

Washington State Auditor's Office
Financial Statements Audit Report

Port of Bremerton
Kitsap County

Audit Period
January 1, 2012 through December 31, 2012

Report No. 1010030

Issue Date
July 1, 2013



WASHINGTON
TROY KELLEY
STATE AUDITOR



**Washington State Auditor
Troy Kelley**

July 1, 2013

Board of Commissioners
Port of Bremerton
Bremerton, Washington

Report on Financial Statements

Please find attached our report on the Port of Bremerton's financial statements.

We are issuing this report in order to provide information on the Port's financial condition.

Sincerely,

TROY KELLEY
STATE AUDITOR

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Kitsap County
January 1, 2012 through December 31, 2012**

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Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

**Port of Bremerton
Kitsap County
January 1, 2012 through December 31, 2012**

Board of Commissioners
Port of Bremerton
Bremerton, Washington

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the Port of Bremerton, Kitsap County, Washington, as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the Port's basic financial statements, and have issued our report thereon dated June 21, 2013. During the year ended December 31, 2012, the Port implemented Governmental Accounting Standards Board Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered the Port's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Port's internal control. Accordingly, we do not express an opinion on the effectiveness of the Port's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Port's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

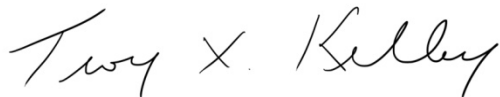
COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the Port's financial statements are free from material misstatement, we performed tests of the Port's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

PURPOSE OF THIS REPORT

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Port's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Port's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.



TROY KELLEY
STATE AUDITOR

June 21, 2013

Independent Auditor's Report on Financial Statements

Port of Bremerton Kitsap County January 1, 2012 through December 31, 2012

Board of Commissioners
Port of Bremerton
Bremerton, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the Port of Bremerton, Kitsap County, Washington, as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the Port's basic financial statements as listed on page 5.

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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 Port'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 Port'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 we have 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 Port of Bremerton, as of December 31, 2012, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Matters of Emphasis

As discussed in Note 1 to the financial statements, in 2012, the Port adopted new accounting guidance, Governmental Accounting Standards Board Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. Our opinion is not modified with respect to this matter.

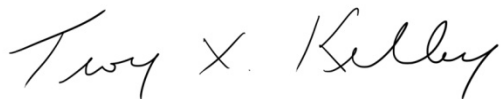
Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 6 through 11 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated June 21, 2013 on our consideration of the Port's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Port's internal control over financial reporting and compliance.



TROY KELLEY
STATE AUDITOR

June 21, 2013

Financial Section

**Port of Bremerton
Kitsap County
January 1, 2012 through December 31, 2012**

REQUIRED SUPPLEMENTARY INFORMATION

Management's Discussion and Analysis – 2012

BASIC FINANCIAL STATEMENTS

Statement of Net Position – 2012

Statement of Revenues, Expenses and Changes in Fund Net Position – 2012

Statement of Cash Flows – 2012

Notes to Financial Statements – 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

Years ended December 31, 2012 and 2011

INTRODUCTION:

This document is the Port of Bremerton's (Port) Management Discussion and Analysis (MD&A) of financial activities and performance for the calendar years ended December 31, 2012 and 2011. It provides an introduction to the Port's 2012 financial statements. Information contained in this MD&A has been prepared by Port management and should be considered in conjunction with the financial statements and the notes to the financial statements.

The notes are essential to a full understanding of the data contained in the financial statements. This report also presents certain required supplementary information regarding capital assets and long-term debt activity during the year, including commitments made for capital expenditures.

OVERVIEW OF THE FINANCIAL STATEMENTS:

The financial section of this annual report consists of three parts: MD&A, the basic financial statements, and the notes to the financial statements. The basic financial statements include: the Statement of Net Position, the Statement of Revenues, Expenses and Changes in Fund Net Position, and the Statement of Cash Flows. This report also includes statistical and economic data and bond information.

Analysis of the Statement of Net Position and the Statement of Revenues, Expenses and Changes in Fund Net Position illustrate whether the Port's financial position has improved as a result of the year's activities. The Statement of Net Position presents information on all of the Port's assets and liabilities, with the difference between the two reported as net position. Over time the increases and decreases in net position may serve as an indicator of whether the financial position of the Port is improving or deteriorating. The Statement of Revenues, Expenses and Changes in Fund Net Position reflect how the operating and non-operating activities of the Port affected changes in the net position of the Port. These activities are recorded under the accrual basis of accounting reflecting the timing of the underlying event regardless of the timing of related cash flows.

Although the financial statements provide useful information in assessing the financial health of the Port, consideration of other factors not shown on the financial reports should be evaluated to assess the Port's true financial condition. Factors such as changes in the Port's tax base and the condition of the Port's asset base are also important when assessing the overall financial condition of the Port.

Government entities typically account for activities by utilizing “fund” accounting. A fund is a grouping of related accounts that is used to maintain control or restrict the use of resources that have been segregated for specific activities or objectives. The Port uses only one fund, an enterprise fund, which reports all business type activities of the Port.

FINANCIAL ANALYSIS OF THE PORT

- Port assets exceeded liabilities by \$77.9 million at the close of 2012 and by \$72.9 million in 2011. Of this amount, \$63.4 million in 2012 and \$62.8 million in 2011 are invested in capital assets, net of related debt.
- The Port’s net assets increased in 2012 over 2011 by \$4,768,776 before recording a prior period adjustment of \$291,521, compared to the increase in 2011 of \$3,903,324 with a prior period adjustment of \$(481,891). The 2012 increase reflects the reduction in Port debt.
- The Port’s long-term debt decreased by \$229,731 in 2012 and by \$4,264,877 in 2011. Both 2012 and 2011 decreases resulted from debt payments on the bonds and loans.
- Operating revenues for 2012 and 2011 totaled \$3,372,277 and \$3,342,189 respectively.
- Operating expenses totaled \$7,631,111 for 2012 and \$7,711,816 for 2011.

PORT OF BREMERTON’S CONDENSED STATEMENT OF NET POSITION:

	2012	2011
Current assets	\$ 12,417,839	\$ 8,242,295
Restricted assets	963,131	2,748,772
Net capital assets	67,951,701	71,351,015
Non-current assets	2,969,439	10,209
Total assets	\$ 84,302,110	\$ 82,352,291
Current liabilities	\$ 2,037,104	\$ 4,917,850
Long-term liabilities	4,337,809	4,567,540
Total liabilities	\$ 6,374,913	\$ 9,485,390
Net position:		
Investment in capital assets	\$ 63,299,314	\$ 62,712,500
Restricted for capital projects	751,329	842,948
Unrestricted net position	13,876,554	9,311,453
Total net position	\$ 77,927,197	\$ 72,866,901
Total Liabilities and Net Position	\$ 84,302,110	\$ 82,352,291

PORT OPERATING FINANCIAL ACTIVITY:

As noted earlier, the Port uses only one fund, an enterprise fund, to comply with Washington State mandated reporting requirements. The Port's operations consist of airport and industrial park operations, land and building leases, and operating a variety of recreational facilities. Of the recreational facilities, the Port Orchard and Bremerton marinas produce the largest portion of revenue from these sources. The remaining recreational facilities, such as boat ramps and parks produce little to no revenue.

