u>	<u>\$ 89,071,847</u>

NOTE 4 LONG-TERM DEBT

Long-term debt activity for the years ended December 31, 2012 and 2011 is as follows:

	2011	Additions	Reductions	2012	Due within One Year
Revenue bonds	\$ 66,105,000	\$ -	\$ (2,350,000)	\$ 63,755,000	\$ 2,605,000
Plus: Unamortized premium	2,057,755	-	(347,586)	1,710,169	-
Less: Unamortized discount	(5,258)	-	5,258	-	-
Total long-term debt	<u>\$ 68,157,497</u>	<u>\$ -</u>	<u>\$ (2,692,328)</u>	<u>\$ 65,465,169</u>	<u>\$ 2,605,000</u>

	2010	Additions	Reductions	2011	Due within
Revenue bonds	\$ 74,410,000	\$ -	\$ (8,305,000)	\$ 66,105,000	\$ 2,350,000
Plus: Unamortized premium	2,465,150	-	(407,395)	2,057,755	-
Less: Unamortized discount	(15,950)	-	10,692	(5,258)	-
Total long-term debt	<u>\$ 76,859,200</u>	<u>\$ -</u>	<u>\$ (8,701,703)</u>	<u>\$ 68,157,497</u>	<u>\$ 2,350,000</u>

Solid Waste Management Notes to Financial Statements Continued

The Division's long-term debt at December 31, 2012 consists of the following payable from revenues of the Division.

	2012	2011
1997 Series B Revenue Refunding Bonds, with an interest rate of 6.0% due in 2012. Original par value \$60,370,000. Purpose was to refund all of the outstanding debt except the notes.	\$ -	\$ 2,350,000
2006 Series A Revenue Bonds, with interest rates ranging from 4.25% to 5.0%. Principal payments range between \$540,000 to \$4,290,000 between 2017 and 2026. Original par value value \$29,385,000 with a call date of December 1, 2016. Purpose was to fund a portion of the capital improvement plan and pay the costs of issuance.	29,385,000	29,385,000
2006 Series B Revenue Refunding Bonds, with an interest rate of 5.0% due in yearly installments of \$340,000 to \$6,480,000 from 2014 through 2021. Original par value \$22,315,000 with a call date of December 1, 2016. Purpose was to refund certain maturities of the outstanding 2001 Bonds and to pay the cost of issuance.	22,315,000	22,315,000
2008 Revenue Refunding Bonds, with an interest rate of 5.75% due in yearly installments of \$2,150,000 to \$2,685,000 from 2013 through 2017. Original par value \$12,055,000. Purpose was to refund a portion of the 1997 Series B Bonds and to pay the costs of issuance.	12,055,000	12,055,000
Total revenue bonds outstanding	63,755,000	66,105,000
Less:		
Unamortized discount	-	(5,258)
Current portion	(2,387,917)	(2,154,167)
Current portion payable from restricted assets	(217,083)	(195,833)
Plus: Unamortized premium	1,710,169	2,057,755
Total long-term debt - Revenue Bonds	\$ 62,860,169	\$ 65,807,497

Annual debt service requirement to maturity are as follows:

	Principal	Interest	Total Debt Service
2013	\$ 2,605,000	\$ 3,261,556	\$ 5,866,556
2014	3,085,000	3,118,594	6,203,594
2015	4,585,000	2,950,881	7,535,881
2016	4,830,000	2,707,306	7,537,306
2017	5,090,000	2,449,938	7,539,938
2018-2022	27,590,000	7,958,500	35,548,500
2023-2026	15,970,000	2,045,000	18,015,000
	\$ 63,755,000	\$ 24,491,775	\$ 88,246,775

Solid Waste Management Notes to Financial Statements Continued

The fair value of the Division's revenue bonds is based on quoted market prices. At December 31, 2012, the fair market value of revenue bonds debt was \$70,323,156 and at December 31, 2011 it was \$74,292,542.

Moody's Investors Service, Standard & Poor's and Fitch Ratings have assigned ratings of "A2," "AA" and "AA-", 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, 2012, 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 2012 or 2011.

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 Public Works utilities 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%). The three utilities have included their pro-rata share of the capital lease and lease obligation for the building in their respective financial statements.

The three utilities 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 utilities' balance sheets to a deferred asset. All assets revert to the City at the end of the lease.

Solid Waste Management

Notes to Financial Statements Continued

The future payments of the lease obligation as of December 31, 2012 total \$67,860,500. The Division's portion of the lease obligation is presented in the following table:

Year	Division
2013	\$ 521,726
2014	521,966
2015	521,966
2016	521,726
2017	522,246
2018-2022	2,610,656
2023-2027	2,610,076
2028-2032	2,610,193
2033-2037	2,609,756
2038	521,788
	\$ 13,572,099

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 with the possibility of five year extensions. The revenues 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 Division's risk exposure includes but is not limited to injuries and property damage due to collection and transfer activities, groundwater contamination, chemical spills and asset damage from earthquakes. Mitigating controls, safety procedures, 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 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 is required to make payments to the Self-Insurance Fund to cover claims incurred by the Division and administrative expenses of the Fund.

