



Office of the Washington State Auditor
Pat McCarthy

Financial Statements Audit Report

City of Poulsbo

Kitsap County

For the period January 1, 2016 through December 31, 2016

Published June 29, 2017

Report No. 1019401





Office of the Washington State Auditor
Pat McCarthy

June 29, 2017

Mayor and City Council
City of Poulsbo
Poulsbo, Washington

Report on Financial Statements

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

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

Sincerely,

Pat McCarthy
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	6
Financial Section.....	9
About The State Auditor's Office.....	80

**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 Poulsbo
Kitsap County
January 1, 2016 through December 31, 2016**

Mayor and City Council
City of Poulsbo
Poulsbo, 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 Poulsbo, Kitsap County, Washington, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated June 23, 2017.

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.



Pat McCarthy

State Auditor

Olympia, WA

June 23, 2017

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

City of Poulsbo Kitsap County January 1, 2016 through December 31, 2016

Mayor and City Council
City of Poulsbo
Poulsbo, 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 Poulsbo, Kitsap County, Washington, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed on page 9.

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 Poulsbo, as of December 31, 2016, 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 10 through 27, information on postemployment benefits other than pensions on page 70 and pension plan information on pages 71 through 79 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated June 23, 2017 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.

A handwritten signature in black ink that reads "Pat McCarthy". The signature is written in a cursive, flowing style.

Pat McCarthy
State Auditor
Olympia, WA

June 23, 2017

FINANCIAL SECTION

**City of Poulsbo
Kitsap County
January 1, 2016 through December 31, 2016**

REQUIRED SUPPLEMENTARY INFORMATION

Management's Discussion and Analysis – 2016

BASIC FINANCIAL STATEMENTS

Statement of Net Position – 2016

Statement of Activities – 2016

Balance Sheet – Governmental Funds – 2016

Reconciliation of Total Governmental Funds Balances to Net Position of Governmental
Activities – 2016

Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental
Funds – 2016

Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund
Balances – Governmental Funds to the Statement of Activities – 2016

Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual
General Fund – 2016

Statement of Net Position – Proprietary Funds – 2016

Statement of Revenues, Expenses, and Changes in Net Position – Proprietary Funds –
2016

Statement of Cash Flows – Proprietary Funds – 2016

Statement of Fiduciary Net Position – 2016

Notes to the Financial Statements – 2016

REQUIRED SUPPLEMENTARY INFORMATION

LEOFF 1 Retiree Medical Benefits Schedule of Funding Progress – 2016

Schedule of Proportionate Share of the Net Pension Liability PERS 1 – 2016

Schedule of Proportionate Share of the Net Pension Liability PERS 2/3 – 2016

Schedule of Proportionate Share of the Net Pension Liability LEOFF 1 – 2016

Schedule of Proportionate Share of the Net Pension Liability LEOFF 2 – 2016

Schedule of Employer Contributions PERS 1 – 2016

Schedule of Employer Contributions PERS 2/3 – 2016

Schedule of Employer Contributions LEOFF 1 – 2016

Schedule of Employer Contributions LEOFF 2 – 2016

Notes to Required Supplementary Information – Pensions – 2016

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis (MD&A) of the City of Poulsbo's financial performance provides an overall review of the City's financial activities for the year ended December 31, 2016. The intent of this discussion and analysis is to look at the City's financial performance.

This Management's Discussion and Analysis (MD&A) combined with the Transmittal Letter, the Financial Statements and the Notes to the Financial Statements represent the complete 2016 financial activities for the City of Poulsbo.

These are all intended to:

- Assist the reader in focusing on significant financial issues
- Provide an overview of the City's financial activity
- Identify changes in the City's financial position
- Identify any material deviations from the financial plan and adopted annual budget
- Identify individual fund issues or concerns

FINANCIAL INFORMATION

The City's government wide financial statements have been prepared on the full-accrual basis of accounting in conformity with generally accepted accounting principles (GAAP). The City's Fund Financial Statements for governmental funds have been prepared on the modified accrual basis in conformity with GAAP. The City's proprietary funds are accounted for on the accrual basis.

The City of Poulsbo's financial system integrates financial and administrative controls that ensure the safeguarding of assets and the reliability of financial reports. These controls are designed to provide:

- Reasonable assurance that transactions are executed in accordance to management understanding and approval
- Reasonable assurance that transactions are executed in accordance to GAAP principles
- Accountability for control of assets and obligations
- Assurance that sufficient reporting and review exists to provide adequate information for analysis and comparability of data

Internal control is a high priority for the City. The Washington State Auditor's Office (SAO) reviews the City's internal controls, and the City receives and acts on all recommendations made by SAO.