Summary of Statement of Revenues, Expenses and Changes in Fund Net Position: The Statement of Revenues, Expenses and Changes in Fund Net Position shows how the Port's net assets changed during the current and previous fiscal year as a result of operations. These changes are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, some revenues and expenses reported in this statement will only affect future period cash flows.

The following summary represents the 2012 operating results to budget:

Revenues: In 2012 operating revenues fell only .5% below budgeted revenues or \$16,577 short of budget. The 2011 operating revenues were below budget by 1.5% or \$50,635. Because of the economic downturn and poor real estate market, the Olympic View Business Park facility was only partially leased during 2011 but was fully leased in 2012.

Expenses: 2012 operating expenses, before depreciation, were \$853,158 (15.3%) below budget, attributed to continued operational cutbacks in overall spending. Airport, industrial and business park operations reduced spending to achieve a combined total of \$465,357 below budget. Marina operations achieved over \$200,000 in budget savings, with general and administration spending for the year of over \$157,000 below budget.

Operating expenses in 2011 were \$635,683 lower than budgeted.

Non-Operating: 2012 non-operating revenues were \$370,189 above budget (4.9%), with other non-operating expenses of \$44,974 (13.0%) under budget. Non-operating revenues continue to exceed budget from timber revenue generated from tree thinning, while interest expense attributed to non-operating expense falling below budget. In 2011, non-operating revenues were significantly above budget because of timber revenue by \$275,943, (3.5%), with non-operating expenses \$129,952 (20.8%) under budget.

Grant contributions were up in 2012 from 2011 by \$653,579 largely from a Washington State Department of Commerce infrastructure grant.

**PORT OF BREMERTON'S CONDENSED STATEMENT OF REVENUES,
EXPENSES AND CHANGES IN FUND NET POSITION:**

	2012	2011
Operating Revenues		
Airport operations	\$ 228,208	\$ 216,843
Marina operations	1,561,244	1,702,583
Property lease/rental operations	1,582,488	1,422,499
Other	337	264
Total operating revenues	3,372,277	3,342,189
Non-operating Revenues		
Ad valorem tax revenues	7,456,636	7,772,679
Investment income	22,784	18,016
Other non-operating income	486,361	276,637
Total non-operating revenues	7,965,781	8,067,332
Total revenues	11,338,058	11,409,521
Operating expenses	7,631,111	7,711,816
Non-operating expenses	301,663	495,174
Total expenses	7,932,774	8,206,990
Excess	3,405,284	3,202,531
Capital contributions	1,364,473	710,894
Special and extraordinary items	(981)	(10,101)
Increase in Fund Net Position	\$ 4,768,776	\$ 3,903,324
Net Position - Beginning of period	72,866,901	69,445,468
Prior period adjustment	291,521	(481,891)
Net Position - End of period	\$77,927,198	\$72,866,901

The Port's overall financial position improved in both 2012 and 2011.

As part of the Port's increased cash in 2012, \$369,089 is to be used for future capital projects so directed by the Board of Commissioners.

CAPITAL ASSETS:

The Port's capital asset investment at the end of 2012 is \$67,951,701, net of accumulated depreciation and \$71,351,015 for 2011. Capital assets consist of land, buildings, machinery and equipment, and construction in progress. Refer to Note 4 of the Notes to Financial Statements. Capital assets declined in 2012 as a result of an Agreement entered into with a local transit agency providing for a reimbursement schedule for the design and

construction costs of the A-Float, B Pontoon section of the Bremerton marina, completed in 2008 by the Port.

The Port purchased a waterfront parcel adjacent to the Bremerton marina for \$3,500,000 in 2009, for the purpose of providing parking to the marina tenants. The property contains underground contamination, with estimated remediation costs ranging from approximately \$210,000 to \$390,000. Please see Note 16 for further information.

In 2011 the Port reduced Capital Assets by \$481,891 with a prior period write off of funds expended on the development of a portion of land which had previously been designated for the Sustainable Energy campus. Costs for site stabilization and an access road were deemed abandoned at the time the land parcel was incorporated into a new land lease for development of a 230 acre parcel by a tenant in the industrial park.

There are no restrictions, commitments, or other limitations that significantly affect the availability of fund resources for future use.

DEBT ADMINISTRATION:

The Port has outstanding general obligation debt at December 31, 2012 of \$3,930,000 compared to \$7,895,000 in 2011. 2012 was the final assessment for the Port's six-year Industrial Development District tax levy which began in 2007 to pay debt service on the 2006 Limited Tax General Obligation Bonds issued for construction of the Bremerton marina. The final debt service payment was made in 2012.

The Port's \$432,000 low interest loan through CERB (Community Economic Revitalization Board) was used as a funding source for the FBO (Fixed Base Operator) building at the airport. The repayment schedule for this loan began in January 2005 and continues through January 2024. The balance at December 31, 2012 and 2011 respectively were \$287,135 and \$307,041. Funds from a low interest \$364,471 CERB loan were received for investment in infrastructure at the Bremerton National Airport, with outstanding balances of \$331,609 and \$348,323 for 2012 and 2011 respectively. The principal balance on rental property purchased in 2005 for \$264,000 was fully paid in 2011, saving the Port an estimated \$44,000 in future interest. See Note 9 of the Notes to Financial Statements.

2013 BUDGET:

The Port's 2013 budget anticipates Operating Revenues to grow by 3.0% over comparable operations for 2012 while operating expenses are budgeted to decline 1.9% from 2012, because of continued spending restrictions implemented during 2011. The loss from Port operations before depreciation and before the general tax levy (partially used for operations) is anticipated to be approximately \$2.0 million. After including the general tax levy, operating income is estimated at \$1.1 million.

In addition to \$613,500 of 2009 bond proceeds and other assigned cash, \$770,571 is required in 2013 for capital projects, net of anticipated grants. This total includes various capital improvements in airport, marinas and real estate projects. Many of these projects are complex and are anticipated to occur over multiple years and are currently in various stages of planning, design and permitting.

Continuing to increase cash balances in 2013, the Port expects that \$343,787 will be available for future capital projects so directed by the Board of Commissioners.

The Port's budget is developed with consultation of much of the Port's management and through analysis of Port operations. However, all budgets inherently are forecasts and the actual results will likely vary from that provided for in the budget. Assumptions regarding interest rates, economic growth and natural disasters are among the many factors that may cause a significant variance of actual results to the budget.

REQUEST FOR INFORMATION:

The Port of Bremerton designed this financial report to provide our citizens, customers, investors and creditors with an overview of the Port's finances. If you have questions or need additional information, please visit our website at www.portofbremerton.org or contact the Chief Financial Officer at 8850 SW State Hwy 3, Bremerton, WA 98312. Telephone: 360/674-2381.