The Division's premium payments totaled \$346,748 for 2012 and \$346,748 for 2011. The Division only recognizes expense for premium payments because the risk of loss transfers to the Self-insurance Fund. Additionally, the City maintains an excess general liability policy with limits of \$15 million, subject to a self-insured retention of \$3 million.

The City has an excess policy to cover extraordinary workers' compensation claims with Statutory Limits (formally \$25 million) and with a (\$1 million self-insured retention), and a property insurance policy with a limit of \$500 million replacement cost (\$100,000 deductible per occurrence). Earthquake coverage has a three percent per building self-insured retention.

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 Self-insurance Fund.

Solid Waste Management

Notes to Financial Statements Continued

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

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

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

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

BENEFITS - There are two formulas that are used for calculating retirement benefits. The benefit will be determined on the formula which provides the higher benefit. The most commonly applied formula, "service retirement", is a product of the member's average monthly salary for the highest consecutive 24-month period, the number of years of membership credit, and a percentage factor (2% maximum) that is determined based on the member's age and years of service. Several options are available for the retiree to provide for their beneficiaries. The System also provides death and disability retirement.

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

<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

Solid Waste Management Notes to Financial Statements Continued

Contributions city-wide totaled \$43.1 million in 2012 (\$22.7 million employer contributions and \$20.4 million employee contributions) and totaled \$42.4 million in 2011 (\$22.5 million employer contributions and \$19.9 million employee contributions).

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

Schedule of Funding Progress (\$ in millions):

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

ACTUARIAL METHODS AND SIGNIFICANT ACTUARIAL ASSUMPTIONS

Actuarial Methods and Significant Actuarial Assumptions:

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

Solid Waste Management

Notes to Financial Statements Continued

ANNUAL PENSION COST AND NET PENSION OBLIGATION - The City's annual pension cost and net pension obligation to the Retirement System for 2012 were as follows:

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

Trend Information

(\$ in millions)

Year Ending December 31,	Annual Required Contribution (ARC) (a)	Annual Net Pension Obligation (NPO) (b)	Annual ARC Adjustment (c)	Annual Pension Cost (APC) (d) = (a) + (b) - (c)	Total Employer Contributions (e)	Change in NPO (f) = (d) - (e)	NPO Balance (g) = (f) + PY	% of APC Contributed (h) = (e) / (d)
2010	\$ 17.1	\$ (0.3)	\$ (0.2)	\$ 17.0	\$ 21.3	\$ (4.3)	\$ (8.1)	125%
2011	\$ 17.1	\$ (0.6)	\$ (0.4)	\$ 16.9	\$ 22.5	\$ (5.6)	\$ (13.7)	133%
2012	\$ 22.7	\$ (1.1)	\$ (1.3)	\$ 22.9	\$ 22.7	\$ 0.2	\$ (13.5)	99%

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. Generally accepted accounting principles require that the portion of age-adjusted expected retiree health claims costs that exceed the premium charged to retirees be recognized as a liability for accounting purposes. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and are subject to continual revision as results are compared to past expectation and new estimates are made about the future.

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

ANNUAL OPEB COST AND NET OPEB OBLIGATION - The Present Value of Benefits (PVB) is the present value of projected benefits discounted at the valuation interest rate (4.00%).

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

Solid Waste Management

Notes to Financial Statements Continued

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

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

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

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

	<u>January 1, 2009</u>	<u>January 1, 2011</u>
Total membership:		
Active employees	3,633	3,675
Terminated vested employees	355	363
Retired employees & Dependents	815	790
Total	<u>4,803</u>	<u>4,828</u>
Annual Benefit Payments	\$ 8,319,788	\$ 9,569,648
Discount rate	4.00%	4.00%
Present Value of Benefits (PVB)	\$ 266,167,781	\$ 319,550,419
Actuarial Accrued Liability (AAL)	\$ 205,168,072	\$ 248,571,791
Assets	\$ -	\$ -
Unfunded Actuarial Accrued Liability (UAAL)	<u>\$ 205,168,072</u>	<u>\$ 248,571,791</u>
Normal Cost	\$ 5,615,626	\$ 5,559,351
Annual Required Contribution (ARC)	\$ 16,761,978	\$ 19,734,041

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

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

Solid Waste Management Notes to Financial Statements Continued

The following table shows the calculation of the Annual Required Contribution and Net OPEB Obligation for the City and for the Division as of December 31, 2012.

