



Washington State Auditor's Office

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Financial Statements Audit Report

City of Port Orchard

Kitsap County

For the period January 1, 2014 through December 31, 2014

Published December 10, 2015

Report No. 1015698





Washington State Auditor's Office

December 10, 2015

Mayor and City Council
City of Port Orchard
Port Orchard, Washington

Report on Financial Statements

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

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

Sincerely,

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

TABLE OF CONTENTS

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	4
Independent Auditor's Report On Financial Statements	7
Financial Section.....	10
About The State Auditor's Office.....	73

**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**

**City of Port Orchard
Kitsap County
January 1, 2014 through December 31, 2014**

Mayor and City Council
City of Port Orchard
Port Orchard, 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 governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Port Orchard, Kitsap County, Washington, as of and for the year ended December 31, 2014, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated November 25, 2015.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered the City'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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City'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 City'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 City's financial statements are free from material misstatement, we performed tests of the City'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 City'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 City'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.

A handwritten signature in black ink that reads "Troy X. Kelley". The signature is written in a cursive, flowing style.

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

November 25, 2015

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

City of Port Orchard Kitsap County January 1, 2014 through December 31, 2014

Mayor and City Council
City of Port Orchard
Port Orchard, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Port Orchard, Kitsap County, Washington, as of and for the year ended December 31, 2014, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed on page 10.

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 opinions 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 City'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 City'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 opinions.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Port Orchard, as of December 31, 2014, and the respective changes in financial position and, where applicable, cash flows thereof, and the budgetary comparison for the General Fund, for the year then ended in accordance with accounting principles generally accepted in the United States of America.

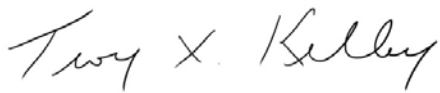
Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 11 through 19 and information on postemployment benefits other than pensions on page 73 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 November 25, 2015 on our consideration of the City'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 City's internal control over financial reporting and compliance.



TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

November 25, 2015

FINANCIAL SECTION

**City of Port Orchard
Kitsap County
January 1, 2014 through December 31, 2014**

REQUIRED SUPPLEMENTARY INFORMATION

Management's Discussion and Analysis – 2014

BASIC FINANCIAL STATEMENTS

Statement of Net Position – 2014

Statement of Activities – 2014

Balance Sheet – Governmental Funds – 2014

Reconciliation of Governmental Funds Balance Sheet to the Statement of Net Position –
2014

Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental
Funds – 2014

Reconciliation of Statement of Revenues, Expenditures and Changes in Fund Balance of
Governmental Funds to the Statement of Activities – 2014

Statement of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual
– General Fund – 2014

Statement of Net Position – Proprietary Funds – 2014

Statement of Revenues, Expenses and Changes in Fund Net Position – Proprietary Funds
– 2014

Statement of Cash Flows – Proprietary Funds – 2014

Statement of Fiduciary Net Position – Fiduciary Funds – 2014

Notes to Financial Statements – 2014

REQUIRED SUPPLEMENTARY INFORMATION

LEOFF 1 Retiree Medical Benefits Schedule of Funding Progress – 2014

MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of Port Orchard's discussion and analysis is a narrative overview of the City's financial activities for the fiscal year ended December 31, 2014. The information presented here should be read in conjunction with the financial statements and notes to the financial statements that follow.

FINANCIAL HIGHLIGHTS

- City of Port Orchard assets exceeded its liabilities at December 31, 2014 by \$85.7 million.
- Net investment in capital assets account for about 74 percent of this amount, with a value of \$63.6 million.
- Of the remaining net position, \$18.6 million may be used to meet the government's ongoing obligations to citizens and creditors, without legal restriction while \$3.4 million is restricted.
- The government's total net position shows an increase of \$233,363. The increase is largely due to reserve funds set aside per the City's financial policy.
- As of December 31, 2014, City of Port Orchard's governmental funds reported combined ending fund balances of \$6.9 million. Approximately 20.8% of this amount is available for spending at the government's discretion. Unassigned fund balance is \$1,434,580, assigned fund balance is \$1,261,399, committed fund balance \$806,997 and restricted fund balance \$3,405,837.
- City of Port Orchard's total bonded debt decreased by \$185,714 during the fiscal year. At December 31, 2014 the total outstanding bonded debt was \$1,018,217.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis provides an introduction and overview to the City of Port Orchard's basic financial statements. This information will assist users in interpreting the basic statements. We will also provide other supplementary information in addition to the basic financial statements. This financial discussion and analysis should assist the reader in understanding the City's financial condition.

Basic Financial Statements

The basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and, 3) notes to the financial statements. The financial section of this report also contains required supplementary information, in addition to the basic financial statements.

Government Wide Financial Statements

Government-wide financial statements provide readers with a broad overview of the City's finances in a manner similar to a private-sector business, distinguishing functions that are principally supported by taxes and intergovernmental revenues (referred to as "governmental activities") from functions that are intended to recover all or a significant portion of their costs through user fees and charges (referred to as "business-type activities"). The governmental activities of the City include a full range of local government services provided to the public, such as law enforcement and public safety; road construction and maintenance; community planning and development; parks and recreation facilities; and other community services. In addition, other general government services are provided, such as, tax collection, and the issuance of permits and licenses. The business-type activities of the City include water, sewer and storm utility management and operation.

The Statement of Net Position presents information on all of the City's assets and liabilities, with the difference between the two reported as net position. This statement serves a purpose similar to that of the balance sheet of a private-sector business. Over time, increases or decreases in net position may serve as one indicator of whether the financial position of the City is improving or deteriorating. Other indicators include the condition of the City's infrastructure systems (roads, drainage systems, bridges, etc.), changes in property tax base, and general economic conditions within the City.

The Statement of Activities presents information showing how the government's net position changed during 2014. This statement separates program revenue (revenue generated by specific programs through charges for services, grants, and contributions) from general revenue (revenue provided by taxes and other sources not tied to a particular program). This shows the extent each program relies on taxes for funding. All changes in net position are reported using the accrual basis of accounting, which requires that revenues be reported when they are earned and expenses are reported when the goods and services are received. Items such as uncollected taxes, unpaid vendor invoices for items received in 2014, and earned but unused vacation leave will be included in the statement of activities as revenue and expense, even though the cash associated with these items was not received or distributed in 2014.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting for compliance with finance-related legal requirements. All of the funds of the City fall into three categories: governmental funds, proprietary funds, and fiduciary funds. Governmental funds account for most, if not all, of a government's tax-supported activities. Proprietary funds account for a government's business type activities, where all or part of the costs of activities are supported by fees and charges that are paid directly by those who benefit from the activities. Fiduciary funds account for resources that are held by the government as an agent for parties outside of the government. The resources of fiduciary funds cannot be used to support the government's own programs.

Governmental Funds

The governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances present separate columns of financial data for the General Fund, Cumulative Reserve for Municipal Facilities, and the Street Capital Projects Fund. These are considered major funds. Data from the remaining governmental funds are combined into a single, aggregated presentation. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. Governmental funds financial statements focus on near-term inflows and outflows of spendable resources and on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating a government's near-term financing requirements in comparison to near-term resources available.

Because the focus of governmental funds financial statements is narrower than that of government-wide financial statements accrual basis focus, it is useful to compare information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. This gives readers a better understanding of the long-term impact of the government's near-term financing decisions. Both the Governmental Funds Balance Sheet and the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances provide reconciliation to the Governmental Activities column in the Government-Wide statements, facilitating this comparison.

The City maintains budgetary controls over its operating funds. Budgetary controls ensure compliance with legal provisions embodied in the annual appropriated budget. Governmental funds budgets are established in accordance with state law, and are adopted on a fund level. Personnel services are budgeted by position and by prorating the costs based on time allocation to the various funds. Budgetary variances are discussed later in this section.

Proprietary Funds

The City has two proprietary funds also known as enterprise funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses one enterprise fund to account for its water and sewer utilities operation. The City also has a Storm Drainage Utility Fund. Proprietary fund statements provide the same type of information as the government-wide financial statements, only in more detail, since both apply the accrual basis of accounting. In comparing the proprietary fund statement of net position to the business-type column on the government-wide statement of net position, the total net position agree, and therefore need no reconciliation.

Fiduciary Funds

Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statement because the resources of those funds are not available to support the City's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided, and are an integral part of the government-wide and fund financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Statement of Net Position

As noted earlier, changes in net position may serve as a useful indicator of a government's financial position. The City of Port Orchard's net position total \$85,671,688 at December 31, 2014. The following is a condensed version of the government-wide statement of net position.

City of Port Orchard's Condensed Statement of Net Position

	Governmental Activities 2014	Governmental Activities 2013	Business-Type Activities 2014	Business-Type Activities 2013	Total Activities 2014	Total Activities 2013
Current and other assets	\$ 8,168,944	\$ 7,498,762	\$ 16,441,692	\$ 15,296,881	\$ 24,610,636	\$ 22,795,643
Capital assets	26,219,934	26,429,662	38,671,196	38,847,060	64,891,130	65,276,722
Total assets	34,388,878	33,928,424	55,112,888	54,143,941	89,501,766	88,072,365
Long-Term liabilities	1,786,532	1,627,307	582,250	578,359	2,368,782	2,205,666
Liabilities Payable from Restricted Assets	51,011	106,287			51,011	106,287
Other liabilities	496,806	161,594	906,914	152,498	1,403,720	314,092
Total liabilities	2,334,349	1,895,188	1,489,164	730,857	3,823,513	2,626,045
Deferred Amount on Refunding	5,806	7,072	759	924	6,565	7,996
Total deferred inflows of resources	5,806	7,072	759	924	6,565	7,996
Net Position						
Invested in capital assets						
net of related debt	25,470,825	25,543,714	38,165,873	38,350,730	63,636,698	63,894,444
Restricted	3,442,902	3,622,688	-	-	3,442,902	3,622,688
Unrestricted	3,134,996	2,859,762	15,457,092	15,061,430	18,592,088	17,921,192
Total net position	\$ 32,048,723	\$ 32,026,164	\$ 53,622,965	\$ 53,412,160	\$ 85,671,688	\$ 85,438,324

The slight decrease in capital assets is due to depreciation. The largest portion of the City's net position (74 percent) reflects its investment in capital, less any related debt used to acquire those assets that is still outstanding. The City's capital assets are used to provide services to citizens. Consequently the value of these assets are not available for future spending. Of the remaining balance, \$3,442,902 is restricted and \$18,592,088 (unrestricted net position) represents the amount that may be used to meet the City's ongoing obligations.

At December 31, 2014, the City of Port Orchard reports positive balances in the two categories of net position, for the government as a whole, as well as for separate governmental and business-type activities.

Statement of Activities

In 2014 the City's total net position increased by \$233,363 including prior period adjustments. The governmental net position increased \$22,558 and business-type activities increased \$210,805 including prior period adjustments.

The following is a condensed version of the statement of activities for the City. The full statement is a tabular depiction of the relationship of revenues and expenses for the City's governmental activities and proprietary funds.

City of Port Orchard's Condensed Statement of Activities

	Governmental Activities		Business-type Activities		Total Primary Government	
	2014	2013	2014	2013	2014	2013
Revenues:						
Program revenues:						
Charges for services	\$ 1,240,472	\$ 1,320,668	\$ 5,950,724	\$ 5,698,164	\$ 7,191,196	\$ 7,018,832
Operating grants & contributions	579,357	510,948	50,000	141,810	629,357	652,758
Capital grants & contributions	34,969	1,485,222	306,796	1,229,148	341,765	2,714,370
General revenues:						
Property taxes	2,225,347	2,265,556	-	-	2,225,347	2,265,556
Sales taxes	4,102,060	3,875,305	-	-	4,102,060	3,875,305
Other taxes	2,264,467	2,117,902	-	-	2,264,467	2,117,902
Interest income	41,397	31,304	18,962	16,355	60,359	47,659
Gain on sale of capital assets	-	22,995	-	-	-	22,995
Other revenues	-	2,085	33	-	33	2,085
Total Revenues	\$ 10,488,069	\$ 11,631,985	\$ 6,326,515	\$ 7,085,477	\$ 16,814,584	\$ 18,717,462
Expenses:						
General government	2,100,241	2,087,020	-	-	2,100,241	2,087,020
Judicial	520,304	479,490	-	-	520,304	479,490
Public safety	4,739,924	4,157,052	-	-	4,739,924	4,157,052
Transportation	2,043,972	1,696,539	-	-	2,043,972	1,696,539
Social services	13,453	13,212	-	-	13,453	13,212
Economic development	573,920	476,914	-	-	573,920	476,914
Culture and recreation	384,640	388,424	-	-	384,640	388,424
Water - Sewer	-	-	4,877,932	4,719,705	4,877,932	4,719,705
Storm Drainage	-	-	940,124	789,126	940,124	789,126
Interest on long-term debt	30,746	33,610	-	-	30,746	33,610
Total Expense	\$ 10,407,200	\$ 9,332,261	\$ 5,818,056	\$ 5,508,831	\$ 16,225,256	\$ 14,841,092
Increase/(decrease) in Net Position before transfers	80,869	2,299,725	508,459	1,576,646	589,328	3,876,370
Transfers	5,804	-	(5,804)	-	-	-
Change in net position	86,673	2,299,725	502,655	1,576,646	589,328	3,876,370
Net Position Beginning	32,026,165	29,815,848	53,412,160	51,840,924	85,438,325	81,656,772
Prior Period Adjustment Annexatn	-	-	-	-	-	-
Prior Period Adjustments	(64,115)	(74,697)	(291,850)	-	(355,965)	(74,697)
Changes in Accounting Principles	-	(14,711)	-	(5,410)	-	(20,121)
Net Position Ending	\$ 32,048,723	\$ 32,026,165	\$ 53,622,965	\$ 53,412,160	\$ 85,671,688	\$ 85,438,324

Governmental Activity Analysis

Total revenues in governmental activities decreased by 9.8%. The City's tax revenues increased by \$333,111, 4% in 2014. The main sources of revenue came from retail sales and use tax and property taxes. Sales tax increased from the prior year by \$226,755, 5.9%. Property taxes experienced a slight decrease of \$40,209, 1.8%. Charges for services decreased by \$80,197, 6.1% due to planning and building revenue decreasing in 2014. Capital grants and contributions decreased significantly by \$1,450,253 due to the completion of several grant funded projects (DeKalb Pier Phase 1, Bay Street Pedestrian Path Segment 2 & 5, Safety and Health Investment Project (SHIP) grant, Cedar Heights Junior High Sidewalk), and also due to the fact that no infrastructure was donated in 2014.