PORT OF BREMERTON
Statement of Net Position
December 31, 2012

ASSETS

CURRENT ASSETS:

Cash and cash equivalents (Note 1 and 2)	\$ 10,631,652
Restricted assets:	
Cash and cash equivalents (Note 1 and 2)	963,131
Taxes receivable (Note 3)	536,455
Accounts receivable (net of allowance for uncollectibles) (Note 1)	454,895
Due from other governments - current portion (Note 1 and 5)	100,000
Other receivables	397,712
Inventory (Note 1)	49,946
Prepaid expenses	247,179

TOTAL CURRENT ASSETS	13,380,970
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NON-CURRENT ASSETS:

Capital assets not being depreciated (Note 4)

Land	7,139,949
Construction in progress	3,537,921

Capital assets being depreciated (Note 4)

Buildings & structures	38,253,968
Machinery and equipment	1,843,845
Marina and other improvements	49,353,668
Less: Accumulated depreciation	(32,177,650)

TOTAL NET CAPITAL ASSETS	67,951,701
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Other Non-Current Assets

Due from other governments - Long term portion (Note 1 and 5)	2,899,905
Other (Note 1)	69,534

TOTAL OTHER NON-CURRENT ASSETS	2,969,439
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TOTAL NONCURRENT ASSETS	70,921,140
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TOTAL ASSETS	\$ 84,302,110
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DEFERRED OUTFLOWS OF RESOURCES	0
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See Accompanying Notes to Financial Statements

PORT OF BREMERTON
Statement of Net Position
December 31, 2012

LIABILITIES AND NET ASSETS**CURRENT LIABILITIES:**

Warrants payable	\$ 1,082,671
Accounts payable	118,437
Payable from restricted assets (customer deposits)	211,802
Accrued expenses	267,708
Accrued interest payable	23,396
Current portion of long-term liabilities (Note 10)	333,090

TOTAL CURRENT LIABILITIES	2,037,104
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NON-CURRENT LIABILITIES:

General obligation bonds (Note 10)	3,646,358
CERB loans (Note 10)	581,401
Employee leave benefits (Note 1)	110,050

TOTAL NON-CURRENT LIABILITIES	4,337,809
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TOTAL LIABILITIES	\$ 6,374,913
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DEFERRED INFLOWS OF RESOURCES	0
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NET POSITION:

Net investment in capital assets	63,299,314
Restricted for debt service and capital projects (Note 11)	751,329
Unrestricted	13,876,554

TOTAL NET POSITION	\$ 77,927,197
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See Accompanying Notes to Financial Statements

PORT OF BREMERTON**Statement of Revenues, Expenses and Changes in Fund Net Position
For Year Ended December 31, 2012****REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION****OPERATING REVENUES:**

Airport operations	\$ 228,208
Marina operations	1,561,244
Property lease/rental operations	1,582,488
Other	337
Total Operating Revenues	<u>3,372,277</u>

OPERATING EXPENSES:

General operations	3,815,047
Maintenance	297,210
General and administrative	621,381
Depreciation (Note 4)	2,897,473
Total Operating Expenses	<u>7,631,111</u>

Operating Income (Loss) **(4,258,834)**

NONOPERATING REVENUES (EXPENSES):

Investment income	22,784
Taxes levied for:	
General purposes (Note 3)	3,023,017
Debt service principal/interest (Note 3)	317,421
Industrial Development District (Note 3)	4,116,198
Interest expense	(301,663)
Other nonoperating revenues (expenses)	486,361
Total Non-Operating Revenues (Expenses)	<u>7,664,118</u>

**Income (loss) before other revenues, expenses, gains, losses
and transfers** **3,405,284**

Capital contributions **1,364,473**
Extraordinary items (Note 17) **(981)**

INCREASE (DECREASE) IN NET POSITION **\$ 4,768,776**

Net position - beginning of period **\$ 72,866,901**
Less: Prior Period adjustments (Note 17) **291,521**

Net position - end of period **\$ 77,927,198**

See Accompanying Notes to Financial Statements

Port of Bremerton
Statement of Cash Flows
For the year ended December 31, 2012

	<u>2012</u>
CASH FLOWS FROM OPERATING ACTIVITIES	
Receipts from customers	\$ 3,099,879
Payments to suppliers	(1,506,255)
Payments to employees	(2,370,438)
Other receipts	171,174
Other payments	(7,425)
Net cash provided (used) by operating activities	<u>(613,065)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Property tax receipts	3,091,462
Net cash provided (used) by noncapital financing activities	3,091,462
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Property tax receipts for capital assets	4,433,619
Acquisition and construction of capital assets	(2,365,340)
Capital Contributions	1,132,942
Proceeds from timber sales	315,488
Principal paid on bonds and note	(3,806,723)
Interest paid on bonds and note	(301,663)
Net cash provided (used) by capital and related financing activities	<u>(591,677)</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Interest received on investments	22,784
Net increase (decrease) in cash and cash equivalents	<u>1,909,504</u>
Balances - beginning of year	<u>9,685,278</u>
Balances - end of year	<u><u>11,594,783</u></u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	
Operating income (loss)	\$ (4,258,834)
Adjustment to reconcile operating income (loss) to net cash provided (used) by operating activities:	
Depreciation	2,897,473
Change in assets and liabilities:	
(Increase) decrease in accounts receivable (net)	(285,741)
(Increase) decrease in fuel inventory	4,527
(Increase) decrease in prepayments	(21,710)
Increase (decrease) in warrants payable	822,764
Increase (decrease) in accounts payable	(24,683)
Increase (decrease) in customer deposits	13,343
Increase (decrease) in accrued expenses	239,796
Net cash provided (used) by operating activities	<u>(613,065)</u>

SEE ACCOMPANYING NOTES TO THE FINANCIAL STATEMENTS

PORT OF BREMERTON

Notes to Financial Statements

January 1, 2012 through December 31, 2012

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

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Port of Bremerton was incorporated in October 1913 and operates under the laws of the State of Washington applicable to a Port District. The financial statements of the Port have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governments.

In compliance with the Government Accounting Standards Board, the Port implemented GASB 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*.

A. Reporting Entity

The Port is a special purpose government and provides airport, harbor and industrial park facilities to the general public and is supported primarily through user charges.

The Port is governed by an elected three member board. As required by generally accepted accounting principles, management has considered all potential component units in defining the reporting entity. The Port has no component units.

B. Basis of Accounting and Reporting

The accounting records of the Port are maintained in accordance with methods prescribed by the State Auditor under the authority of Chapter 43.09 RCW. The Port uses the *Budgeting, Accounting, and Reporting System for GAAP Port Districts* in the State of Washington.

Funds are accounted for on a cost of services or an economic resources measurement focus. This means that all assets and all liabilities (whether current or noncurrent) associated with their activity are included on their statements of net position. Their reported fund position (total net assets) is segregated into net investment in capital assets, restricted and unrestricted components of net position. Operating statements present increases (revenues and gains) and decreases (expenses and losses) in net position. The Port discloses changes in cash flows by a separate statement that presents their operating, noncapital financing, capital and related financing and investing activities.