	City	Division
Determination of Annual Required Contribution:		
Normal Cost at Year-end	\$ 5,559,351	\$ 254,536
Amortization of UAAL	14,174,690	94,768
Annual Required Contribution (ARC)	<u>\$ 19,734,041</u>	<u>\$ 349,304</u>
Determination of Net OPEB Obligation:		
Annual Required Contribution (ARC)	\$ 19,734,041	\$ 349,304
Interest on prior year Net OPEB Obligation	1,455,746	36,459
Adjustments to ARC	<u>(1,720,609)</u>	<u>(35,418)</u>
Annual OPEB Cost	19,469,178	350,345
Actual benefits paid	<u>9,393,431</u>	<u>161,140</u>
Increase in Net OPEB Obligation	10,075,747	189,205
Net OPEB Obligation - beginning of year	<u>36,393,621</u>	<u>911,469</u>
Net OPEB Obligation - end of year	<u>\$ 46,469,368</u>	<u>\$ 1,100,674</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.

Year Ended	Annual OPEB Cost		Benefits Paid		Net OPEB Obligation	
	City	Division	City	Division	City	Division
12/31/2010	\$16,700,184	\$ 297,234	\$ 9,206,060	\$ 120,000	\$26,366,848	\$ 705,469
12/31/2011	\$19,596,420	\$ 351,196	\$ 9,569,648	\$ 145,196	\$36,393,620	\$ 911,469
12/31/2012	\$19,469,178	\$ 350,345	\$ 9,393,431	\$ 161,140	\$46,469,368	\$1,100,674

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

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

The portion of the actuarial present value allocated to a valuation year is called the normal cost. The portion of this actuarial present value not provided for at a valuation date by the sum of (a) the actuarial value of the assets, and (b) the actuarial present value of future normal costs is called the Unfunded Actuarial Accrued Liability (UAAL). In determining the Annual Required Contribution, the UAAL is amortized as a level percentage of expected payrolls for non-LEOFF 1 groups. For LEOFF 1, the UAAL is amortized as a level dollar amount. The amortization period was 30 years in 2007 and is now 25 years.

Solid Waste Management Notes to Financial Statements Continued

Actuarial Methods and Significant Actuarial Assumptions:

Valuation DateJanuary 1, 2011
 Census DateJanuary 1, 2011
 Actuarial Cost Method:Entry Age
 Amortization Method:Combination of level percentage and level dollar amount, see note above.
 Remaining Amortization Period:25 years, closed
 Demographic Assumptions:.....Demographic assumptions regarding retirement, disability, and turnover are based upon pension valuations for the various pension plans.

Actuarial Assumptions:

Discount Rate.....4.00% for pay-as-you-go funding
 Medical Cost Trend.....2011 8.1%
 2012 7.3%
 2013 6.6%
 2014-19 6.5%
 2020-27 6.4%
 Grading down to an ultimate of 5.2% in 2082 and beyond.
 Projected Payroll Increases4.25% per year

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 LANDFILL CLOSURE AND POST CLOSURE LIABILITIES

The Division operates a 235 acre landfill site, which became part of the South Tacoma Channel Superfund Site in 1983. In 1991, the City entered a Consent Decree settlement with the United States Environmental Protection Agency (“EPA”) and the Washington State Department of Ecology (“DOE”), titled *United States et al v. City of Tacoma* US District Court Cause No. C-89C583T, to “clean-up” the release of hazardous substances at the Landfill. The City completed the majority of the remediation work required by the Consent Decree several years ago. The remaining work mostly involves monitoring the remediation work completed by the City in the 1990s to assure that it continues to protect human health and the environment. The Consent Decree settlement was entered pursuant to the federal Comprehensive Environmental Response, Compensation, and Liability Act (“CERCLA”), 42 U.S.C. §9601 et seq., and the state Model Toxics Control Act (“MTCA”), Chapter 70.105D RCW.

Solid Waste Management

Notes to Financial Statements Continued

The City's remediation work has included: (1) covering the landfill with a double flexible membrane cap that is impermeable to water; (2) capturing methane gas within and at the landfill perimeter to prevent off-site migration; (3) pumping and treating ground water to remove contamination at the point of compliance and beyond property boundaries; and (4) closing the landfill in accordance with the above-referenced Consent Decree. The City has an obligation under the Consent Decree to monitor the remediation work over the next 20 years, or more years to make sure it continues to be effective at protecting human health and the environment.

Due to the success of the City's groundwater pump and treat system, on February 11, 2009, EPA and DOE granted the City's request to shut down 14 of the Landfill's 19 groundwater extraction wells.