Total expenses in governmental activities increased by 11.5%. The City incurred increases in the following functions: Public Safety \$582,872, Judicial \$40,814, Transportation \$347,433 and Economic Development \$97,006, General Government \$13,221 and Social Services \$241. While Culture and Recreation incurred a decrease of \$3,784. Public safety major increase was due to rising cost for prisoner boarding costs. Public safety had a large increase to compensated absences balances this year due to a change in the union contract that became effective in 2014. Transportation had an increase in expenses for paving overlay and the purchase of a man-lift for the supersingle truck. Economic environment increased due to staffing returning to normal levels and the purchase of permitting software. The net position associated with governmental activities increased by \$22,558.

Business-Type Activities Analysis

The Water-Sewer Utility experienced an increase in 2014 operating revenues of 5.1%, and a 2.1% increase in operating expenses. The Utility ended the year with a slight decrease in net position of -.1%. This was due to the decrease in Capital Grants and Contributions. Contractor contributions were significantly less in 2014 due to the completion of a large apartment complex in 2013. The Storm Drainage Utility had a slight decrease in operating revenues of -1.8%, and an increase in operating expenses of 19.1%. There was an overall increase in storm drainage net position of 2.7%. The Storm Drainage Utility's increase in net position is due to grant revenues, and new infrastructure.

FINANCIAL ANALYSIS OF CITY FUNDS

Governmental Funds Analysis

The City uses fund accounting to ensure compliance with legal requirements and to assist in the budgeting and operations of the different activities of the City. The City has ten governmental funds that are categorized into four fund types. Each type has its unique purpose. The City Street Fund and Stabilization Fund are managerial funds and are reported in the General Fund. Three funds are classified as major funds for the purposes of this report, based on GASB criteria. They are the General Fund, Cumulative Reserve for Municipal Facilities, and Street Capital Projects Fund.

The General Fund's fund balance increased by \$463,484. Revenues are higher and expenditures lower. The largest source of revenue is sales and use tax representing 41%. The largest expenditure category is public safety, representing 47% of the General Fund activity.

The Cumulative Reserve for Municipal Facilities had an increase in fund balance of \$33,340. In 2014 the City had capital expenditures for McCormick Woods Village Park, Paul Powers Park, and Bay Street Pedestrian Path within this fund.

The Street Capital Projects Fund had a decrease in fund balance of \$32,578. In 2014, the City demolished a building in preparation for the Tremont widening project and hired a consultant for a precursor right-of-way work for the Bay Street Pedestrian Pathway. These expenses were not grant funded and did not have an offsetting revenue source.

The change in total governmental funds' fund balance was an overall increase of \$321,910.

Business-Type Fund Analysis

Proprietary funds are those funds that account for government operations where the intent is for the costs to be primarily paid for by user charges. Enterprise funds are those funds that provide services primarily to external users, and Internal Service funds provide their services primarily within the City, or to other governmental units.

The Water-Sewer Fund had a total net position at year-end of \$43.7 million. This fund had operating income of \$91,690. The Water-Sewer fund had a slight decrease in total net position of (\$50,929) or -.1%. This was due to the decrease in Capital Grants and Contributions. Contractor contributions were significantly less in 2014 due to the completion of a large apartment complex in 2013. The increasing numbers of users are having the dual effect of increasing revenues and placing additional demands on the systems. The Storm Drainage Utility Fund had an operating decrease of \$103,406. This was largely due to an increase in expenditures including several large maintenance projects. The total net position at year-end was \$10 million this was an increase in net position of 2.7% or \$261,734. The increase was partially due to grants and new infrastructure.

2014 Capital Projects for Water-Sewer included Well 9 construction, Well 10 and the purchase of vehicles and equipment. Storm drainage funded work on the Decant Station Retrofit, culvert work and purchased equipment.

GENERAL FUND BUDGETARY HIGHLIGHTS

GASB 54 mandates that managerial funds cannot be reported in the Budget vs. Actual for the General Fund. This results in not including the City Street and Stabilization Funds. The City appropriates funds through an annual budget process while state law allows additional funds to be expended if authorized by an ordinance amending the original budget. Revenues ended the year ahead of the budget 1.9%. Sales taxes increased by \$23,759 and property tax increased by \$1,821. Expenditures were 92.4% of the amended budget.

The final budget, when compared to the original budget, showed increases (decreases) in: General Government \$75,607, Public Safety \$274,345, Economic Development \$23,570, Culture and Recreation (\$9,995), and Capital Expenditures \$39,000.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

The City of Port Orchard's investment in capital assets, including construction in progress, for its governmental and business type activities as of December 31, 2014, amounts to \$64,891,130, (net of accumulated depreciation). This investment in capital assets includes land, intangible assets, construction in progress, buildings, equipment, and infrastructure.

	Governmental Activities		Business Activities		Government Wide	
	1/1/2014	12/31/2014	1/1/2014	12/31/2014	1/1/2014	12/31/2014
Land	\$ 1,706,176	\$ 1,710,328	\$ 787,012	\$ 787,012	\$ 2,493,188	\$ 2,497,340
Intangible Assets	3,045,952	3,041,232	549,575	538,849	3,595,527	3,580,081
Construction in Progress	1,852,353	1,824,064	1,958,020	2,123,665	3,810,373	3,947,729
Buildings	5,327,112	5,256,626	2,809,215	2,859,227	8,136,327	8,115,853
Equipment	861,040	952,419	1,398,392	1,244,891	2,259,432	2,197,310
Infrastructure	13,637,029	13,435,265	31,540,146	31,117,552	45,177,175	44,552,817
	<u>\$ 26,429,662</u>	<u>\$ 26,219,934</u>	<u>\$ 39,042,360</u>	<u>\$ 38,671,196</u>	<u>\$ 65,472,022</u>	<u>\$ 64,891,130</u>

In governmental activities, infrastructure, buildings & structures and intangible assets decreased due to depreciation. Machinery & equipment is increased due to vehicle purchases. Construction in progress decreases slightly this year as projects are completed. Land has increased slightly due to property purchase.

In business activities the infrastructure, machinery & equipment and intangible assets categories decreased due to depreciation. Construction in progress experienced an increase because of the Well No. 10 construction project. And buildings and structures were increased by the Decant Station.

Additional information on the City of Port Orchard's capital assets can be found in Note 6 (capital assets) of this report.

Long-Term Debt

At December 31, 2014 the City of Port Orchard had total long-term debt outstanding of \$2,368,782. Of this amount, \$1,018,217 is general obligation bonds, \$169,650 is a note made with a private party, New in 2014 is a Drinking Water State Revolving Fund Loan in the amount of \$60,000, \$666,313 long-term compensated absences, and other postemployment benefits (OPEB) \$454,602.

During 2014, the City of Port Orchard's net total debt increased by \$163,117. The Increase included a new Drinking Water State Revolving Fund Loan, annual payments on the outstanding debt, changes in compensated absences policies, and the current year increase for OPEB.

Additional information on the City's long-term debt can be found in Note 11, Long-Term Debt and Note 13, Changes in Long-Term Liabilities of the notes to the financial statement in this report.

Economic Factors

The state of Washington does not have a state personal income tax and therefore the state operates primarily using sales and use tax, ad valorem, and motor vehicle excise tax. The City relies on sales and use tax, property tax, and utility taxes and a limited array of permitted taxes, fees, and state and federal grants to support its governmental activities.

Sales and use tax represents a major revenue source for governmental funds and provides an economic measurement of the local economy. General fund revenues experienced an additional 2% over budget projections in 2014. Sales and use tax increased year-over-year by 5.6%. The city views these increases as indicators of increased local economic activity, albeit at a moderate pace. The areas major employer,

The Puget Sound Naval Shipyard (PSNS) plans to add jobs to meet demand for scheduled maintenance and emergent repairs of U.S. military vessels. PSNS plans to grow to 13,300 employees during the next five years. PSNS currently has about 12,800 employees.

Construction within Port Orchard in 2014 remained strong and showed signs of further strengthening. The city saw the completion of the large 100+ unit multifamily housing development at the intersection of Sedgwick and Sidney as well as an uptick in single-family construction starting towards the end of 2014 with several residential subdivisions receiving or approaching final plat approval. Land Use and Building Permit activity was up in 2014 across the board as was business license reviews. The city also held a record number of pre application meetings in 2014 suggesting that permit activity will remain high for the near future. These trends have continued into 2015 and in the first 4 months of the year, permit activity appears to be on track to surpass 2014 numbers by at least 10% barring any slow down. The city has received numerous applications for large developments including a 300 unit residential development near Sedgwick and Glenwood as well as a large Commercial project along Sidney Road SW. Activity has increased to the point that the city is now taking longer than in 2013 and 2014 to review most type of permit applications.

The Office of Financial Management (OFM) reported Port Orchard's 2014 population in June of 2014 at 13,150, an increase of 280 people over the reported June 2013 number.

The Washington State Economic and Revenue Council expects the moderate pace of economic recovery to continue in both the U.S. and Washington economies. The City Council continues to be proactive with other agencies lobbying the State to provide funding for City and area services.

The level of taxes, fees, and charges for services will have a bearing on the City's competitive ability to encourage retail, office, residential, and industrial development. The City places significant emphasis on encouraging economic development to attract family wage paying jobs, and as an incentive does not assess a business and occupation tax (B & O).

Requests for Information

This financial report is designed to provide a general overview of the City of Port Orchard's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report, or requests for additional financial information, should be addressed to the City Treasurer, City of Port Orchard, 216 Prospect Street, Port Orchard, WA, 98366.

CITY OF PORT ORCHARD
Statement of Net Position
December 31, 2014

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and Cash Equivalents	\$ 3,899,799	\$ 7,067,240	\$ 10,967,039
Receivables (Net of Allowance for Uncollectable)			
Taxes Receivable	121,791	-	121,791
Accounts Receivable	537,808	934,307	1,472,115
Due from Other Governmental Units	9,079	20,838	29,917
Restricted Assets:			
Cash and Cash Equivalents	3,450,531	-	3,450,531
Receivables	97,133	-	97,133
Due from Other Governmental Units	12,003	-	12,003
Investment in Joint Venture	-	8,419,307	8,419,307
Capital Assets not being depreciated	6,560,190	3,369,086	9,929,276
Capital Assets (Net of Accumulated Depreciation)	19,659,744	35,302,110	54,961,854
Total Assets	34,348,078	55,112,888	89,460,966
LIABILITIES			
Accounts Payable	278,510	311,099	589,609
Contracts Payable		487,150	487,150
Deposits	-	350	350
Unearned Revenue	47,013	62,879	109,892
Other Accrued Liabilities	171,283	45,436	216,719
Liabilities Payable from Restricted Assets	51,011	-	51,011
Noncurrent Liabilities:			
Due within One Year	577,945	109,394	687,339
Due in More than One Year	1,208,587	472,856	1,681,443
Total Liabilities	2,334,349	1,489,164	3,823,513
DEFERRED INFLOWS of RESOURCES			
Deferred Amount on Refunding	5,806	759	6,565
Total Deferred Inflows of Resources	5,806	759	6,565
NET POSITION			
Net Investment in Capital Assets	25,470,825	38,165,873	63,636,698
Restricted for:			
Criminal Justice	354,091	-	354,091
Law Enforcement Investigative Funds	50,575	-	50,575
Tourism Promotion	50,991	-	50,991
Parks	165,812	-	165,812
McCormick Woods Park	174,793	-	174,793
Paths & Trails	3,245	-	3,245
Vacation abutting water	7,500	-	7,500
Transportation	1,273,957	-	1,273,957
Capital (REET)	1,361,938	-	1,361,938
Unrestricted	3,094,196	15,457,092	18,551,288
Total Net Position	\$ 32,007,923	\$ 53,622,965	\$ 85,630,888

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD

Statement of Activities

Year Ended December 31, 2014

Functions/Programs	Net (Expense) Revenue and Changes in Net Position				
	Program Revenues			Position	
	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities
PRIMARY GOVERNMENT					
Governmental Activities:					
General Government	\$ 2,100,241	\$ 240,400	\$ 158,784	\$ -	\$ (1,701,057)
Judicial	520,304	257,820	247	-	(262,237)
Public Safety	4,739,924	278,691	149,647	-	(4,311,586)
Transportation	2,043,972	124,025	265,458	34,969	(1,619,520)
Social Services	13,453	-	-	-	(13,453)
Economic Development	573,920	285,360	-	-	(288,560)
Culture and Recreation	384,640	13,376	5,221	-	(366,043)
Interest on Long-Term Debt	30,746	-	-	-	(30,746)
TOTAL GOVERNMENTAL ACTIVITIES	10,407,200	1,199,672	579,357	34,969	(8,593,202)
Business-Type Activities:					
Water - Sewer	4,877,932	5,114,006	-	-	422,870
Storm Drainage	940,124	836,717	50,000	-	66,594
TOTAL BUSINESS-TYPE ACTIVITIES	5,818,056	5,950,723	50,000	-	489,464
Total Primary Government	\$ 16,225,256	\$ 7,150,395	\$ 629,357	\$ 341,764	(8,103,738)
General Revenues:					
Taxes:					
Property Taxes Levied for General Purposes				2,225,347	-
Other Taxes				619,404	-
Sales and Use Taxes				4,102,060	-
Business and Occupation Taxes				1,645,063	-
Unrestricted Investment Earnings				41,397	18,962
Miscellaneous				-	33
Transfers				5,804	(5,804)
Total General Revenues and Special Items				8,639,075	13,191
Change in Net Position				45,873	502,655
Net Position - Beginning				32,026,165	53,412,160
Prior Period Adjustments				(64,115)	(291,850)
Net Position - Ending				\$ 32,007,923	\$ 53,622,965
					\$ 85,630,888

The notes to the financial statements are an integral part of this statement.