The Port uses the full-accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Capital asset purchases are capitalized and long-term liabilities are accounted for in the appropriate fund(s).

The Port distinguishes between operating revenues and expenses from nonoperating ones. Operating revenues and expenses result from providing services and producing and delivering goods in connection with a district's principal ongoing operations. The principal operating revenues of the Port are charges to customers for boat moorage and aircraft hanger rent and tie-down. The Port also recognizes land and building lease revenue as operating revenue. Operating expenses for the Port include general operations expenses, maintenance, administrative expenses, and depreciation on capital assets, etc. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

The Port receives federal and state grants for both capital reimbursement as well as operating grants for specific purposes. Operating grants and related expenses are accounted for as Non-operating Revenues and Expenses while Capital grants are accounted for as Capital Contributions increasing the Net Position of the Port.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Significant Risks and Uncertainties

The Port is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include economic conditions, collective bargaining disputes, federal, state and local government regulations, and changes in law.

C. Assets, Liabilities and Net Position

1. Cash and Cash Equivalents

The Port acts as its own treasurer. It is the Port's policy to invest all temporary cash surpluses. At December 31, 2012, the Port was holding \$11,382,981 in short-term residual investments of surplus cash. This amount is classified on the statement of net position as cash and cash equivalents.

The amounts reported as cash and cash equivalents also include compensating balances maintained with certain banks in lieu of payments for services rendered. The average compensating balances maintained during 2012 were approximately \$349,565.

For purposes of the statement of cash flows, the Port considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

2. Short-Term Investments – See Deposits and Investments Note No. 2.

3. Receivables

Taxes receivable consist of property taxes and related interest and penalties. See Property Tax Note No. 3. Accrued interest receivable consists of amounts earned on investments, notes, and contracts at the end of the year.

Customer accounts receivable consist of amounts owed from private individuals or organizations for goods and services including amounts owed for which billings have not been prepared.

Receivables have been recorded net of estimated uncollectible amounts. Because property taxes and special assessments are considered liens on property, no estimated uncollectible amounts are established. The allowance method is used to account for bad debt expense. The allowance for doubtful accounts for customer accounts receivables is \$9,000 at December 31, 2012.

4. Amounts Due To and From Other Governments

The Port has a non-interest bearing long-term receivable with a local transit authority for reimbursable costs related to the design and construction costs of the Passenger Only Ferry Operations Float and Service Float in Bremerton in the amount of \$2,999,905. The receivable was previously conditioned upon regularly scheduled full daily passenger only ferry service operating from the Bremerton ferry terminal. An Interlocal Agreement and Memorandum of Agreement were executed in 2007 and 2009 respectively. In 2012 an A-Float – B Pontoon Reimbursement, Maintenance and Use Agreement was executed, providing a reimbursement schedule of \$100,000 annual installments, beginning March 1, 2013. An accelerated repayment term is also included in the agreement, such that if and when long term operational funding for the initiation and undertaking of regular cross-sound passenger only ferry service between Seattle and Bremerton is secured, the unpaid balance of the receivable is to be paid in four equal annual installments. If service is not initiated or is cancelled, the 30 year repayment plan resumes.

5. Inventories

Inventories for retail and fuel sales are valued by the FIFO method (which approximates the market value).

6. Restricted Assets and Liabilities

In accordance with bond resolutions and certain related agreements, separate restricted accounts are required to be established. The assets held in these funds are restricted for specific uses, including construction, debt service and other special restricted requirements. Specific debt service reserve requirements are described in Long-Term Debt and Leases Note 10.

The restricted assets are composed of the following:

Cash and Cash Equivalent – General Obligation Bond	\$
Debt Service	0
Cash and Cash Equivalents – Unspent Bond Proceeds	751,329
Customer Deposits	<u>211,802</u>
Total Restricted Assets	\$ 963,131

Only customer deposits are shown with a related liability.

7. Capital Assets and Depreciation - See Capital Assets and Depreciation Note No. 4.

8. Other Assets and Debits

In accordance with generally accepted accounting principles for regulated businesses, the Port has deferred costs of \$69,534 in 2012, comprised of the remainder of deferred real estate lease broker fees of \$11,294 and \$58,239 in construction retainage.

9. Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation and sick leave. The Port records unpaid leave for compensated absences as an expense and liability when incurred.

Vacation pay, which may be accumulated up to a maximum of 40 days, is payable upon resignation, retirement or death at employee's regular pay rate. Sick leave may

accumulate up to a maximum of 90 days. For employees who have reached their maximum sick leave accrual, the monthly value of excess sick leave is deposited into the employee's VEBA account.

Administrative, non-union employees are provided, at termination, a sick leave cash out payment at his/her regular pay rate according to the following schedule:

Less than 5 years' service	0 %
At least 5 but less than 10 years of service	20 %
At least 10 but less than 15 years of service	35 %
At least 15 but less than 20 years of service	50 %
20 or more years of service	75%

Union employees who retire from the Port under the Port's retirement plan shall be provided a sick leave cashout payment at seventy-five percent (75%) of the employee's accrued and unused sick leave hours.

10. Other Accrued Liabilities

These accounts consist of wages payable, employee withholdings, and sales and business taxes.

11. Long-Term Debt – See Long-Term Debt and Leases Note No. 10

NOTE 2 – DEPOSITS AND INVESTMENTS

DEPOSITS

The Port's deposits and certificates of deposit are entirely covered by federal depository insurance (FDIC) or for deposits in the Washington State Local Government Investment Pool are secured by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC). In accordance with GASB criteria, PDPC protection is of the nature of collateral, not of insurance. The Pool is a 2a7-like investment operated by the Washington State Treasurer that is not rated and is subject to annual audits by the Washington State Auditor's Office.

INVESTMENTS

As of December 31, 2012, the Port had the following short term investments with the Local Government Investment Pool (LGIP), which are considered cash or cash equivalent:

Local Government Investment Pool	\$11,069,962
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All temporary investments are stated at cost, which is equivalent to fair value for these investments.

Custodial credit risk is the risk that in event of a failure of the counterparty to an investment transaction the Port would not be able to recover the value of the investment or collateral securities. None of the Port's investments are held by counterparties.

Investment Type	Moody's Investor Service	Standard & Poor's
Washington Local Government Investment Pool	N/R	N/R

NOTE 3 – PROPERTY TAXES

The county treasurer acts as an agent to collect property taxes levied in the county for all taxing authorities.

Property Tax Calendar	
January 1	Taxes are levied and become an enforceable lien against properties.
February 14	Tax bills are mailed.
April 30	First of two equal installment payments is due.
May 31	Assessed value of property established for next year's levy at 100 percent of market value.
October 31	Second installment payment is due.

Property taxes are recorded as a receivable and revenue when levied. No allowance for uncollectible taxes is established because delinquent taxes are considered fully collectible. Prior year tax levies were recorded using the same principal, and delinquent taxes are evaluated annually.

The Port may levy up to \$.45 per \$1,000 of assessed valuation for general governmental services. Washington State Constitution and Washington State Law, RCW 84.55.010, limit the rate. The Port may also levy taxes at a lower rate.