On December 21, 2009, EPA and DOE conditionally approved the City's request for an extension of the Landfill closure date until 2014. One of the conditions is for the City to fill the Landfill's remaining open cell and place a permanent cap over it by December 2014. The City began placing solid waste and fill in the open cell in 2010.

Although future closure and post-closure care costs will be paid only near or after the date the landfill stops accepting waste, the Division began reporting a portion of these future closure and post-closure care costs as an operating expense in 1994 based on landfill capacity used as of the balance sheet date.

The City's Finance Department reports \$27,935,614 as landfill closure and post-closure liability at December 31, 2012 based on 100% use of the total capacity of the landfill. This compares to \$29,412,162 at December 31, 2011 based on 99% of capacity. Based on 100% of capacity, the liability was fully recognized as of December 31, 2012 compared to \$179,067 as of December 31, 2011. Actual costs may be higher or lower due to inflation, changes in technology, or changes in regulations. The City will be responsible for the costs of additional work if migration of pollutants from the site is not completely controlled by current remedial actions.

The Division has determined that the City satisfies the requirements of 40 CFR Part 258 (f) "Local government financial test". To meet the previous requirements of State and Federal laws and regulations, contributions were made to a reserve for financing closure costs. According to the City's Finance Department, the balance as of December 31, 2012 is \$2,780,404 compared to \$2,780,404 in 2011 and is reported as a restricted asset on the balance sheet.

NOTE 10 COMMITMENTS AND CONTINGENCIES

Long-term Contract - Land Recovery, Inc. - In February 2000, the Division entered into a 20-year contract with Land Recovery, Inc. (LRI) to dispose of all "acceptable waste" collected or handled by the Division (as that term is defined in the agreement), at the 304th Street landfill operated by LRI. The Division entered into this agreement to extend the life of the Tacoma Landfill and to secure a long-term disposal arrangement at a favorable disposal cost. The agreement excludes solid waste that LRI is not authorized by law or permit to receive, or which could create or expose LRI or the Division to potential liability, among other things. Recycling and/or composting waste is not covered by the agreement. The agreement further provides that LRI shall charge a base rate per ton for disposal services, and that said rate shall decrease as the tonnage increases during each contract year. The agreement also provides that the base rate charged by LRI shall increase annually based on the Seattle-Tacoma CPI. The rate per ton is periodically increased by LRI to cover certain increased costs, including the increased cost of landfill closure liabilities. These rate adjustments are part of the existing agreement.

Solid Waste Management

Notes to Financial Statements Continued

Long-term Contract - Pierce County Recycling, Composting and Disposal - In October 2004 the Division entered into a ten (10) year agreement with Pierce County Recycling Composting and Disposal (PCRCD) LLC to accept organic material collected by the City curbside or delivered to the City's landfill for processing into compost. Under the agreement, which has two 5-year renewal options, PCRCD will charge a base rate per ton for the organic waste it receives from the City. This price may be adjusted beginning on the second anniversary of the agreement, and thereafter annually based on the Seattle-Tacoma-Bremerton CPI. The agreement also includes a revenue sharing component. The Division entered into this agreement to extend the life of the Tacoma landfill and secure a long-term composting arrangement at a favorable cost.

NOTE 11 LITIGATION

EPA Clean Air Act Penalty Action - During January 2009, the Department of Justice ("DOJ") and EPA notified the City that the Tacoma Landfill had allegedly violated the federal clean air act and its implementing regulation by failing to properly recover ozone-depleting substances between October 2004 and August 2008 from refrigerant-containing appliances which were processed by Landfill staff for disposal. The City resolved any liability it may have had for the alleged violations by entering a Consent Decree settlement with DOJ and EPA in August 2010. Under the terms of the settlement, the City paid the federal government a civil penalty in the amount of \$224,684, and agreed to complete three supplemental environmental projects ("SEPs"). These SEPs include purchasing a hydraulic launch garbage truck and a hybrid electric "yard mule" vehicle and using both for five years and retrofitting ten long-haul trucks with diesel reduction equipment and operating them for five years, or until the end of their useful life, whichever occurs first. The City's cost for the three SEPs was estimated to be \$675,252.

In 2012, the manufacturer of the hybrid electric "yard mule" vehicle notified the City that it had ceased production of the vehicle. In response, the City made a stipulated penalty payment to EPA and DOJ in the amount of \$81,378, in lieu of completing this SEP. The City also had technical issues with the diesel reduction equipment it installed as part of that SEP, which made the continued use of this equipment impractical. EPA and DOJ have been notified, and the City's hope is that further performance of this SEP will be excused, and that any stipulated penalties owing will be waived. EPA and DOJ were notified, and responded to the City on March 28, 2013, excusing further performance of this SEP, including payment of any stipulated penalties that may be owing for failure to fully complete it.

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.

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