CITY OF PORT ORCHARD
Governmental Funds
Balance Sheet
December 31, 2014

	General Fund	Cumulative Reserve for Municipal Facilities	Street Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
Assets:					
Cash and Cash Equivalents	\$ 3,606,662	\$ 1,386,655	\$ 732,672	\$ 1,624,341	\$ 7,350,330
Property Taxes Receivables (net)	121,791	-	-	-	121,791
Accounts Receivable	537,808	-	1,520	95,613	634,941
Due from Other Governmental Units	9,079	8,090	3,913	-	21,082
Total Assets	4,275,340	1,394,745	738,105	1,719,954	8,128,144
Liabilities, Deferred Inflows of Resources, and Fund Balances:					
Liabilities:					
Accounts Payable	278,510	32,807	3,049	15,155	329,521
Other Accrued Liabilities	166,074	-	-	2,982	169,056
Unearned Revenue	47,013	-	-	-	47,013
Total Liabilities	491,597	32,807	3,049	18,137	545,590
Deferred Inflows of Resources					
Unavailable Revenue-Property Taxes	113,343	-	-	-	113,343
Unavailable Revenue-Court	464,785	-	-	58,548	523,333
Unavailable Revenue-Impact Fees	-	-	-	37,065	37,065
Total Deferred Inflows of Resources	578,128	-	-	95,613	673,741
Fund Balances:					
Restricted for:					
Criminal Justice	-	-	-	354,091	354,091
Law Enforcement	-	-	-	50,575	50,575
Tourism	-	-	-	50,991	50,991
Parks	-	-	-	165,812	165,812
McWds Parks	-	-	-	174,793	174,793
Paths & Trails	-	-	-	3,245	3,245
Vacation abutting water	7,500	-	-	-	7,500
Transportation	-	-	735,056	501,836	1,236,892
Capital Projects	-	1,361,938	-	-	1,361,938
Committed to:					
Recreation	287,818	-	-	-	287,818
Stabilization	519,179	-	-	-	519,179
Assigned to:					
Parks	86,615	-	-	-	86,615
City Hall	33,610	-	-	-	33,610
Street	836,313	-	-	-	836,313
Capital Equipment Replacement	-	-	-	304,861	304,861
Unassigned	1,434,580	-	-	-	1,434,580
Total Fund Balances	3,205,615	1,361,938	735,056	1,606,204	\$ 6,908,813
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	\$ 4,275,340	\$ 1,394,745	\$ 738,105	\$ 1,719,954	

The notes to the financial statements are an integral part of this statement

Amounts reported for governmental activities in the statement of net position are different because (See Note 2 also):

Capital assets used in governmental activities are not
financial resources and therefore are not reported in the
funds

26,219,934

Unavailable revenue to pay current year expenditures

673,741

Long-term liabilities that are not due and payable in the
current period and are not reported in the funds

(1,794,565)

Net position of governmental activities

\$ 32,007,923

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD
Governmental Funds
Statement of Revenues, Expenditures and Changes in Fund Balances
For the year ended December 31, 2014

	General Fund	Cumulative Reserve for Municipal Facilities	Street Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
Revenues:					
Property Taxes	\$ 2,237,909	\$ -	\$ -	\$ -	\$ 2,237,909
Retail Sales and Use Taxes	3,852,759	-	-	249,301	4,102,060
Other Taxes	1,751,842	512,625	-	-	2,264,467
License and Permits	278,962	-	-	-	278,962
Intergovernmental	461,608	21,341	26,847	104,531	614,327
Charges for Services	417,482	166	-	-	417,648
Fines and Forfeits	239,125	-	164	4,217	243,506
Interest Earnings	31,429	7,483	2,975	4,888	46,775
Rents and Royalties	133,377	-	-	-	133,377
Planning & Development Contributors	-	-	-	79,020	79,020
Contributions/Donations	5,105	-	-	-	5,105
Miscellaneous	8,374	-	-	3,161	11,535
Total Revenues	9,417,972	541,615	29,986	445,118	10,434,691
Expenditures:					
Current					
General Government	1,885,104	-	-	-	1,885,104
Judicial	520,304	-	-	-	520,304
Public Safety	4,272,266	-	-	134,196	4,406,462
Transportation	1,352,923	-	-	-	1,352,923
Economic Development	573,920	-	-	-	573,920
Social Services	13,453	-	-	-	13,453
Culture and Recreation	272,694	-	-	58,246	330,940
Capitalized Expenditures	131,369	469,889	62,564	157,538	821,360
Debt Service					
Principal Retirement	-	-	-	135,050	135,050
Interest/Fiscal Charges	-	-	-	31,112	31,112
Total Expenditures	9,022,033	469,889	62,564	516,142	10,070,628
Excess (Deficiency) of Revenues Over (Under) Expenditures	395,939	71,726	(32,578)	(71,024)	364,063
Other Financing Sources (Uses)					
Sale of Capital Assets	1,910	-	-	-	1,910
Transfers In	257,262	443,348	-	301,118	1,001,728
Insurance Recoveries	14,247	-	-	-	14,247
Transfers Out	(205,874)	(417,619)	-	(372,430)	(995,923)
Total Other Financing Sources and Uses	67,545	25,729	-	(71,312)	21,962
Net Change in Fund Balances	463,484	97,455	(32,578)	(142,336)	386,025
Fund Balance at Beginning of Year	2,742,131	1,328,598	767,634	1,748,540	6,586,903
Prior Period Adjustments	-	(64,115)	-	-	(64,115)
Fund Balance at End of Year	\$ 3,205,615	\$ 1,361,938	\$ 735,056	\$ 1,606,204	\$ 6,908,813

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balance
of Governmental Funds to the Statement of Activities
Year Ended December 31, 2014

Amounts reported for governmental activities in the statement of activities are different because:

Net changes in fund balances - total governmental funds:	\$ 386,025
 Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expenses. This is the amount by which capital outlays exceeded depreciation in the current period.	 (200,827)
 The net effect of various miscellaneous transactions involving capital assets (i.e., sales, trade-ins, and donations) to decrease net position.	 (8,901)
 Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	 27,169
 The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net position. Also, governmental funds report the effect of issuance costs, premiums, discounts and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. This amount is the net effect of these differences in the treatment of long-term debt and related items.	 135,050
 Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.	 (292,643)
 Changes in Net Position (governmental activities)	 <u>\$ 45,873</u>

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD
General Fund
Statement of Revenues, Expenditures and Changes in Fund Balances
Budget (GAAP Basis) and Actual
For the Fiscal Year Ended December 31, 2014

	Budgeted Amounts		Actual Amount	Variance with Final Budget
	Original	Final		
Revenues:				
Property Taxes	\$ 1,082,611	\$ 1,082,611	\$ 1,084,432	\$ 1,821
Sales and Use Taxes	3,723,000	3,829,000	3,852,759	23,759
Other Taxes	1,596,000	1,596,000	1,751,842	155,842
License and Permits	358,200	358,200	276,782	(81,418)
Intergovernmental	194,995	194,995	210,483	15,488
Charges for Services	371,000	371,000	397,447	26,447
Fines and Forfeits	266,800	266,800	239,125	(27,675)
Interest Earnings	16,200	16,200	27,221	11,021
Rents and Royalties	113,000	113,000	124,604	11,604
Contributions/Donations	1,500	1,500	5,000	3,500
Miscellaneous	-	-	8,524	8,524
Total Revenues	7,723,306	7,829,306	7,978,219	148,913
Expenditures:				
Current				
General Government	2,018,262	2,093,869	1,885,104	208,765
Judicial	550,931	572,301	520,304	51,997
Public Safety	4,222,748	4,497,093	4,272,266	224,827
Economic Development	620,308	643,878	573,920	69,958
Social Services	14,443	14,443	13,453	990
Culture and Recreation	350,889	340,894	272,694	68,200
Capitalized Expenditures	19,000	58,000	57,857	143
Intergovernmental Payments	-	-	-	-
Total Expenditures	7,796,581	8,220,478	7,595,598	624,880
Excess (Deficiency) of Revenues Over (Under) Expenditures	(73,275)	(391,172)	382,621	773,793
Other Financing Sources (Uses):				
Sale of Capital Assets	-	-	1,910	1,910
Compensation for Loss/Impair Capital Assets	-	-	-	-
Transfers In	50,000	62,997	62,880	(117)
Insurance Recoveries	-	-	5,878	5,878
Transfers Out	(803,478)	(842,234)	(495,620)	346,614
Total Other Financing Sources and Uses	(753,478)	(779,237)	(424,952)	354,285
Net Change in Fund Balance	(826,753)	(1,170,409)	(42,331)	1,128,078
Fund Balances at Beginning of Year	1,604,885	1,604,885	1,884,955	280,070
Prior Period adjustments	-	-	-	-
Fund Balances at End of Year	\$ 778,132	\$ 434,476	\$ 1,842,624	\$ 1,408,148
Adjustment to generally accepted accounting principles (GAAP) basis:				
City Street Fund			843,812	
Stabilization Fund			519,179	
Fund Balance - GAAP basis			<u>\$ 3,205,615</u>	

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD
Proprietary Funds
Statement of Net Position
December 31, 2014

	Major Enterprise Fund Water-Sewer	Major Enterprise Fund Storm Drainage	Total Business Activities
Assets:			
<i>Current Assets:</i>			
Cash and Cash Equivalents	\$ 6,236,368	\$ 830,872	\$ 7,067,240
Receivables (net)			
Accounts	\$ 808,866	125,441	934,307
Due from Other Governmental Units	\$ -	20,838	20,838
Total Current Assets	7,045,234	977,151	8,022,385
<i>Non Current Assets:</i>			
Investment in Joint Venture	\$ 8,419,307	-	8,419,307
Property, Plant and Equipment (Net)	\$ 29,594,257	9,076,939	38,671,196
Total Non Current Assets	38,013,564	9,076,939	47,090,503
Total Assets	45,058,798	10,054,090	55,112,889
Liabilities			
<i>Current Liabilities:</i>			
Accounts Payable	\$ 253,781	57,318	311,099
Contracts Payable	\$ 487,150	-	487,150
Other Accrued Liabilities	\$ 32,023	11,969	43,992
Deposits	\$ 350	-	350
Accrued Interest Payable	\$ 1,444	-	1,444
Accrued Employee Benefits	\$ 38,297	19,605	57,902
Bonds, Notes, Loans Payable	\$ 51,492	-	51,492
Total Current Liabilities	864,537	88,892	953,429
<i>Non Current Liabilities:</i>			
Bonds, Notes and Loan Payable (Net)	\$ 453,072	-	453,072
Accrued Employee Benefits	\$ 13,085	6,699	19,784
Unearned Revenues	\$ 62,879	-	62,879
Total Non Current Liabilities	529,036	6,699	535,735
Total Liabilities	1,393,573	95,591	1,489,164
Deferred Inflows of Resources			
Deferred Amounts on Refunding	\$ 759	-	759
Total Deferred Inflows of Resources	759	-	759
<i>Net Position</i>			
Net Invested in Capital Assets	29,088,934	9,076,939	38,165,873
Unrestricted	14,575,532	881,560	15,457,092
Total Net Position	\$ 43,664,466	\$ 9,958,499	\$ 53,622,965

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD
Proprietary Funds
Statement of Revenues, Expenses and Changes in Fund Net Position
For the Fiscal Year Ended December 31, 2014

	Major Enterprise Fund Water-Sewer	Major Enterprise Fund Storm Drainage	Total Business Activities
Operating Revenues			
Charge for Services	\$ 4,766,651	\$ 818,924	\$ 5,585,575
Fines & Penalties	73,559	16,644	90,203
Miscellaneous	57,782	1,150	58,932
Total Operating Revenues	4,897,992	836,718	5,734,710
Operating Expenses			
Operations			
General Operations	2,732,877	510,231	3,243,108
Water Purchased for Resale	16,951	-	16,951
Customer Service and Marketing	203,322	66,351	269,673
General Administration	890,782	178,348	1,069,130
Taxes	353,765	52,191	405,956
Depreciation, Amortization, Depletion	608,605	133,003	741,608
Total Operating Expenses	4,806,302	940,124	5,746,426
Operating Income (loss)	91,690	(103,406)	(11,716)
Nonoperating Revenues (Expenses)			
Interest Earnings	18,093	869	18,962
State and Federal Grants	-	50,000	50,000
Interest and Fiscal Charges	(71,630)	-	(71,630)
Net Income (Loss) of Joint Ventures	216,014	-	216,014
Miscellaneous Revenue (Expense)	-	33	33
Total Nonoperating Revenues (Expenses)	162,477	50,902	213,379
Income (Loss) before Contributions	254,167	(52,504)	201,663
Capital Contributions	186,796	120,000	306,796
Transfers Out	(4,742)	(1,062)	(5,804)
Increase (Decrease) in Net Position	436,221	66,434	502,655
Total Net Position at Beginning of Year	43,715,395	9,696,765	53,412,160
Prior Year Adjustment	(487,150)	195,300	(291,850)
Total Net Position at End of Year	\$ 43,664,466	\$ 9,958,499	\$ 53,622,965