Special levies approved by the voters are not subject to the above limitations.

The Port's regular and debt service levy for 2012 was \$.3647 per \$1,000 on an assessed valuation of \$9,252,295,752 for a total regular levy of \$3,374,263. In 2011, the regular levy was \$3,339,150.

The second six-year Industrial Development District (IDD) tax levy imposed by the Port in 2007 is not subject to the limitations listed above. The Port levied an additional \$.4500 per \$1,000 in 2012 to pay the debt service on the bonds issued for the expansion of the Bremerton Marina and for other capital projects as approved by the Port Commission. The additional IDD levy for 2012 was \$4,163,533. In 2011, the Port levied an additional \$4,399,200. The final principal and interest payment on the bonds was made in 2012.

NOTE 4 – CAPITAL ASSETS AND DEPRECIATION

- A. Major expenditures for capital assets, including capital leases and major repairs that increase useful lives, are capitalized. Maintenance, repairs, and minor renewals are accounted for as expenses when incurred.

All capital assets are valued at historical cost (or estimated historical cost, where historical cost is not known/or estimated market value for donated assets).

The Port has acquired certain assets with funding provided by federal financial assistance programs. Depending on the terms of the agreements involved, the federal government could retain an equity interest in these assets. However, the Port has sufficient legal interest to accomplish the purposes for which the assets were acquired, and has included such assets within the applicable account.

The original cost of operating property retired or otherwise disposed of and the cost of installation, less salvage, is charged to accumulated depreciation. However, in the case of the sale of a significant system, the original cost is removed from the Port's plant accounts, accumulated depreciation is charged with the accumulated depreciation related to the property sold, and the net gain or loss on disposition is credited or charged to income.

An allowance for funds used during construction is capitalized as part of the cost of Port plant. The procedure is intended to remove the cost of financing construction

activity from the income statement and to treat such cost in the same manner as construction labor and material costs.

The Port's policy is to capitalize all asset additions greater than \$2,500, with an estimated life of more than one year. Depreciation expense is charged to operations to allocate the cost of capital assets over their estimated useful lives, using the straight line method. Buildings and improvements are assigned useful lives of 25 to 33 years; equipment 5 to 10 years; and furniture and fixtures 5 to 10 years.

B. Capital assets activity for the year ended December 31, 2012, was as follows:

	BEGINNING ASSET BALANCE January 1, 2012	ADDITIONS	DELETIONS	ENDING ASSET BALANCE December 31, 2012
Capital assets, not being depreciated:				
Land	\$ 7,139,949	\$ 0	\$ 0	\$ 7,139,949
Construction in progress	1,876,895	2,037,791	376,764	3,537,921
Total capital assets, not being depreciated	9,016,844	2,037,791	376,764	10,677,871
Capital assets being depreciated:				
Buildings & structures	41,015,809	154,227	2,916,068	38,253,968
Machinery and equipment	1,839,037	31,651	26,843	1,843,845
Marina and other improv.	49,077,866	275,801	0	49,353,668
Total capital assets being depreciated	91,932,712	461,679	2,942,911	89,451,480
Less accumulated depreciation for:				
Buildings & structures	15,869,646	1,100,912	290,780	16,679,778
Machinery and equipment	1,434,324	121,413	27,584	1,528,153
Marina and other improv.	12,294,571	1,675,148	0	13,969,719
Total accumulated depreciation	29,598,541	2,897,473	318,364	32,177,650
Total capital assets, being depreciated, net	62,334,171	(2,435,794)	2,624,547	57,273,830

C. Construction Commitments

The Port has active construction projects as of December 31, 2012. The projects include: Cross SKIA connector road, industrial park pad ready sites, Water Street boat launch, marina park expansion and terminal improvements.

At year-end the Port's commitments with contractors are as follows:

Project	Spent To Date	Remaining Commitment
Clean Tech Incubator	\$1,292,843	\$ 0
Cross SKIA Phase 2 (Design)	510,594	233,609
Port orchard Marina End Wall Curtains	37,588	
OVIP #5 Tenant Improvements	31,836	17,584
Large Onsite Sewage Disposal	14,883	4,500
Marina Park Expansion	61,819	450,586
NE Campus Phase 2 Basin 7	1,438,345	554
Water Street Boat Ramp	37,293	402,000
Viking Fence Sewer	5,470	9,418
Airport Terminal Lunchroom Remodel	8,190	
Bremerton Hangars LLC	16,145	2,179
BNA Infrastructure	19,431	30,569
Airport Plans Update	63,484	258,061
	\$ 3,537,921	\$ 1,409,060

Of the committed balance of \$1,409,060, the Port will not be required to raise funds in future financing.

NOTE 5 – DUE FROM OTHER GOVERNMENTS

The annual minimum receivable amount Due From Other Governments is as follows:

Year Ending December 31	Receivable Amount
2013	100,000
2014	100,000
2015	100,000
2016	100,000
2017	100,000
2018-2022	500,000
2023-2027	500,000
2028-2032	500,000
2033-2037	500,000
2038-2042	499,905
Total	\$ 2,999,905

NOTE 6 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

There have been no material violations of finance-related legal or contractual provisions.

NOTE 7 – PENSION PLANS

Substantially all Port full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer public employee defined benefit retirement plans. The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan.

The DRS CAFR may be obtained by writing to: Department of Retirement Systems, Communications Unit, PO Box 48380, Olympia, WA 98504-8380; or it may be downloaded from the DRS website at www.drs.wa.gov.

The following disclosures are made pursuant to GASB Statements 27, *Accounting for Pensions by State and Local Government Employers* and No. 50, *Pension Disclosures, an Amendment of GASB Statements No. 25 and No. 27*.

Public Employees' Retirement System (PERS) Plans 1, 2 and 3

Plan Description

The Legislature established PERS in 1947. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior courts; employees of legislative committees; community and technical colleges, college and university employees not participating in higher education retirement programs; employees of district and municipal courts; and employees of local governments. Approximately 50% of PERS salaries are accounted for by state employment. PERS retirement benefit provisions are established in Chapters 41.43 and 41.40 RCW and may be amended only by the State Legislature.

PERS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a defined benefit plan with a defined contribution component.

PERS members who joined the system by September 30, 1977 are Plan 1 members. Those who joined on or after October 1, 1977 and by either, February 28, 2002 for state

and higher education employees, or August 31, 2002 for local government employees, are Plan 2 members unless they exercised an option to transfer their membership to Plan 3. PERS members joining the system on or after March 1, 2002 for state and higher education employees, or September 1, 2002 for local government employees have the irrevocable option of choosing membership in either PERS Plan 2 or Plan 3. The option must be exercised within 90 days of employment. Employees who fail to choose within 90 days default to Plan 3. Notwithstanding, PERS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill, with less than five years to live.