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD
Proprietary Funds
Statement of Cash Flows
For the Fiscal Year Ended December 31, 2014

	Major Enterprise Fund Water-Sewer	Major Enterprise Fund Storm Drainage	Total Business Activities
Cash Flows from Operating Activities:			
Cash Received from Customers	\$ 4,873,863	\$ 845,522	\$ 5,719,385
Cash Payments to Suppliers	(2,448,438)	(262,429)	(2,710,867)
Cash Payments to Employees	(1,229,592)	(429,242)	(1,658,834)
Cash Payments to other Governments (Taxes)	(353,765)	(52,191)	(405,956)
Net Cash Provided by Operating Activities	842,068	101,660	943,728
Cash Flows from Noncapital Financing Activities:			
Receipt of Grant Funds	-	50,000	50,000
Operating Transfers - Out	(4,742)	(1,062)	(5,804)
Net Cash Provided (Used) by Noncapital Financing Activities	(4,742)	48,938	44,196
Cash Flows from Capital and Related Financing Activities:			
Acquisition and Construction of Capital Assets	(184,318)	(152,165)	(336,483)
Principal Paid on GO Bond	(49,950)	-	(49,950)
Principal Paid on Other Long-Term Obligations	(700)	-	(700)
Interest Paid on Revenue Bonds and Other Long-Term Debt	(11,506)	-	(11,506)
Receipt of Capital Contributions	186,796	136,777	323,573
Net Cash Provided for Capital and Related Financing Activities	(59,678)	(15,388)	(75,066)
Cash Flows from Investing Activities:			
Interest on Investments	18,093	869	18,962
Net Cash Used by Investing Activities	18,093	869	18,962
Net Increase (Decrease) in Cash and Cash Equivalents	795,741	136,079	931,820
Cash and Cash Equivalents at Beginning of Year	5,440,627	694,793	6,135,420
Cash and Cash Equivalents at End of Year	6,236,368	830,872	7,067,240
Cash and Cash Equivalents	6,236,368	830,872	7,067,240
Total Cash and Cash Equivalents	\$ 6,236,368	\$ 830,872	\$ 7,067,240

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD
Proprietary Funds
Statement of Cash Flows
For the Fiscal Year Ended December 31, 2014

	Major Enterprise Fund Water-Sewer	Major Enterprise Fund Storm Drainage	Total Business Activities
Reconciliation of Operating Income (Loss) to Net			
Cash Used by Operating Activities:			
Net Operating Income (Loss)	\$ 91,690	\$ (103,406)	\$ (11,716)
Adjustments to Reconcile Net			
Operating Income (Loss) to Net			
Cash Provided by Operations:			
Depreciation Expense	608,605	133,003	741,608
(Increase) Decrease in Receivables	(22,522)	8,771	(13,751)
Increase (Decrease) in Current Payables	140,265	50,170	190,435
Increase (Decrease) in Other Current Payables	32,023	11,969	43,992
Increase (Decrease) in Accrued Employee Benefits	(6,386)	1,120	(5,266)
Increase (Decrease) in Customer Deposits	(850)	-	(850)
Increase (Decrease) in Unearned Revenues	(757)	-	(757)
Increase (Decrease) Non Operating Revenues	-	33	33
Total Adjustments	750,378	205,066	955,444
Net Cash Provided by Operating Activities	\$ 842,068	\$ 101,660	\$ 943,728
Noncash Investing, Financing and Capital Activities			
Capital Assets - Donated /Grants Received	-	120,000	120,000
Capital Assets - Annexations	-	195,300	195,300
Gain / (Loss) on Joint Venture	216,014	-	216,014
Debt Issuance Costs	60,000		60,000
Total Noncash Investing, Financing and Capital Activities	\$ 276,014	\$ 315,300	\$ 591,314

The notes to the financial statements are an integral part of this statement

CITY OF PORT ORCHARD
Statement of Fiduciary Net Position
Fiduciary Funds
December 31, 2014

	Agency Funds
Assets:	
<i>Current Assets:</i>	
Cash and Cash Equivalents	\$ 2,793,907
Total Assets	<u>2,793,907</u>
 Liabilities	
Accounts Payable	16,738
Custodial Accounts	<u>2,777,169</u>
Total Liabilities	<u>\$ 2,793,907</u>

The notes to the financial statements are an integral part of this statement

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the City of Port Orchard have been prepared in conformity with Generally Accepted Accounting Principles (GAAP) as applied to governmental units. The Governmental Accounting and Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The significant accounting policies are described below.

A. REPORTING ENTITY

The City of Port Orchard, Washington was incorporated on September 1, 1890 and operates under the laws of the state of Washington applicable to non-charter code cities (second-class city) with a Mayor/Council form of government. As required by the Generally Accepted Accounting Principles the financial statements represent the City of Port Orchard. The City has no component units.

B. GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the nonfiduciary activities of the primary government. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segments are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements or a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate fund financial statements are provided for governmental funds, proprietary funds and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

C. MEASUREMENT FOCUS, BASIS OF ACCOUNTING AND FINANCIAL STATEMENT PRESENTATION

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the city considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. The city considers property taxes as available if they are collected with 60 days after year end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, licenses and interest associated within the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the City.

The City reports the following major governmental funds:

The general (or current expense) fund is the city's operating fund. It accounts for all financial resources of the general government, except those required or elected to be accounted for in another fund. Included and reported in the General Fund are two managerial funds one of those is the City Street fund which accounts for a percentage of the revenue from state motor vehicle fuel taxes and expenditures for street construction, maintenance and repair. This fund accounts for transportation activities that the City Council wants to review separately from other activities. The other fund included in the General fund is the Stabilization fund.

The Cumulative Reserve for Municipal Facilities is a capital projects fund used to account for financial resources, including Real Estate Excise Tax (REET), to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds and trust funds). REET is imposed on the sale of real property. The first quarter percent is dedicated to local capital projects as identified in RCW 82.46. The second quarter percent shall be used solely for financing capital projects specified in a capital facilities plan element of a comprehensive plan. In 2011 legislature expanded, for a limited period of time, the uses of REET both the first and second quarter. Cities may now, with restrictions, use REET 1 & 2 for operation and maintenance of existing capital facilities. This new authority expires on December 31, 2016. Cumulative Reserve for Municipal Facilities also accounts for grant funding for facility improvements.

The Street Capital Projects fund is used for the receipt and expenditure of a percentage of the state levied motor vehicle fuel taxes distributed to the City. The City utilizes these revenues as matching funds for grants specified for arterial street purposes. These are restricted revenue sources. Projects that use this tax are reflected on the six-year transportation improvement program as passed annually by Council.

The government reports the following major proprietary funds:

The Water Sewer fund accounts for the activity of the City's utilities. Its revenues are received from the sales of water and sewer services. Expenses are for the maintenance and extensions of water and sewer service facilities, operating a water supply system, maintaining a sewer treatment plant and lift stations.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

The Storm Drainage Fund monitors and maintains the City's storm and surface water drainage. Revenues are based on fees received from properties within City limits that have impervious surfaces. Expenses are for operation, maintenance and improvement of the City's storm and surface water drainage system.

Fiduciary funds represent assets held in a trustee or agency capacity for others and do not report results of operation.

The City has two fiduciary funds. The Wastewater Treatment Facility Fund receives money from the joint venture to repay the Public Works Trust Fund loans. Also deposited into this fund are the Wastewater Treatment Facility Fees component of the Sewer Capital Facility Charge and interest earnings on such funds. These dollars are held in trust to mitigate the debt and future construction costs for the Wastewater Treatment Facility. The Trust and Agency Fund collects fees which the Treasurer, acting as an intermediary depository, shall distribute to the proper agencies on a regular and timely basis. Examples of these fees include but are not limited to state court fines, county crime victim fines, state building code fees, state concealed pistol licenses and background checks.

Additionally, the government reports the following fund types:

Special revenue funds are used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service or capital projects.

Debt service funds are used to account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest.

Capital project funds are used to account for and report for financial resources that are restricted, committed, or assigned to expenditure for capital outlays, including the acquisition or construction of capital facilities and other capital assets.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes and other charges between the government's water, sewer and storm functions and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as program revenues include 1) charges to customers 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than as program revenues. General revenues include all taxes, except those that are credited to their appropriate restricted fund.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the enterprise funds are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, and then unrestricted resources as they are needed.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

D. BUDGETARY INFORMATION

1. Scope of Budget

Annual appropriated budgets are adopted for the general fund, special revenue funds, debt service funds, and capital project funds on the modified accrual basis of accounting. Budgets for debt service and capital project funds are adopted at the level of the individual debt issue or project and for fiscal periods that correspond to the lives of debt issues or projects. The budgetary basis of accounting differs from generally accepted accounting principles. The City budgets the City Street activity and Stabilization activity as if they were special revenue funds. However, GAAP requires these activities to be reported with the General Fund, as they do not have significant streams of restricted resources. From a budgetary perspective, the City budgets for City Street activity and Stabilization activity separate from the General Fund. The budgetary comparison for the General Fund does not include the managerial funds.

Proprietary funds are budgeted on the full accrual basis for management control purposes only. Appropriations lapse at year-end.

2. Amending the Budget

The City Treasurer is authorized to transfer budgeted amounts between departments within any fund; however any revisions that alter the total expenditures of a fund or that affect the number of authorized employee positions, salary ranges, hours, or other conditions of employment must be approved by the City Council.

When the City Council determines that it is in the best interest of the City to increase or decrease the appropriations for a particular fund, it may do so by ordinance approved by one more than the majority after holding public hearing(s).

The budget amounts shown in the financial statements are the final authorized amounts as revised during the year.

The financial statements contain the original and final budget information. The original budget is the first complete appropriated budget. The final budget is the original budget adjusted by all reserves, transfers, allocations, supplemental appropriations, and other legally authorized changes applicable for the fiscal year.

E. ASSETS, LIABILITIES, FUND BALANCE, NET POSITION

1. Cash & Cash Equivalents

It is the city's policy to invest all temporary cash surpluses. At December 31, 2014, the treasurer was holding \$16,179,411 in short-term, residual investments of surplus cash. This amount is classified on the balance sheet as cash and cash equivalents in various funds. The interest on these investments is prorated to the various funds.

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 2014 were approximately \$871,988.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

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

2. Investments See Note 3. Deposits and Investments

3. Receivables

Property tax revenues are recognized when cash is collected. The amount of taxes receivable at year-end that would be collected soon enough to be available to pay the liabilities of the current period is immaterial.

The Kitsap County Treasurer acts as an agent to collect property taxes levied in the county for all taxing authorities. Taxes are levied annually before December 15, and become a lien as of January 1, on property value listed as of the prior May 31. Assessed values are established by the County assessor at 100 percent of fair market value. A physical inspection of all property is required at least every six years with annual review and update based on sales analysis.

Taxes are due in two equal installments on April 30 and October 31. The county treasurer remits collections monthly to the appropriate district. Taxes receivable consists of property taxes and related interest and penalties. (See Note 4)

Special assessments are recorded when levied. Special assessments receivable consists of current and delinquent assessments and related interest and penalties. Assessments consist of unbilled special assessments that are liens against the property benefited. There were no outstanding special assessments receivables at December 31, 2014.

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. Notes and contracts receivable consist of amounts owed on open accounts from private individuals or organizations for goods and services rendered.

4. Amounts Due to and from Other Funds and Governments, Interfund Loans and Advances Receivable

Activities between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either interfund loans receivable/payable or advances to/from other funds. All other outstanding balances between funds are reported as due to/from other funds. Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as internal balances. In 2014, there were no interfund loans receivable and payable.

5. Inventories

Inventories in governmental and proprietary funds consist of expendable supplies held for consumption. The cost is recorded as an expenditure at the time individual items are purchased.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

6. Restricted Assets and Liabilities

These accounts contain resources for programs, construction, and impact fees. The current portion of related liabilities is shown as Payables from Current Restricted Assets. Specific debt service reserve requirements are described in Note 10, Long-Term Debt.

7. Capital Assets See Note 5, Capital Assets

Capital assets, which include property, intangible assets, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the City as assets with an initial, individual cost of more than \$4,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

Costs for additions or improvements to capital assets are capitalized when they increase the effectiveness or efficiency of the asset.

The costs of normal maintenance and repairs are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Property, plant and equipment are depreciated using the straight line method over the following estimated useful lives:

<u>Asset Category</u>	<u>Useful Life</u>
Buildings	50
Infrastructure	10-40
Intangible Assets	6
Utility Improvements	10-100
Mowers/Public Works Equipment	6-12
Vehicles	5

The City 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 City has sufficient legal interest to accomplish the purposes for which the assets were acquired, and has included such assets within the applicable column in the statement of net position.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

8. Deferred Outflows/Inflows of Resources

Governmental funds report deferred inflows of resources in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period.

	<u>Unavailable</u>
Delinquent property taxes receivable (general)	\$ 113,343
Cout receivables-not yet collected (general)	464,785
Court Receivables-not yet collected (nonmajor governmental funds)	58,548
Impact Fees-not yet collected (nonmajor governmental funds)	37,065
Total	<u>\$ 673,741</u>

The deferred inflow of resources recognized in the government-wide financial statements is a deferred amount on refunding of debt that will be amortized over the life of the refunding bond issue.

9. Unearned Revenue

Governmental funds also defer revenue recognition in connection with resources that have been received, but have not yet been earned.

	<u>Unearned</u>
South Kitsap School District-School Resource Officer Program	\$ 40,596
Kitsap Transit Prepaid Lease-not yet earned	6,417
Total	<u>\$ 47,013</u>

10. Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation and compensated time. In governmental funds, compensated absences that are expected to be liquidated with expendable available financial resources are reported as an expenditure. In prior years the General Fund has typically been used to liquidate compensated absences. In proprietary funds, compensated absences are recorded as an expense and liability of the fund that will pay for them.