PERS is comprised of and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of this Plan 2/3 defined benefit plan may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

PERS Plan 1 and Plan 2 retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the PERS Plan 1 and Plan 2 defined benefit plans accrue interest at a rate specified by the Director of DRS. During DRS' Fiscal Year 2012, the rate was five and one-half percent compounded quarterly. Members in PERS Plan 1 and Plan 2 can elect to withdraw total employee contributions and interest thereon upon separation from PERS-covered employment.

PERS Plan 1 members are vested after the completion of five years of eligible service.

PERS Plan 1 members are eligible for retirement after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The monthly benefit is 2% of the average final compensation (AFC) per year of service, but the benefit may not exceed 60 percent of AFC. The AFC is the monthly average of the 24 consecutive highest-paid service credit months.

The monthly benefit is subject to a minimum for retirees who have 25 years of service and have been retired 20 years, or who have 20 years of service and have been retired 25 years. If a survivor option is chosen, the benefit is reduced. Plan 1 members retiring from inactive status prior to the age of 65 may also receive actuarially reduced benefits. Plan 1 members may elect to receive an optional COLA that provides an automatic annual adjustment based on the Consumer Price Index. The adjustment is capped at 3% annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 1 provides duty and non-duty disability benefits. Duty disability retirement benefits for disablement prior to the age of 60 consist of a temporary life annuity. The benefit amount is \$350 a month, or two-thirds of the monthly AFC, whichever is less. The benefit is reduced by any workers' compensation benefit and is payable as long as the member remains disabled or until the member attains the age of 60, at which time the benefit is converted to the member's service retirement amount. A member with five years of covered employment is eligible for non-duty disability retirement. Prior to the age of 55, the benefit amount is 2% of the AFC for each year of service reduced by 2% for each year that the member's age is less than 55. The total benefit is limited to 60% of the AFC and is actuarially reduced to reflect the choice of a survivor option. Plan 1 members may elect to receive an optional COLA amount (based on the Consumer Price Index), capped at 3% annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 1 members can receive credit for military service while actively serving in the military if such credit makes them eligible to retire. Members can also purchase up to 24 months of service credit lost because of an on-the-job injury.

The survivor of a PERS Plan 1 member who dies after having earned ten years of service credit has the option, upon the member's death, of either a monthly survivor benefit or the lump sum of contributions plus interest.

PERS Plan 2 members are vested after the completion of five years of eligible service. Plan 2 members are eligible for normal retirement at the age of 65 with five years of service. The monthly benefit is 2% of the AFC per year of service. The AFC is the monthly average of the 60 consecutive highest-paid service months. There is no cap on years of service credit; and a cost-of-living allowance is granted (based on the Consumer Price Index), capped at 3% annually.

PERS Plan 2 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by an early retirement factor (ERF) that varies according to age, for each year before age 65.

PERS Plan 2 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions:

- With a benefit that is reduced by 3% for each year before age 65; or,
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules.

PERS Plan 2 retirement benefits are also actuarially reduced to reflect the choice, if made, of a survivor option.

The surviving spouse or eligible child(ren) of a PERS Plan 2 member who dies after having earned ten years of service credit has the option of either a monthly benefit or a lump sum payment of the member's contributions plus interest.

PERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component and member contributions finance a defined contribution component. As established by chapter 41.34 RCW, employee contribution rates to the defined contribution component range from 5% to 15% of salaries, based on member choice. There are currently no requirements for employer contributions to the defined contribution component of PERS Plan 3.

PERS Plan 3 defined contribution retirement benefits are dependent upon the results of investment activities. Members may elect to self-direct the investment of their contributions. Any expenses incurred in conjunction with self-directed investments are paid by members. Absent a member's self-direction, PERS Plan 3 investments are made in the same portfolio as that of the PERS 2/3 defined benefit plan.

For DRS' Fiscal Year 2012, PERS Plan 3 employee contributions were \$95.2 million, and plan refunds paid out were \$66.2 million.

The defined benefit portion of PERS Plan 3 provides members a monthly benefit that is 1% of the AFC per year of service. The AFC is the monthly average of the 60 consecutive highest-paid service months. There is no cap on years of service credit, and Plan 3 provides the same cost-of-living allowance as Plan 2.

Effective June 7, 2006, PERS Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service, if twelve months of that service are earned after age 44; or after five service credit years earned in PERS Plan 2 by June 1, 2003. Plan 3 members are immediately vested in the defined contribution portion of their plan.

Vested Plan 3 members are eligible for normal retirement at age 65, or they may retire early with the following conditions and benefits:

- If they have at least ten service credit years and are 55 years old, the benefit is reduced by an ERF that varies with age, for each year before age 65.
- If they have 30 service credit years and are at least 55 years old, they have the choice of a benefit that is reduced by 3% for each year before age 65; or a benefit with a smaller (or no) reduction factor (depending on age) that imposes stricter return-to work rules.

PERS Plan 3 benefit retirement benefits are also actuarially reduced to reflect the choice, if made, of a survivor option.

PERS Plan 2 and Plan 3 provide disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 monthly benefit amount is 2% of the AFC per year of service. For Plan 3, the monthly benefit amount is 1% of the AFC per year of service. These disability benefit amounts are actuarially reduced for each year that the member's age is less than 65, and to reflect the choice of a survivor option. There is no cap on years of service credit, and a cost-of-living allowance is granted (based on the Consumer Price Index) capped at 3% annually.

PERS Plan 2 and Plan 3 members may have up to ten years of interruptive military service credit; five years at no cost and five years that may be purchased by paying the required contributions.

PERS Plan 2 and Plan 3 members who becomes totally incapacitated for continued employment while serving the uniformed services, or a surviving spouse or eligible child(ren), may request for interruptive military service credit.

PERS Plan 2 and Plan 3 members can purchase up to 24 months of service credit lost because of an on-the-job injury.

PERS members may also purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement and can be used only to provide the member with a monthly annuity that is paid in addition to the member's retirement benefit.

Beneficiaries of a PERS Plan 2 or Plan 3 member with ten years of service who is killed in the course of employment receive retirement benefits without actuarial reduction. This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Director of the Department of Labor and Industries.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a PERS member who dies in the line of service as a result of injuries sustained in the course of employment, or if the death resulted from an occupational disease or infection that arose naturally and proximately out of the member's covered employment, if found eligible by the Department of Labor and Industries.

There are 1,184 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans as of June 30, 2011:

Retirees and Beneficiaries Receiving Benefits	\$ 79,363
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	29,925
Active Plan Members Vested	105,578
Active Plan Members Non-vested	<u>46,839</u>
Total	\$261,705

Funding Policy

Each biennium, the state Pension Funding Council adopts PERS Plan 1 employer contribution rates, PERS Plan 2 employer and employee contribution rates, and PERS Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at 6% for state agencies and local government unit employees, and at 7.5% for state government elected officials. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. Under PERS Plan 3, employer contributions finance the defined benefit portion of the plan and member contributions finance the defined contribution portion. The Plan 3 employee contribution rates range from 5% to 15%, based on member choice. Two of the options are graduated rates dependent on the employee's age.