For all employees except LEOFF II employees, vacation pay, which may be accumulated up to 30 days at December 31, is payable upon resignation, retirement or death (upon termination, pay is limited to 240 hours). There is no cap on the amount of payment for accrued vacation for LEOFF II employees (excluding management) upon termination. LEOFF II employees (excluding management) earn 120 hours holiday leave annually and may carry over 96 hours at

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

December 31. There is no cap on the holiday leave payable upon resignation, retirement or death. Sick leave may be accumulated up to 960 hours and is not payable upon resignation, retirement or death for all employees except LEOFF II (excluding management). LEOFF II employees (excluding management) can accumulate more than 960 hours during the year, but may only carry over 960 hours from one year to the next. Effective October 1, 2014 all LEOFF II employees (excluding management) may elect to cash out up to 400 hours of accrued but unused sick leave, upon permanent separation from the City due to the employee's death, disability or voluntary termination. Any such sick leave cash out payments shall be made directly to respective employees medical health retirement/voluntary employee's beneficiary association account (HRA/VEBA). The remainder shall be forfeited without compensation.

11. Other Accrued Liabilities

These accounts consist of accrued wages, accrued taxes, accrued employee benefits, and accrued interest payable.

12. Long-Term Debt See Note 10, Long Term Debt

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities or proprietary fund type statement of net position. Bond premiums (discounts) are amortized over the life of the bonds. Bonds payable are reported net of the applicable bond premium (discount).

In the fund financial statements, governmental fund types recognize bond premium (discounts) during the current period. The face amount of debt issued is reported as other financing sources while discounts on debt issuances are reported as other financing uses.

13. Fund Balance Classification

The City presents fund balance classifications as follows:

- Restricted fund balance: includes amounts that can be spent only for the specific purposes stipulated by external resource providers (for example, grant providers), constitutionally, or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.
- Committed fund balance: includes amounts that can be used only for specific purposes determined by formal action of the government's highest level of decision-making authority. The City Council enacts ordinances and resolutions that may impose, modify or rescind fund balance commitments. Commitments may be changed or lifted only by the government taking the same formal action that imposed the constraint originally.
- Assigned fund balance: comprises amounts intended to be used by the government for specific purposes. Intent can be by City Council action or by the City Treasurer. In governmental funds other than the general fund, assigned fund balance represents the amount that is not restricted or committed. This indicates that resources in other governmental funds are, at a minimum, intended to be used for the purpose of that fund.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

- Unassigned fund balance, is the residual classification for the general fund and includes all amounts not contained in the other classifications. Unassigned amounts are technically available for any purpose. If another governmental fund has a fund balance deficit, then it will be reported as a negative amount in the unassigned classification in that fund. Positive unassigned amounts will be reported only in the general fund.
- When both restricted and unrestricted resources are available, the City's policy is to use restricted resources first, and then unrestricted resources, as they are needed. When committed, assigned or unassigned amounts are available, the City's policy is to use committed resources first, assigned secondly and finally unassigned resources.

14. Fund Balance Details

Reserve Policies

The City will maintain the reserves, contingencies, and ending fund balances of the various operating funds at levels sufficient to protect the City's credit as well as its financial position from emergencies.

General Fund Reserves

The City recognizes that reserves need to be acquired over multiple budget years, and require discipline and a strong commitment to maintain them.

Reserves are a necessary component of the overall finance management strategy of the City. Reserves serve a variety of purposes; 1) Ensuring adequate resources for cash flow, 2) Mitigating short-term effects of revenue shortages, 3) Leveraging beneficial opportunities, 4) Providing the ability to exercise flexible financial planning, and 5) To address unforeseen emergencies or changes in conditions.

The City will strive to maintain a two tier reserve structure.

- Assigned Ending Fund Balance designated as working capital in the general fund
- Stabilization Arrangement reported as restricted or committed in the general fund

Working Capital

The City's goal shall be to maintain an undesignated General Fund ending fund balance of at least five percent of budgeted General Fund operating revenues. Ending fund balance may be used to cover cash flow needs caused by the ad valorem tax cycle which results in the traditional "W" cash flow sequence. Ending fund balance reserve is considered working capital of the General Fund.

F. OTHER

1. Stabilization Arrangement

A City Stabilization Arrangement in an amount of two months of its five year arithmetic mean of General Fund expenditure budget may be maintained annually as resources allow. Funding may

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

come from one time revenues, monthly budgeted amounts from general revenues, and transfers from ending fund balance as authorized by Council resolution.

Stabilization reserves shall be used if all efforts have been exhausted to fund a qualifying event and no reasonable budget adjustments are available to continue to provide essential services to the public. The City Treasurer must quantify, document and present the significance of the qualifying event. Authorization for spending stabilization reserves requires a simple majority vote of the City Council.

Qualifying Events:

- The state of Washington or Federal government formally declares a disaster or emergency.
- A natural or urgent event that jeopardizes public safety, impedes commerce, or threatens additional damage to City infrastructure.
- Unforeseen events or situation outside of the scope of contingency, planning or planned normal course of government operations.
- An act of war, terrorism, or declaration of Martial law.

NOTE 2. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

A. EXPLANATION OF CERTAIN DIFFERENCES BETWEEN THE GOVERNMENTAL FUNDS BALANCE SHEET AND THE GOVERNMENT-WIDE STATEMENT OF NET POSITION

The governmental funds' balance sheet includes reconciliation between fund balance—total governmental funds and net position—governmental activities as reported in the government-wide statement of net position.

One element of that reconciliation explains that “long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.” The details of this difference are as follows:

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

Bonds Payable	\$ 740,950
Plus: Deferred charge on refunding (to be amortized as interest expense)	5,806
	2,353
Plus: Issuance premium (to be amortized as interest expense)	
Accrued interest payable	2,227
Other post employment benefits	454,602
Compensated absences	588,627
Net adjustment to reduce fund balance-total governmental funds to arrive at net position-governmental activities	<u><u>\$ 1,794,565</u></u>

B. EXPLANATION OF CERTAIN DIFFERENCES BETWEEN THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES AND THE GOVERNMENT-WIDE STATEMENT OF ACTIVITIES

The governmental funds' statement of revenues, expenditures and changes in fund balances includes reconciliation between net changes in fund balances—total governmental funds and changes in net position of governmental activities as reported in the government-wide statement of activities.

One element of that reconciliation explains, “governmental funds report capital outlays as expenditures.” However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. The details of this difference are as follows:

Current Year Capital outlay	\$ 821,360
Current Year Depreciation expense	(1,022,187)
Net adjustment to decrease net changes in fund balances-total governmental funds to arrive at change in net position of governmental activities	<u><u>\$ (200,827)</u></u>

Another element of that reconciliation is the net effect of various miscellaneous transactions involving capital assets (i.e., sales, trade-ins, and donations) to increase net position. The details of this are as follows:

Sale of Capital Assets	\$ (1,910)
Gain on Sale of Capital Assets	(6,991)
Increase in Net Position	<u><u>\$ (8,901)</u></u>

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

Another element of that reconciliation states that “revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.” The details of this are as follows:

Municipal Court & Non-major fund revenues	\$ 2,666
Tax revenues - unavailable	(12,562)
Impact Fees	37,065
Net adjustment to increase net changes in fund balances-	\$ 27,169
total governmental funds to arrive at changes in net position of governmental activities	

Another element of that reconciliation states “some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.” The details of this are as follows:

Accrued interest	\$ 366
Employee benefits accrual	(208,386)
Amortization of deferred amount on refunding	1,266
Amortization of bond premiums	522
OPEB	(86,411)
Net adjustment to decrease net changes in fund balances-	\$ (292,643)
total governmental funds to arrive at changes in net position of governmental activities	

NOTE 3. DEPOSITS AND INVESTMENTS

A. DEPOSITS

The City’s deposits are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC). The City has no policy related to custodial credit risk; however, all deposits are insured or collateralized with securities held by the entity or by the agent in the City’s name.

The Washington State Treasurer’s Office Local Government Investment Pool is classified as a 2(a) 7 investment pool, and therefore the City states the fair value of its investment in the pool based upon the share price of the pool. The taxes and fees collected by the Kitsap County Treasurer, on behalf of the City, are deposited directly into the Kitsap County Investment Pool and credited to the City. The City considers the amount invested in the government investment pools to be liquid investments, and as such are cash equivalents.

The book value of deposits does not materially differ from the bank balance of deposits.

As of December 31, 2014, the City’s cash and cash equivalents is as follows:

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

Cash & Cash Equivalents	City	Fiduciary	Total
Cash on hand	\$ 3,750		\$ 3,750
Cash deposits in bank accounts	1,007,157	\$ 16,935	1,024,092
Cash deposits in bank accounts-SHIP	4,224		4,224
Washington State Local Government Investment Pool	4,419,246		4,419,246
Kitsap County Investment Pool	6,579,777	1,584,857	8,164,634
Kitsap Bank Money Market	2,403,416	1,192,115	3,595,531
Total Cash and Cash Equivalents	\$14,417,570	\$ 2,793,907	\$17,211,477

B. INVESTMENTS

As required by state law, all investments of the City's funds are obligations of the U.S. Government, U.S. agency issues, obligations of the state of Washington, general obligations of Washington State municipalities, or certificates of deposit with Washington State banks and savings and loan institutions. All temporary investments are stated at fair value. The only investments made by the City are with the Washington State Treasurer's Office Local Government Investment Pool (LGIP), Kitsap County Investment Pool, and Kitsap Bank which are classified as cash equivalents. The LGIP and County Investment Pool are unrated external investment pools.

Further, the City is not subject to foreign currency risk or interest rate risk.

NOTE 4. PROPERTY TAX

The Kitsap 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.
July 31	New construction valued as of July 31 st of the assessment year.
October 31	Second Installment is due.

Property taxes revenues are recognized when cash is collected. The amount of taxes receivable at year-end that would be collected soon enough to be available to pay liabilities of the current period is immaterial. The balance at year-end is recorded as taxes receivable.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

The City is permitted by law to levy up to \$3.60 per \$1,000 of assessed valuation for general governmental services. The City is annexed to South Kitsap Fire and Rescue and Kitsap Regional Library. South Kitsap Fire may levy up to \$1.50, Kitsap Regional Library may levy up to \$0.50; the difference of South Kitsap Fire's levy and Kitsap Regional Library's levy, and \$3.60 is the City's capacity.

The City's regular levy for 2014 was \$1.697917 per \$1,000 on an assessed valuation of \$1,319,792,155 for a total regular levy of \$2,240,898.

For 2014, the City levied the following property taxes:

Purpose of Levy	Levy Rate per \$1,000	Total Levy Amount
Port Orchard City	1.697917	2,240,898
State School Levy	2.472372	3,263,017
Kitsap County CE	1.235616	1,630,756
PUD	0.085440	112,763
Port of Bremerton	0.394390	520,513
SK Schools	3.638812	4,802,476
SK Fire & Rescue	2.000000	2,639,584
Kitsap Regional Library	0.402083	530,666
Totals	11.926630	15,740,673

Special levies approved by the voters are not subject to the limitations listed above. In 2014, there were no outstanding voter approved bonds, therefore there was no additional levy.

Washington State Constitution and Washington State Law, RCW 84.55.010 limit the rate.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

NOTE 5. CAPITAL ASSETS

A. CAPITAL ASSETS

A summary of capital asset activity for the year ended December 31, 2014 was as follows:

	Beginning Bal. 01/01/14	Increases	Decreases	Ending Bal. 12/31/14
Governmental activities:				
Capital assets, not being depreciated				
Land and other improvements	\$ 1,706,176	\$ 5,200	\$ 1,048	\$ 1,710,328
Intangible Assets	3,025,798	-	-	3,025,798
Construction in progress	1,852,353	365,506	393,795	1,824,064
Total capital assets, not being depreciated	6,584,327	370,706	394,843	6,560,190
Capital assets, being depreciated/depleted:				
Buildings	7,329,317	91,949	-	7,421,266
Equipment	2,929,877	278,239	155,195	3,052,921
Infrastructure	28,941,238	474,261	-	29,415,499
Intangible Assets	79,609	-	-	79,609
Total capital assets being depreciated	39,280,041	844,449	155,195	39,969,295
Less accumulated depreciation for:				
Buildings	2,002,205	162,435	-	2,164,640
Equipment	2,068,837	179,007	147,342	2,100,502
Infrastructure	15,304,209	676,025	-	15,980,234
Intangible Assets	59,455	4,720	-	64,175
Total accumulated depreciation	19,434,706	1,022,187	147,342	20,309,551
Total capital assets, being depreciated, net	19,845,335	(177,738)	7,853	19,659,744
Governmental activities capital assets, net	\$ 26,429,662	\$ 192,968	\$ 402,696	\$ 26,219,934

Depreciation expense was charged to functions/programs of the primary government as follows:

Governmental activities:	
General government	\$ 140,332
Security of persons and property	112,357
Transportation	715,798
Physical environment	-
Culture and recreation	53,700
Total depreciation expense—governmental activities	\$ 1,022,187

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

	Beginning Bal. 01/01/14	Increases	Decreases	Ending Bal. 12/31/14
Business-type Activities:				
Capital assets, not being depreciated				
Land and other improvements*	\$ 787,012	\$ -	\$ -	\$ 787,012
Intangible Assets	458,409	-	-	458,409
Construction in progress	1,958,020	165,645	-	2,123,665
Total capital assets, not being depreciated	3,203,441	165,645	-	3,369,086
Capital assets, being depreciated/depleted:				
Buildings	3,819,454	129,231	-	3,948,685
Equipment	4,570,327	32,930	6,684	4,596,573
Infrastructure*	38,009,295	42,639	-	38,051,934
Intangible Assets	128,033	-	-	128,033
Total capital assets being depreciated	46,527,109	204,800	6,684	46,725,225
Less accumulated depreciation for:				
Buildings	1,010,239	79,219	-	1,089,458
Equipment	3,171,935	186,431	6,684	3,351,682
Infrastructure	6,469,149	465,233	-	6,934,382
Intangible Assets	36,867	10,726	-	47,593
Total accumulated depreciation	10,688,190	741,609	6,684	11,423,115
Total capital assets, being depreciated, net	35,838,919	(536,809)	-	35,302,110
Business-type activities capital assets, net	\$ 39,042,360	\$ (371,164)	\$ -	\$ 38,671,196

*The beginning balance for Land and Infrastructure are restated due to additional assets received in 2014 from Kitsap County as part of the 2012 Bethel Annexation.

Depreciation expense was charged to functions/programs of the primary government as follows:

Business-type activities:	
Water-Sewer	\$ 608,606
Storm Drainage	133,003
Total depreciation expense-business-type activities	\$ 741,609

NOTE 6. CONSTRUCTION AND OTHER SIGNIFICANT COMMITMENTS

A. Construction Commitments

The City of Port Orchard has active construction projects as of December 31, 2014.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

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

2014 Governmental Construction in Progress Activity:

Project	Spent to Date	Remaining Commitment
Bay Street Pedestrian Path	\$ 364,154	\$ 215,056
Tremont Street Widening	1,459,910	8,097
Total	\$ 1,824,064	\$ 223,153

2014 Business-type Construction in Progress Activity:

Project	Spent to Date	Remaining Commitment
Marina Pump Station	\$ 48,118	\$ -
Tremont Widening Water Mains	29,656	-
Tremont Widening Sewer Mains	29,656	-
Water Rights & 2nd Wa Rights-Well #10	85,012	-
Well #9	1,110,488	-
Well #10	283,957	1,171,171
Well #11	536,778	-
Total	\$ 2,123,665	\$ 1,171,171

NOTE 7. PENSION PLANS

Substantially all City of Port Orchard 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, P.O. Box 48380, Olympia, WA 98504-8380; or it may be downloaded from the DRS website at www.drs.wa.gov.

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

Plan Description

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

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; employees of district and municipal courts; and employees of local governments. Membership also includes higher education employees not participating in higher education retirement programs. Approximately 49 percent of PERS salaries are accounted for by state employment. PERS retirement benefit provisions are established in Chapters 41.34 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.

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 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 2013, 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, in lieu of any retirement benefit, 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 from active status at any age with at least 30 years of service, at age 55 with 25 years of service, or at age 60 with at least 5 years of service. Plan 1 members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits.

The monthly benefit is 2 percent of the average final compensation (AFC) per year of service, but the benefit may not exceed 60 percent of the AFC. The AFC is the monthly average of the 24 consecutive highest-paid service credit months.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

PERS Plan 1 retirement benefits are actuarially reduced to reflect the choice, if made, of a survivor option.

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 percent 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 percent of the AFC for each year of service reduced by 2 percent for each year that the member's age is less than 55. The total benefit is limited to 60 percent 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 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

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 percent 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 percent 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, if hired prior to May 1, 2013:

- With a benefit that is reduced by 3 percent 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 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of 5 percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

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

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 percent to 15 percent of salaries, based on member choice. Members who do not choose a contribution rate default to a 5 percent rate. 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 contributions are invested in the Retirement Strategy Fund that assumes the member will retire at age 65.

For DRS' Fiscal Year 2013, PERS Plan 3 employee contributions were \$99.0 million, and plan refunds paid out were \$69.4 million.

The defined benefit portion of PERS Plan 3 provides members a monthly benefit that is 1 percent 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, and were hired before May 1, 2013, they have the choice of a benefit that is reduced by 3 percent 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.
- If they have 30 service credit years, are at least 55 years old, and were hired after May 1, 2013, they have the option to retire early by accepting a reduction of 5 percent for each year before age 65.

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

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

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 percent of the AFC per year of service. For Plan 3, the monthly benefit amount is 1 percent 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 percent annually.

PERS members meeting specific eligibility requirements have options available to enhance their retirement benefits. Some of these options are available to their survivors.

A one-time duty-related death benefit is provided to the beneficiary or the estate of a PERS member who dies 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.

From January 1, 2007 through December 31, 2007, judicial members of PERS were given the choice to elect participation in the Judicial Benefit Multiplier (JBM) Program enacted in 2006. Justices and judges in PERS Plan 1 and Plan 2 were able to make an irrevocable election to pay increased contributions that would fund a retirement benefit with a 3.5 percent multiplier. The benefit would be capped at 75 percent of AFC. Judges in PERS Plan 3 could elect a 1.6 percent of pay per year of service benefit, capped at 37.5 percent of AFC.

Newly elected or appointed justices and judges who chose to become PERS members on or after January 1, 2007, or who had not previously opted into PERS membership, were required to participate in the JBM Program.

There are 1,176 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of June 30, 2013:

Retirees and Beneficiaries Receiving Benefits	85,328
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	31,047
Active Plan Members Vested	150,706
Terminated Plan Members Nonvested	101,191
Total	368,272

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 percent for state agencies and local government unit employees, and at 7.5 percent 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

CITY OF PORT ORCHARD

Notes to Financial Statements

December 31, 2014

the defined contribution portion. The Plan 3 employee contribution rates range from 5 percent to 15 percent.

As a result of the implementation of the Judicial Benefit Multiplier Program in January 2007, a second tier of employer and employee rates was developed to fund, along with investment earnings, the increased retirement benefits of those justices and judges that participate in the program

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, 2014, are as follows:

Members Not Participating in JBM:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
Employer*	9.21%**	9.21%**	9.21%***
Employee	6.00%****	4.92%****	*****

* The employer rates include the employer administrative expense fee currently set at 0.18%.

** The employer rate for state elected officials is 13.73% for Plan 1 and 9.21% 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 4.92% for Plan 2.

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

Members Participating in JBM:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
Employer-State Agency*	11.71%	11.71%	11.71%**
Employer-Local Gov't Units*	9.21%	9.21%	9.21%**
Employee-State Agency	9.76%	9.80%	7.50%***
Employee-Local Gov't Units	12.26%	12.30%	7.50%***

CITY OF PORT ORCHARD

Notes to Financial Statements

December 31, 2014

* The employer rates include the employer administrative expense fee currently set at 0.18%.

** Plan 3 defined benefit portion only.

***Minimum rate.

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

	PERS Plan 1	PERS Plan 2	PERS Plan 3
2014	\$ 20,973	\$ 260,336	\$ 13,680
2013	\$ 17,812	\$ 227,460	\$ 10,128
2012	\$ 15,880	\$ 195,812	\$ 8,712

Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plans 1 and 2

Plan Description

LEOFF was established in 1970 by the Legislature. Membership includes all full-time, fully compensated, local law enforcement commissioned officers, firefighters and, as of July 24, 2005, emergency medical technicians. LEOFF membership is comprised primarily of non-state employees, with Department of Fish and Wildlife enforcement officers, who were first included effective July 27, 2003, being an exception. LEOFF retirement benefit provisions are established in chapter 41.26 RCW and may be amended only by the State Legislature.

LEOFF is a cost-sharing multiple-employer retirement system comprised of two separate defined benefit plans. LEOFF members who joined the system by September 30, 1977 are Plan 1 members. Those who joined on or after October 1, 1977 are Plan 2 members.

Effective July 1, 2003, the LEOFF Plan 2 Retirement Board was established by Initiative 790 to provide governance of LEOFF Plan 2. The Board's duties include adopting contribution rates and recommending policy changes to the Legislature.

LEOFF retirement benefits are financed from a combination of investment earnings, employer and employee contributions, and a special funding situation in which the state pays through legislative appropriations. Employee contributions to the LEOFF Plan 1 and Plan 2 defined benefit plans accrue interest at a rate specified by the Director of DRS. During DRS' Fiscal Year 2013, the rate was five and one-half percent compounded quarterly. Members in LEOFF Plan 1 and Plan 2 can elect to withdraw total employee contributions and interest earnings, in lieu of any retirement benefit, upon separation from LEOFF-covered employment.

LEOFF Plan 1 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement with five years of service at the age of 50.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

The benefit per year of service calculated as a percent of final average salary (FAS) is as follows:

Term of Service	Percent of Final Average Salary
20 or more years	2.0%
10 but less than 20 years	1.5%
5 but less than 10 years	1.0%

The FAS is the basic monthly salary received at the time of retirement, provided a member has held the same position or rank for 12 months preceding the date of retirement. Otherwise, it is the average of the highest consecutive 24 months' salary within the last 10 years of service. A cost-of-living allowance is granted (based on the Consumer Price Index).

LEOFF Plan 1 provides death and disability benefits. Death benefits for survivors of Plan 1 members on active duty consist of the following: (1) If there is an eligible spouse, 50 percent of the FAS, plus 5 percent of the FAS for each eligible surviving child, with a limitation on the combined benefit of 60 percent of the FAS; or (2) If there is no eligible spouse, eligible children receive 30 percent of the FAS for the first child plus 10 percent for each additional child, subject to a 60 percent limitation of the FAS, divided equally.

A one-time duty-related death benefit is provided to the beneficiary or the estate of a LEOFF Plan 1 member who dies as a result of injuries or illness 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.

The LEOFF Plan 1 disability benefit is 50 percent of the FAS plus 5 percent for each child up to a maximum of 60 percent. Upon recovery from disability before the age of 50, a member is restored to service with full credit for service while disabled. Upon recovery after the age of 50, the benefit continues as the greater of the member's disability benefit or service retirement benefit.

LEOFF Plan 2 members are vested after the completion of five years of eligible service.

Plan 2 members are eligible for retirement at the age of 53 with five years of service, or at age 50 with 20 years of service. Plan 2 members receive a benefit of 2 percent of the FAS per year of service (the FAS is based on the highest consecutive 60 months), actuarially reduced to reflect the choice of a survivor option. Members who retire prior to the age of 53 receive reduced benefits. If the member has at least 20 years of service and is age 50, the reduction is 3 percent for each year prior to age 53. Otherwise, the benefits are actuarially reduced for each year prior to age 53. A cost-of-living allowance is granted (based on the Consumer Price Index), capped at 3 percent annually.

LEOFF Plan 2 provides disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 benefit amount is 2 percent of the FAS for each year of service. Benefits are reduced to reflect the choice of survivor option and for each year that the

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

member's age is less than 53, unless the disability is duty-related. If the member has at least 20 years of service and is age 50, the reduction is 3 percent for each year prior to age 53.

A disability benefit equal to 70 percent of their FAS, subject to offsets for workers' compensation and Social Security disability benefits received, is also available to those LEOFF Plan 2 members who are catastrophically disabled in the line of duty and incapable of future substantial gainful employment in any capacity. Effective June 2010, benefits to LEOFF Plan 2 members who are catastrophically disabled include payment of eligible health care insurance premiums.

Members of LEOFF Plan 2 who leave service because of a line of duty disability are allowed to withdraw 150 percent of accumulated member contributions. This withdrawal benefit is not subject to federal income tax. Alternatively, members of LEOFF Plan 2 who leave service because of a line of duty disability may be eligible to receive a retirement benefit of at least 10 percent of FAS and 2 percent per year of service beyond five years. The first 10 percent of the FAS is not subject to federal income tax.

LEOFF Plan 2 retirees may return to work in an eligible position covered by another retirement system, choose membership in that system and suspend their pension benefits, or not choose membership and continue receiving pension benefits without interruption.

A one-time duty-related death benefit is provided to the beneficiary or the estate of a LEOFF Plan 2 member who dies as a result of injuries or illness 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.

Benefits to eligible surviving spouses and dependent children of LEOFF Plan 2 members killed in the course of employment include the payment of eligible health care insurance premiums.

Legislation passed in 2009 provides to the Washington state registered domestic partners of LEOFF Plan 2 members the same treatment as married spouses, to the extent that the treatment is not in conflict with federal laws.

LEOFF members meeting specific eligibility requirements have options available to enhance their retirement benefits. Some of these options are available to their survivors.

There are 374 participating employers in LEOFF. Membership in LEOFF consisted of the following as of the latest actuarial valuation date for the plans of June 30, 2013:

Retirees and Beneficiaries Receiving Benefits	10,511
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	699
Active Plan Members Vested	16,830
Terminated Plan Members Nonvested	1,600
Total	29,640

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

Funding Policy

Employer and employee contribution rates are developed by the Office of the State Actuary to fully fund the plans. Starting on July 1, 2000, Plan 1 employers and employees contribute zero percent, as long as the plan remains fully funded. Plan 2 employers and employees are required to pay at the level adopted by the LEOFF Plan 2 Retirement Board.

The Legislature, by means of a special funding arrangement, appropriates money from the state General Fund to supplement the current service liability and fund the prior service costs of Plan 2 in accordance with the recommendations of the Pension Funding Council and the LEOFF Plan 2 Retirement Board. This special funding situation is not mandated by the state constitution and could be changed by statute. For DRS' Fiscal Year 2014, the state contributed \$55.6 million to LEOFF Plan 2.

The methods used to determine the contribution requirements are established under state statute in accordance with Chapters 41.26 and 41.45 RCW.

The required contribution rates expressed as a percentage of current-year covered payroll, as of December 31, 2014, are as follows:

	LEOFF Plan 1	LEOFF Plan 2
Employer*	0.18%	5.23%**
Employee	0.00%	8.41%
State	N/A	3.36%

*The employer rates include the employer administrative expense fee currently set at 0.18%.