The methods used to determine the contribution requirements are established under state statute in accordance with Chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of current-year covered payroll, as of December 31, 2012, are as follows:

Members not participating in JBM:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
Employer*	7.21%**	7.21%**	7.21%***
Employee	6.00%****	4.64%****	*****

*The employer rates include the employer administrative expense fee currently set at 0.16%.

**The employer rate for state elected officials is 10.74% for Plan 1 and 7.21% for Plan 2 and Plan 3.

*** Plan 3 defined benefit portion only.

****The employee rate for state elected officials is 7.50% for Plan 1 and 4.64% for Plan 2.

*****Variable from 5.0% minimum to 15.0% maximum based on rate selected by the PERS 3 member.

Both Port and the employees made the required contributions. The Port's required contributions for the years ended December 31 were as follows:

Year	PERS Plan 1	PERS Plan 2	PERS Plan 3
2012	\$ 0	\$ 94,285	\$ 25,321
2011	0	98,148	19,666
2010	0	83,171	16,513

Deferred Compensation Plans

The Port offers its employees two deferred compensation plans created in accordance with Internal Revenue Code Section 457. These plans are with independent plan Administrators (Nationwide Retirement Solutions and the Washington State Committee for Deferred Compensation). The plans, available to eligible employees at their option, permit employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

Compensation deferred under the plans and all income attributable to the plans is solely the property of the employee. The plan administrator holds the money, in the employee's name, in a custodial trust fund.

NOTE 8 – RISK MANAGEMENT

The Port participates in the Pacific Northwest Port Association Group, comprised of eight ports to go to the property and liability insurance market for its insurance needs to take advantage of group size to obtain efficiencies in insurance costs. Each member of the group obtains individual policies and individual premiums for its coverage. There is no sharing of risks or claims.

General liability coverage is in effect to a limit of \$1 million with a \$25,000 deductible. Excess liability coverage is in effect with a limit of \$50 million over the first \$1 million of loss. Airport liability coverage of \$20 million has a deductible of \$250,000. Commercial property coverage with a loss limit of \$100 million including \$30 million of earthquake and flood is in effect with a deductible of \$25,000. In addition, the Port maintains standard business automobile, skiff, boiler and machinery, crime and public officials' coverage.

In comparison to prior years, there were no significant changes in the type and coverage of insurance policies purchased by the Port. Settled claims have not exceeded this commercial coverage in any of the past three years.

NOTE 9 – SHORT-TERM DEBT

There was no short-term debt activity during 2012.

NOTE 10 – LONG-TERM DEBT AND LEASES

A. Long-Term Debt

The Port issued general obligation bonds in 2006 to finance the construction of the Bremerton marina and in 2009 for the purchase of property adjacent to the Bremerton marina. 2012 was the final debt service payment on the 2006 Limited Tax General Obligation Bond issue. The Port is also liable for low interest CERB loans to finance the construction of the FBO building and a waterline project.

The general obligation bonds currently outstanding are as follows:

Purpose	Maturity Range	Interest Rate	Original Amount	Amount of Installment
2009 Series – Purchase of waterfront property adjacent to Bremerton marina	2029	1.75% - 4.30%	\$4,425,000	\$ 321,242

The annual debt service requirements to maturity for general obligation bonds and other contracts are as follows:

Year Ending December 31	2009 Series		Other Contracts	
	Principal	Interest	Principal	Interest
2013	180,000	144,443	37,344	11,356
2014	180,000	141,293	38,086	10,614
2015	185,000	137,333	38,845	9,855
2016	190,000	132,800	39,624	9,077
2017	195,000	127,575	40,420	8,280
2018-2022	1,085,000	534,375	214,734	28,768
2023-2027	1,310,000	301,790	149,816	8,901
2028-2029	605,000	39,345	59,877	1,207
Total	\$ 3,930,000	\$ 1,558,954	\$ 618,746	\$ 88,058

RCW 39.36 limits the amount of general obligation debt that the Port may issue. Bond indebtedness without a vote is limited to .25% of the assessed value of the taxable property in the Port District.

At December 31, 2012, the Port's assessed value and limitation of unvoted general obligation debt are as follows:

Total Taxable Property Value	\$ 8,892,393,025
General Purpose Indebtedness Available Without a Vote	\$ 22,230,983
Indebtedness Incurred	<u>4,548,744</u>
Margin of Indebtedness Available Without a Vote	\$ 17,682,239

Unamortized debt issue costs are recorded as deferred charges and bonds are displayed net of premium or discount. Annual interest expense is decreased by amortization of debt premium and increased by the amortization of debt issue costs and discount.

At December 31, 2012, the Port had no available assigned funds for payment of bond indebtedness.

The Port issued \$4,425,000 General Obligation Bonds on September 30, 2009 to purchase a waterfront parcel adjacent to the Bremerton marina to be used for parking for \$3,500,000. The remaining bond proceeds, which are invested in the State of Washington Local Government Investment Pool, will be used for the marina park expansion and the Water Street boat launch as approved by the Port Commission. After issue costs of \$123,032 for underwriting, rating, insurance, legal and other issue costs, the Port received proceeds of \$4,301,968. An Aa2 rating was assigned by Moody's Investment Service at the time the bonds were issued. The bonds are to be paid from an assigned portion of the regular property tax levy.

These bonds are subject to federal arbitrage regulations. The Port is required to comply with certain requirements of the Internal Revenue Code of 1986, after the date of issuance of the Bonds in order to maintain the exclusion of the interest on the Bonds from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Bond proceeds and the facilities financed or refinanced with Bond proceeds, limitations on investing gross proceeds of the Bonds in higher yielding investments in certain circumstances, and the requirement to comply with arbitrage rebate requirements to the extent applicable to the Bonds. The Port has covenanted in the Bond Resolution to comply with those requirements, but if the Port fails to comply, interest on the Bonds could become taxable retroactive to the date of issuance of the Bonds. During this audit period arbitrage is not applicable.

B. Operating Leases

The Port leases office space in the Norm Dicks Government Center from the Kitsap County Housing Authority (KCCHA) under a noncancelable operating lease. The KCCHA sublease for 73.3% of the space was cancelled effective October 6, 2009 as a condition of the waterfront property purchase from KCCHA. In 2011 KCCHA entered into a 3 year sublease with two, three year extensions. The total lease cost in 2012 was \$16,661 (net of \$11,875 paid by KCCHA).

The Port executed a 10 year lease on a newly constructed 24,000 square foot building in the Olympic View Business Park, taking possession of the building in January, 2008. The lease is expressly conditioned and contingent upon a 65 year lease for the 3 acre real property upon which the building stands. The Port subleased a portion of the building to a defense contractor in 2009 and leased the remainder of the facility to them at the end of 2011. The total lease cost to the Port in 2012 was \$247,186.

The Port leases other office equipment under operating leases that expire in 2017, with a total lease cost in 2012 of \$5,782.