** The employer rate for ports and universities is 8.59%.

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

	LEOFF Plan 1	LEOFF Plan 2
2014	\$ 0	\$ 96,571
2013	\$ 0	\$ 89,408
2012	\$ 0	\$ 93,237

NOTE 8. RISK MANAGEMENT

The City of Port Orchard is a member of the Association of Washington Cities Risk Management Service Agency (AWC RMSA). Chapter 48.62 RCW authorizes the governing body of any one or more governmental entities to form together into or join a pool or organization for the joint purchasing of insurance, and/or joint self-insuring, and/or joint hiring

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

or contracting for risk management services to the same extent that they may individually purchase insurance, self-insure, or hire or contract for risk management services. An agreement to form a pooling arrangement was made pursuant to the provisions of Chapter 39.34 RCW, the Interlocal Cooperation Act. The AWC RMSA was formed on January 1, 1989 when 32 municipalities in the State of Washington joined together by signing an Interlocal Governmental Agreement to pool their self-insured losses and jointly purchase insurance and administrative services. As of December 31, 2014, 94 municipalities/entities participate in the AWC RMSA pool.

The AWC RMSA allows members to establish a program of joint insurance and provides risk management services to all members. All coverages are on an occurrence basis. The AWC RMSA provides all risk property, comprehensive crime, general liability, automobile liability, police liability, public officials' liability, employee fidelity and faithful performance, and equipment breakdown insurance coverage. Equipment breakdown is included with the property insurance carrier and fidelity (crime) coverage is a stand-alone policy which the AWC RMSA procures for its members. The AWC RMSA also allows members with airports to group purchase airport liability coverage.

Members pay an annual assessment to the AWC RMSA. The AWC RMSA is responsible for payment of all covered causes of loss against the jurisdiction above the stated retention. All members in the AWC RMSA have \$10 million in both per occurrence and aggregate liability limits. For the first \$1 million, AWC RMSA is self-insured for its Self-Insured Retention (SIR) of \$250,000, per occurrence, and is reinsured by Berkley Public Entity for the additional \$750,000. For the \$9 million in excess coverage limits, an excess liability policy is purchased from Starr Indemnity & Liability Company. The excess property coverage is purchased through Lexington Insurance Company using the Pool's broker, Arthur J. Gallagher Risk Management Services. In 2014, AWC RMSA carried a retention of \$50,000 and limits up to \$250 million. Since AWC RMSA is a cooperative program, there is joint liability among the participating members.

Members contract to remain in the AWC RMSA pool for a minimum of one year and must give a one-year notice before terminating participation. Even after termination, a member is still responsible for contributions to the Pool for any unresolved, unreported, and in-process claims for the period they were signatory to the Interlocal Governmental Agreement.

The AWC RMSA establishes a loss fund for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses.

In accordance with WAC 200.100.02023, the AWC RMSA is governed by a board of directors which is comprised of elected officials of participating members.

There have been no settlements in the past three years that exceeded the City's insurance coverage.

NOTE 9. SHORT-TERM DEBT

The City had no short term debt.

NOTE 10. LONG-TERM DEBT

A. LONG-TERM DEBT

The City issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities. The City has \$1,015,000 in general obligation bonds outstanding on December 31, 2014 for the construction of city hall.

General obligation bonds are direct obligations and pledge the full faith and credit of the government. These bonds generally are issued as 20-year serial bonds with equal amounts of principal maturing each year. General obligation bonds are either created by 3/5 majority vote of the people and, therefore, financed by a special tax levy; or created by ordinance, adopted by the City Council, and normally financed from general revenues (councilmanic bonds). General obligation bonds currently outstanding are as follows:

Name of Issuance	Purpose	Maturity Date	Interest Rate	Original Amount	Debt Outstanding
	Bus. Type & Gov't'l.				
2003 LTGO Bond	Activities	12/1/2019	2%-3.8%	\$ 3,000,000	\$ 1,015,000
Total General Obligation Bonds					\$ 1,015,000

The City provides for cash to fund current debt service requirements as a part of the budgeting process. Annual debt service requirements to maturity for general obligation bonds are as follows:

	Governmental Activities			Business-Type Activities		
	Principal	Interest	Total Requirements	Principal	Interest	Total Requirements
2015	138,700	26,721	165,421	51,300	9,884	61,184
2016	142,350	22,006	164,356	52,650	8,139	60,789
2017	149,650	17,024	166,674	55,350	6,296	61,646
2018	153,300	11,636	164,936	56,700	4,304	61,004
2019	156,950	5,964	162,914	58,050	2,206	60,256
	\$ 740,950	\$ 83,351	\$ 824,301	\$ 274,050	\$ 30,829	\$ 304,879

All bond issues comply with arbitrage regulations. The city is not subject to federal arbitrage requirements at this time.

B. DUE TO OTHER GOVERNMENTS

On April 8, 2014 the City approved Contract No. 043-14 authorizing the Mayor to Execute a Loan Contract with the Department of Commerce in the amount of \$6,060,000 for the Well No.10 project. The

CITY OF PORT ORCHARD

Notes to Financial Statements

December 31, 2014

loan is funded from the Drinking Water State Revolving Fund (DWSRF) which is a federal infrastructure loan program designed to assist Municipal and other drinking water systems with low-interest construction loan funding. The City's interest rate is 1.5% and the loan term is 24 years. Total debt outstanding as of December 31, 2014 is as follows:

Name	Original Amount	Purpose	Issuance Date	Maturity Date	Interest Rate	Debt Outstanding
Business-Type Activities						
Drinking Water State Revolving Fund	\$ -	Capital	4/8/2014	10/1/2038	1.50%	\$ 60,000
Business.-Type Total						60,000
Total Due to Other Governments						\$ 60,000

Business-Type Activities			
	Total		
	Principal	Interest	Requirements
2015	-	-	-
2016	-	-	-
2017	-	-	-
2018	-	-	-
2019	3,000	31	3,031
2020-2024	15,000	155	15,155
2025-2029	15,000	155	15,155
2030-2034	15,000	155	15,155
2035-2038	12,000	124	12,124
	\$ 60,000	\$ 620	\$ 60,620

C. GOVERNMENT NOTE

Government note in business activity outstanding at year-end is as follows:

Name	Original Amount	Purpose	Issuance Date	Maturity Date	Interest Rate	Debt Outstanding
Business-Type Activities						
McCormick Note	\$ 441,250	Capital	11/23/1998	N/A	0.00%	\$ 169,650
Business-Type Total						169,650
Total Note						\$ 169,650

The promissory note that was entered into for the purchase of the McCormick Water Company is being repaid with new McCormick water connection fees as the revenue source. There is \$700

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

paid on each of the first 550 connections and \$225 paid on the 551st through the 800th connection. Payments are made no less frequent than quarterly. This type of note does not have a repayment schedule.

C. REFUNDED DEBT

In prior years, the City has defeased various bond issues by creating separate irrevocable trust funds. New debt has been issued and the proceeds have been used to purchase US Government securities that were placed in the trust funds. The investments and fixed earnings from the investments are sufficient to fully service the defeased debt until the debt is called or matures. For financial reporting purposes, the debt has been removed as a liability from the governmental activities column of the statement of net position. At December 31, 2014, \$19,000 of bonds outstanding are considered defeased.

NOTE 11. LEASES

Operating Leases

The City is obligated under certain leases accounted for as operating leases. These represent lease of copiers, a postage machine, lease for a police substation and an aquatic lands lease. The lease for the police substation expires May, 2016. The City signed an aquatic lands lease June 4, 2012, with Washington State Department of Natural Resources. The first four year period the lease payment amount is \$21,280.43 (with an inflation adjustment annually.) In 2014, \$22,404.22 was paid to DNR for this lease. At the end of each four year period, the state will re-value the annual rent.

The following is a schedule by years of future minimum rental payments required under operating leases that have initial or remaining non-cancelable lease terms in excess of one year as of December 31, 2014:

Year Ending December 31	Total
2015	37,616.04
2016	28,806.34
2017	5,652.12
Total minimum payments required	<u>\$ 72,074.50</u>

Total rent expense for the year ended December 31, 2014 was \$46,618.89.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

NOTE 12. CHANGES IN LONG-TERM LIABILITIES

The following is a summary of long-term debt changes of the City for the year ended December 31, 2014:

	Beginning			Ending	Due Within
	Balance	Additions	Reductions	Balance	One Year
Governmental Activities					
Bonds payable:					
General obligation bonds	\$ 876,000	\$ -	\$ 135,050	\$ 740,950	\$ 138,700
Premiums	2,875	-	522	2,353	522
Discounts	-	-	-	-	-
Total bonds payable	878,875	-	135,572	743,303	139,222
Capital leases	-	-	-	-	-
Claims	-	-	-	-	-
Pension/OPEB obligations	368,191	148,976	62,565	454,602	-
Compensated absences	380,241	208,386		588,627	438,723
Governmental activity long-term liabilities	\$ 1,627,307	\$ 357,362	\$ 198,137	\$ 1,786,532	\$ 577,945
Business-type activities					
Bonds payable:					
General obligation bonds	\$ 324,000	\$ -	\$ 49,950	\$ 274,050	\$ 51,300
Revenue bonds	-	-	-	-	-
Premiums	1,056	-	192	864	192
Discounts	-	-	-	-	-
Total bonds payable	325,056	-	50,142	274,914	51,492
Drinking Water State Revolving Fund Loan	-	60,000	-	60,000	-
Private note	170,350	-	700	169,650	-
Compensated absences	82,952	-	5,266	77,686	57,902
Business-type activities long-term liabilities	\$ 578,358	\$ 60,000	\$ 56,108	\$ 582,250	\$ 109,394

NOTE 13. CONTINGENCIES AND LITIGATION

The City of Port Orchard has situations which are not yet resolved, but based on available information, in the opinion of management, the City of Port Orchard's insurance policies and/or reserves are adequate to pay all known or pending claims.

The City 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 request for reimbursement to grantor agencies for expenditures disallowed under the terms of the grants. (Other than the instances described above,) City management believes that such disallowances, if any, will be immaterial.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

NOTE 14. RESTRICTED COMPONENT OF NET POSITION

The government-wide statement of net position reports \$3,442,902 of restricted component of net position, all of which is restricted by enabling legislation.

NOTE 15. INTERFUND BALANCES AND TRANSFERS

A. INTERFUND BALANCES

There were no interfund loans in 2014.

B. INTERFUND TRANSFERS

Interfund transfers are the flow of assets without a reciprocal return of assets, goods or services. These are transfers to support other funds without a requirement for repayment. Non-routine transfers included General Fund receiving \$55,483 for new City Hall phones and \$195,974 for street paving and improvements from the Cumulative Reserve for Municipal Facilities Fund. Cumulative Reserve for Municipal Facilities Fund received \$70,918 from the General Fund for Parks and \$372,430 from Impact Mitigation Fee Fund for the McCormick Woods Park. The interfund transfer activity for 2014 is as follows:

	Transfer From					
	General Fund	Cumulative Reserve for Municipal Facilities	Water Sewer	Storm Drainage	Nonmajor Gov't Funds	Total
General Fund	\$ -	\$ 251,457	\$ 4,742	\$ 1,062	\$ -	\$ 257,261
Cumulative Reserve for Municipal Facilities	70,918	-	-	-	372,430	443,348
Nonmajor Governmental Funds	134,956	166,162	-	-	-	301,118
Total	\$ 205,874	\$ 417,619	\$ 4,742	\$ 1,062	\$ 372,430	\$ 1,001,727

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

NOTE 16. RECEIVABLES AND PAYABLES BALANCES

A. RECEIVABLES

Receivables at December 31, 2014 were as follows:

	Due from			
	Other Gvts	Taxes	Other	Total
Governmental Activities:				
General Fund taxes	\$ -	\$ 121,791	\$ -	\$ 121,791
General Fund miscellaneous receivables	-	-	73,023	73,023
General Fund municipal court receivables	-	-	464,785	464,785
General Fund due from other governments	9,079	-	-	9,079
Special Investigative Unit court receivables	-	-	58,548	58,548
Impact Mitigation Fee Fund bayside receivable	-	-	37,065	37,065
Cumulative Reserve for Municipal Facilities due from other governments	8,090	-	-	8,090
Street Capital Projects miscellaneous receivables	-	-	1,520	1,520
Street Capital Projects due from other gov/misc rec	3,913	-	-	3,913
Total Governmental Activities	\$ 21,082	\$ 121,791	\$ 634,941	\$ 777,814
Business Type Activities:				
Water-Sewer accounts receivables	\$ -	\$ -	\$ 691,465	691,465
Water-Sewer soil clean-up receivable	-	-	117,401	117,401
Storm Drainage accounts receivable	-	-	125,441	125,441
Storm Drainage due from other governments	20,838	-	-	20,838
Total Business Type Activities	\$ 20,838	\$ -	\$ 934,307	\$ 955,145

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

B. PAYABLES

Payables at December 31, 2014 were as follows:

	Vendors	Salaries & Benefits	Interest Payable	Total
Governmental Activities:				
General Fund Payables	\$ 278,510	\$ 166,074		\$ 444,584
Cumulative Reserve for Municipal Facilities Fund	32,807			32,807
Street Capital Projects Fund Payables	3,049			3,049
Non-Major Fund Payables	15,155	2,982		18,137
Reconciliation of balances in fund financial statements to government-wide statements			2,227	2,227
Total Governmental Activities	\$ 329,521	\$ 169,056	\$ 2,227	\$ 500,804
Business Type Activities:				
Water Sewer Fund Payables	\$ 740,931	\$ 32,023	\$ 1,444	\$ 774,398
Storm Drainage Fund Payables	57,318	11,969		\$ 69,287
Total Business Type Activities	\$ 798,249	\$ 43,992	\$ 1,444	\$ 843,685

NOTE 17. JOINT VENTURES

In 1983, the City of Port Orchard and West Sound Utility District (previously the Karcher Creek Sewer District) amended an intergovernmental agreement relating to the construction and management of the secondary wastewater treatment facility. In April of 2014 the City and District signed an interlocal agreement for the management and operation of the joint wastewater treatment facility for an additional term of 25 years. This joint venture establishes a Sewer Advisory Committee (SAC) consisting of three representatives from each entity who prepare and monitor the Facility's budget. The District and the City share 50% ownership in the facility's total assets. In accordance with the generally accepted accounting principles, the proportional shares of the joint venture's results of operations are presented as a single operating account on the City's proprietary fund's operating statement – Investment in Joint Venture. In 2014, the change in the City's equity in the joint venture was an increase of \$216,014. The City of Port Orchard's equity interest in the secondary Wastewater Treatment Facility as of December 31, 2014 was \$8,419,307.

The Utility District is responsible for the daily operation of the facility. The participants pay their share of the expenses based on their portion of flow into the facility. The City and the District pay the joint venture an amount determined during the budget process to cover maintenance, operation, capital improvements and debt monthly. The current cost sharing is 48% City and 52% District.

The City was the lead agency on the wastewater treatment plant expansion project, and is the signatory on two Public Works Trust Fund Loans for the Facility's expansion. Revenues of the facility are used to make debt service payments on the two loans. Annually, the facility makes a

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

payment to the City to cover the debt service on these loans. The SAC recommended and the City Council and the District Commissioners approved using a portion of Wastewater Treatment Facility Fees collected by each jurisdiction to help make the annual debt payments. This cost sharing formula is 50% and in 2014 each entity paid \$150,000.

Name of Issuance	Purpose	Total Amount of Loan	First Draw Date	Maturity Date	Interest Rate	Debt Outstanding
Public Works Trust Fund						
Loan 1	Capital	\$ 10,000,000	2/29/2004	7/1/2022	0.50%	\$ 4,420,760
Loan 2	Capital	6,800,000	6/30/2005	7/1/2024	0.50%	3,600,000
Joint Venture Total						<u>\$ 8,020,760</u>
Total Loans						<u>\$ 8,020,760</u>

West Sound Utility District maintains separate accounting records and prepares separate financial statements for the operations of the Joint Wastewater Treatment Facility. Complete financial statements for the Facility can be obtained from West Sound Utility District at 2924 SE Lund Ave, Port Orchard, WA 98366.

NOTE 18. OTHER POST EMPLOYMENT BENEFITS (OPEB) PLANS

A. PLAN DESCRIPTION – DEFINED BENEFIT – SINGLE EMPLOYER PLAN (LEOFF 1 OPEB)

As required by the Revised Code of Washington (RCW) Chapter 41.26, the City provides lifetime medical care for members of the Law Enforcement Officers and Firefighters (LEOFF) retirement system hired before October 1, 1977. The members necessary hospital, medical and nursing care expenses, not payable by worker's compensation, social security, insurance provided by another employer, other pension plan or any other similar source are covered. Most medical coverage for eligible retirees is provided by one of the City's employee medical insurance programs. As of December 31, 2014 the City has five members in this group.

This OPEB plan does not issue a stand-alone financial report nor is it included in the report of another entity.

Funding Policy

Funding for LEOFF retiree healthcare costs is provided entirely by the City as required by RCW. The plan is not currently funded. The City finances it on a pay-as-you-go-basis.

Actuarial Methods and Assumptions

The City used the alternative measurement method permitted under GASB Statement No. 45. A single retirement age of 56.24 was assumed for all active members for the purpose of determining the actuarial accrued liability (AAL) and normal cost. Retirement, disablement, termination and mortality rates were assumed to follow the LEOFF 1 rates used in the June 30, 2011 actuarial valuation report issued by the Office of the State Actuary (OSA). Healthcare costs and trends were determined by Milliman and used by OSA in the state-wide LEOFF1 medical study performed in 2013. The results were based on grouped data with four active groupings and four inactive groupings. The actuarial cost method used to determine the AAL

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

was Projected Unit Credit. The AAL and NOO are amortized on an open basis as a level dollar over 15 years. These assumptions are individually and collectively reasonable for the purposes of this valuation.

Annual OPEB Cost and Net OPEB Obligation

The City was required to contribute \$167,364, but only contributed \$62,565 at December 31, 2014. This \$62,565 contributed differs from the Annual Required Contribution (ARC) because the plan is financed on a pay-as-you-go basis. The difference between the OPEB Costs and the required contribution is called the Net OPEB Obligation (NOO). This amount of \$454,601 is the actuarial accrued liability recognized on the government wide statement of net position.

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation is as follows:

Fiscal Year Ended	Annual OPEB Costs	Percentage of Annual OPEB Costs Contributed	Net OPEB Obligation
2014	\$ 148,976	42%	\$ 454,602
2013	\$ 147,498	45%	\$ 368,191
2012	\$ 119,976	63%	\$ 286,963

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability Projected Unit Credit	Unfunded Actuarial Accrued Liabilities (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/2014	0	1,860,814	1,860,814	0%	0	N/A
12/31/2013	0	1,799,275	1,799,275	0%	0	N/A
12/31/2012	0	1,413,544	1,413,544	0%	0	N/A

The Annual Required Contribution (ARC) represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities over a period of twenty five years using closed group contribution rates, and annual budget growth of 10.80%, with a +or- 5.0% medical inflation sensitivity performed as of December 31, 2014. The following table shows the components of the City's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the net OPEB Obligation. The net OPEB obligation of \$454,602 is included as a non-current liability in the statement of net position.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

	<u>2014</u>
Determination of Annual Required Contribution	
Normal Cost at beginning of year	\$ -
Amortization of UAAL*	167,364
Annual Required Contribution (ARC) at year-end	<u>\$ 167,364</u>
 Determination of Net OPEB Obligation	
Actuarial Required Contribution (ARC 12/31/14)	\$ 167,364
Interest on Net OPEB Obligation (NOO)	14,728
Adjustment to NOO	(33,115)
Annual OPEB Cost	<u>\$ 148,977</u>
 Employer Contributions	\$ (62,565)
Increase (Decrease) in NOO	86,411
Net OPEB Obligation January 1, 2014	368,191
Net OPEB Obligation December 31, 2014	<u><u>\$ 454,602</u></u>

The City's percentage of annual OPEB cost contributed to the plan for 2014 is 42%.

The required schedule of funding progress is immediately following the notes to the financial statements.

B. OTHER RETIREES - AWC (OTHER THAN LEOFF1)

The City is a Participating Employer in the Association of Washington Cities Employee Benefit Trust ("Trust"), a cost-sharing multiple-employer welfare benefit plan administered by the Association of Washington Cities. The Trust provides medical benefits to certain eligible retired employees of Participating Employers and their eligible family members. Under Article VII of the Trust document, the Trustees have the authority and power to amend the amount and nature of the medical and other benefit provided by the Trust. The Trust issues a publicly available financial report that includes financial statements and required supplementary information for the Trust. That report, along with a copy of the document, may be obtained by writing to the Trust at 1076 Franklin Street SE, Olympia WA 98501-1346 or by calling 1-800-562-8981.

Funding Policy

The Trust provides that contribution requirements of participating employers and of participating employees, retirees and other beneficiaries, if any, are established and may be amended by the Board of Trustees of the Trust. Retirees of the City receiving medical benefits from the Trust contribute the following monthly amounts:

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

Retirees receiving medical benefits from the trust Monthly Contributions:	2014	
	Healthfirst	Healthfirst
	R- 1000	R- 2500
Non-Medicare enrolled retiree coverage	\$ 830.01	\$ 724.72
Non-Medicare enrolled spouse coverage	837.26	729.99
Medicare enrolled retiree coverage *	443.30	388.08
Medicare enrolled spouse coverage *	456.13	398.04

*Plans no longer available in 2015

Participating employers are not contractually required to contribute an assessed rate each year by the Trust for the non-LEOFF1 retirees. The retiree pays for 100% of the premium.

NOTE 19. HEALTH & WELFARE

The City of Port Orchard is a member of the Association of Washington Cities Employee Benefit Trust Health Care Program (AWC Trust HCP). Chapter 48.62 RCW provides that two or more local government entities may, by Interlocal agreement under Chapter 39.34 RCW, form together or join a pool or organization for the joint purchasing of insurance, and/or joint self-insurance, to the same extent that they may individually purchase insurance, or self-insure.

An agreement to form a pooling arrangement was made pursuant to the provisions of Chapter 39.34 RCW, the Interlocal Cooperation Act. The AWC Trust HCP was formed on January 1, 2014 when participating cities, towns, and non-city entities of the AWC Employee Benefit Trust in the State of Washington joined together by signing an Interlocal Governmental Agreement to jointly self-insure certain health benefit plans and programs for participating employees, their covered dependents and other beneficiaries through a designated account within the Trust.

As of December 31, 2014, 263 cities/towns/non-city entities participate in the AWC Trust HCP.

The AWC Trust HCP allows members to establish a program of joint insurance and provides health and welfare services to all participating members. The AWC Trust HCP pools claims without regard to individual member experience. The pool is actuarially rated each year with the assumption of projected claims run-out for all current members. The AWC Trust HCP includes medical insurance through Regence BlueShield and Asuris Northwest Health, dental insurance through Delta Dental of Washington, and vision insurance through Vision Service Plan. Eligible members are cities and towns within the state of Washington. Non-City Entities (public agency, public corporation, intergovernmental agency, or political subdivision within the state of Washington) are eligible to apply for coverage into the AWC Trust HCP, submitting application to the Board of Trustees for review as required in the Trust Agreement.

Participating employers pay monthly premiums to the AWC Trust HCP. The AWC Trust HCP is responsible for payment of all covered claims. The AWC Trust HCP purchases stop loss insurance for Regence/Asuris plans at an Individual Stop Loss (ISL) of \$1.5 million through Life Map, and Group Health ISL at \$750,000 through Sun Life. The aggregate policy is for 200% of expected medical claims.

CITY OF PORT ORCHARD
Notes to Financial Statements
December 31, 2014

Participating employers contract to remain in the AWC HCP for a minimum of three years. Participating employers with over 250 employees must provide written notice of termination of all coverage a minimum of 12 months in advance of the termination date, and participating employers with under 250 employees must provide written notice of termination of all coverage a minimum of 6 months in advance of termination date. When all coverage is being terminated, termination will only occur on December 31. Participating employers terminating a group or line of coverage must notify the HCP a minimum of 60 days prior to termination. A participating employer's termination will not obligate that member to past debts, or further contributions to the HCP. Similarly, the terminating member forfeits all rights and interest to the HCP Account.

The operations of the Health Care Program are managed by the Board of Trustees or its delegates. The Board of Trustees is comprised of four regionally elected officials from Trust member cities or towns, the Employee Benefit Advisory Committee Chair and Vice Chair, and the AWC Board of Directors President and Vice President. The Trustees or its appointed delegates review and analyze Health Care Program related matters and make operational decisions regarding premium contributions, reserves, plan options and benefits in compliance with Chapter 48.62 RCW. The Board of Trustees has decision authority consistent with the Trust Agreement, Health Care Program policies, Chapter 48.62 RCW and Chapter 200-110-WAC.

The accounting records of the Trust HCP are maintained in accordance with methods prescribed by the State Auditor's office under the authority of Chapter 43.09 RCW. The Trust HCP also follows applicable accounting standards established by the Governmental Accounting Standards Board ("GASB"). Year-end financial reporting is done on an accrual basis and submitted to the Office of the State Auditor as required by Chapter 200-110 WAC. The audit report for the AWC Trust HCP is available from the Washington State Auditor's office.

NOTE 20. TERMINATION BENEFITS

The funding policy for any termination benefits is based upon pay-as-you-go. These termination benefits are handled on a case by case basis.

NOTE 21. PRIOR PERIOD ADJUSTMENTS

A prior period adjustment of \$64,115 was made in the Cumulative Reserve for Municipal Facilities Fund for Real Estate Excise Tax revenue received in prior years from the Kitsap County Treasurer that was improperly allocated to the City.

A prior period adjustment of \$487,150 was made in the Water Sewer Fund to recognize a development agreement that the City entered into in 2013 with The Sinclair, LLC. The agreement allows for the developer to receive a credit and/or reimbursement against the sewer capital facilities charge. The amount of the credit shall not exceed the cost of the construction of the sewer force main and the Pottery Sewer Pump Station deeded to the City.

A prior period adjustment of \$195,300 was made in the Storm Drainage Fund for additional infrastructure transferred from Kitsap County for the Bethel Annexation that occurred in 2012.

NOTE 22. SUBSEQUENT EVENT

Subsequent to December 31, 2014 an incident with a sinkhole and water main that had previously been repaired in 2007 redeveloped on August 23, 2015. The city's insurer AWC-RMSA is conducting a review of the previous incident in light of the current occurrence. On November 17, 2015 AWC-RMSA provided a New Claim Notification to the City to reflect an open claim in the amount of \$121,014.37 it is currently under investigation and review.

On November 10, 2015, the City approved Resolution No. 019-15 authorizing the City to enter into a grant and loan agreement with the Department of Ecology for the Regional Decant Facility Retrofit project. The City was awarded a 75% grant for \$761,250 and 25% loan match for \$253,750 for a total construction price of \$1,015,000. The loan rate is 2.4% and is included in the 2016 budget.

Required Supplementary Information
LEOFF 1 Retiree Medical Benefits
Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability Projected Unit Credit	Unfunded Actuarial Accrued Liabilities (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/2012	0	\$1,413,544	\$1,413,544	0%	0	N/A
12/31/2013	0	\$1,799,275	\$1,799,275	0%	0	N/A
12/31/2014	0	\$1,860,814	\$1,860,814	0%	0	N/A

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.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

In fulfilling our mission to hold state and local governments accountable for the use of public resources, we also hold ourselves accountable by continually improving our audit quality and operational efficiency and developing highly engaged and committed employees.

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.

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 as well as [fraud](#), state [whistleblower](#) and [citizen hotline](#) investigations.

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We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

Contact information for the State Auditor's Office	
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