The Port holds five long-term Washington State Department of Natural Resource (DNR) land leases. The leases call for initial lease payments of \$62,030, adjusted annually by the Consumer Price Index – All Urban Consumers for the Seattle-Everett region, except for each four years when the non water-dependent annual rent will be revalued to reflect the then-current fair market value. The land leases are:

Land Leases				
December 31, 2012				
LESSOR	DATE OF LEASE	LEASE NUMBER	ANNUAL RENT	LAND RENTED
Dept of Natural Resources	9/1/11	2235A	\$ 13,678	Port Orchard Marina
Dept of Natural Resources	9/1/11	9891	32,701	P.O. Marina Parking
Dept of Natural Resources	9/1/11	2234	5,164	Port Orchard Area North of Old Post Office
Dept of Natural Resources	9/1/11	2736	8,772	Bremerton
Dept of Natural Resources	1/1/06	2544	1,715	Water St Boat Ramp
Total			\$62,030	

The future minimum lease payments for these leases are as follows:

Year Ending December 31	KCCHA Lease	Olympic View Lease	Office Equipment	Land Leases	Total
2013	29,283	247,186	4,468	60,315	341,252
2014	30,371	247,186	4,468	60,315	342,340
2015	31,480	247,186	4,468	60,315	343,449
2016	32,532	247,186	4,467	60,315	344,500
2017	33,835	247,186	1,319	60,315	342,655
2018-2022	178,494	10,299		301,575	490,368
2023-2027	183,151			187,122	370,273
2028-2032	182,898			138,070	320,968
2033-2037	54,918			138,070	192,988
2038-2042				124,263	124,263
Total	\$756,962	\$1,246,229	\$ 19,190	\$ 1,190,675	\$ 3,213,056

C. Changes in Long-Term Liabilities

During the year ended December 31, 2012, the following changes occurred in long-term liabilities:

	Beginning Balance 1/01/12	Additions	Reductions	Ending Balance 12/31/12	Due Within One Year
Bonds payable:					
L.T.G.O. Bonds	\$ 7,895,000	\$ 0	\$ 3,965,000	\$ 3,930,000	\$ 180,000
Deferred Premium/Discount	<u>88,150</u>	<u>0</u>	<u>15,493</u>	<u>103,642</u>	
Total Bonds Payable	\$ 7,806,850	\$ 0	\$ 3,980,493	\$ 3,826,358	
Loans/Notes Payable	655,364	0	36,620	618,744	37,344
Compensated Absences	<u>229,577</u>	<u>193,156</u>	<u>196,938</u>	<u>225,795</u>	115,746
Total Long Term Liabilities	\$ 8,691,791	\$ 193,156	\$ 4,214,050	\$ 4,670,897	

NOTE 11 – RESTRICTED COMPONENT OF NET POSITION

The Port's statement of net position reports \$751,329 of restricted component of net position. The entire amount is unspent general obligation bond proceeds.

NOTE 12 – CONTINGENCIES AND LITIGATION

The Port has recorded in its financial statements all material liabilities, including an estimate for situations which are not yet resolved but where, based on available information, management believes it is probable that the Port will have to make payment. In the opinion of management, the Port's insurance policies are adequate to pay all known or pending claims. The Port participates in a number of federal and state-assisted programs. These grants are subject to audit by the grantors or their representatives. Such audits could result in requests for reimbursement to grantor agencies for expenditures disallowed under the terms of the grants. Port management believes that such disallowances, if any, will not be significant.

The Port has been named as a defendant as a result of injuries occurring from an accident involving a motorcycle. The defense has been assumed by an insurance carrier for one of the other named defendants. This comes as a result of a "Tender of Defense" as provided in a port lease that is in existence with that defendant. The Port will continue to monitor this civil action and believes that there is little likelihood of liability for the Port.

As a result of contractor malfeasance, the Port is seeking reimbursement for damages incurred involving the construction of Port facilities. Reimbursement is expected to come from restitution in a criminal case involving the contractor in question as well as a judgment in connection with a civil action brought by the Port against the contractor. Additionally, the Port seeks relief from the federal bankruptcy proceedings initiated by the contractor in question. The total obligation owing to the Port is \$287,068 of which approximately \$1,872 has been collected.

In February, 2010, a longstanding tenant of the Port filed Chapter 11 bankruptcy. On March 22, 2011 a Notice of Order Confirming Plan was issued by the United States Bankruptcy Court. In April, 2012, the tenant filed for Chapter 7 bankruptcy, leaving an outstanding receivable balance of \$26,783 owing to the Port for five property leases, in addition to \$5,139 remaining from the Chapter 11 filing. Four of the five leases were subsequently auctioned through the bankruptcy court and assigned by the Port to the successful auction bidder with all outstanding amounts for the four assigned leases paid to the Port as part of the assignment agreement. The Port is waiting distribution from the Bankruptcy Trustee on its claim of \$10,909 on the fifth lease.

NOTE 13 – DEFERRED CREDITS

In accordance with generally accepted accounting principles for regulated businesses, the Port has no deferred costs and revenues for 2012.

NOTE 14 – OTHER POST EMPLOYMENT BENEFIT (OPEB) PLANS

The Port does not have post employment obligations other than defined pension plans.

NOTE 15 – TERMINATION BENEFITS

The Port is not obligated for termination benefits.

NOTE 16 – POLLUTION REMEDIATION OBLIGATIONS

In November 2006, the Government Accounting Standards Board issued GASB No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. This Statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. The provisions of this Statement are effective for fiscal periods beginning after December 15, 2007.

The Port purchased a waterfront property in 2009, which has known underground contaminants, resulting from the presence of former underground storage tanks. The site is listed by the Department of Ecology as a Voluntary Cleanup Site. The governmental agencies having jurisdiction over the property are not requiring remediation of the site or removal of contaminated soil at this time, but such action will likely be required in the future if the property is developed. There has been no obligating event to require recording a pollution remediation obligation on the financial statements. At the time of purchase of the property, it was estimated between \$210,000 and \$390,000 for remediation cleanup. The Port assumed all costs from the seller with regard to environmental clean-up.

NOTE 17 – OTHER DISCLOSURES

A. Prior Period Adjustments

Depreciation was reduced by \$291,521 for 2009 through 2011 based on an Agreement reached in 2012 between the Port and a local transit authority for the reimbursable costs for design and construction of the A-Float B Pontoon. See Amounts Due To and From Other Governments Note No. 5.

B. Major Receivables

In 2012, 14% of the operating revenues or \$478,776 charged for property lease/rental income was billed to a manufacturing company for several land and facility leases.

C. Extraordinary/Special Items

The Port incurred \$981 in net extraordinary expense for 2012, consisting of environmental costs related to the former Norseland Estate Site. Compliance monitoring actions, which focused on cap integrity, ambient air monitoring and groundwater testing, have been done consistent with the Compliance Monitoring Plan (CMP) for the Site. Removal of the former Norseland Estates Site from the Hazardous Sites List was approved by the State of Washington Department of Ecology in early 2012.



ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

Our mission is to work with our audit clients and citizens as an advocate for government accountability. As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

The State Auditor's Office employees are located around the state to deliver services effectively and efficiently.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments and fraud, whistleblower and citizen hotline investigations.

The results of our work are widely distributed through a variety of reports, which are available on our Web site and through our free, electronic subscription service.

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