FINANCIAL HIGHLIGHTS

- City of Poulsbo assets exceeded its liabilities at the close of the 2016 fiscal year by \$141 million (net position). Of this amount, \$18.2 million (unrestricted net position) may be used to meet the city's ongoing obligations to its citizens and creditors.
- Reported net position increased \$5 million. Net position of governmental activities increased \$1.7 million, or 2.38%, during 2016. Net position of business-type activities increased \$3.3 million, or 5.1%, during 2016. The variations are spread over several areas and can be attributed to many factors. Increase in development and sales tax revenue created a growing cash balance increasing the current assets. Construction of capital assets which were primarily grant funded increasing the City's assets, but not reducing cash. Contributed capital due to developments contributing infrastructure and street lights to the City. An increase in the City's Pension Obligation as figures are updated per GASB 68 standards and provided by Washington State Department of Retirement.

- Net investment in capital assets, increased \$3.1 million with the bulk of the increase occurring in business-type activities. Much of this is due to City projects being completed in 2016, including a project on Hostmark Street replacing infrastructure and pavement. Other factors were contributed capital inclusive of connections fees and infrastructure from developers.
- Total liabilities decreased by \$843,990. Most of the decrease can be attributed to the expiration of debt principal in large part because of an amount owed to a developer for the City's portion of the infrastructure improvements. A large final payment was made in 2016 reducing the liability.
- The book value of capital assets has increased \$1.7 million over 2015. Total capital assets from governmental activities increased \$73,422 or .1%. The increase in capital assets is primarily attributed to new equipment purchases and a pavement restoration project on Hostmark. Capital assets of business-type activities increased \$1.6 million or 3%. This is due to the completion of the Decant/Transfer Station and replacement of Hostmark infrastructure supporting the utility functions.
- City governmental fund tax revenue has increased an average of 4.9% for the past several years. This average is based on the largest increase in 2015 of 11.14% and the lowest of -.54% in 2013. In 2016, the City saw an increase over the prior year of \$331,538. Sales tax is the largest revenue source for Poulsbo and saw an increase of \$217,022. The increase is spread among many categories, with the largest category increases in Construction, Retail Trade and Food Services. This helps provide assurance the increase is not attributable to one time revenues, proving the hard work the Mayor and Council have done to diversify development.
- Utility taxes have seen a decrease in 2016 which is due to Council reducing the City utility tax rates for water and sewer services from 12% to 9%. The City continues to focus and promote diversification, planning for future growth and not remain dependent on a single line of business. It is the intention to lower utility tax rates for water and sewer to 6% in 2017, to be consistent with all other utility tax rates.
- The financial statements represent fund balances as required by GASB. Balance Sheets display fund balances in the following manner:
 - Unassigned – Residual net resources without any of the other fund balance limitations. The only fund which has an unassigned fund balance is General Fund.
 - Assigned – Amounts assigned for specific uses such city road maintenance or law enforcement funds not restricted by law
 - Committed – Self-imposed limitations at the highest level of decision makers that requires formal action at the same level. The City of Poulsbo does not have any committed fund balance for 2016.
 - Restricted – Fund balances which have externally enforceable limitations on use by grantors, creditors or legal restrictions
 - Nonspendable – This is comprised of assets, which will never convert to cash such as inventory or portion of proceeds which cannot be expended because they must be intact such as imprest funds
- At the close of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$7.9 million. Approximately 70% of this total amount, or \$5.5 million, is available for spending at the government's discretion and 30% or \$2.4 million is non-spendable or restricted per debt or legal requirements.
- At the end of the current fiscal year, the unassigned fund balance for the General Fund was \$1.1 million or 9.5% of the total General Fund expenditures. The total General Fund balance inclusive of the amount assigned for revenue stabilization and legal expenditures amounts to \$3.3 million which equates 27% of General Fund expenditures.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis provides an introduction and overview to the City of Poulsbo’s basic financial statements. The basic financial statements are comprised of three components.

- Government-wide Financial Statements
- Fund Financial Statements
- Notes to the Financial Statements

This report contains other supplementary information in addition to the basic financial statements, including combining statements for non-major funds, budget to actual comparisons and statistical tables.

Financial statements focus on both the City as a whole (government-wide) and on major individual funds. Both perspectives allow the user to address relevant questions, broaden a basis for annual comparisons and enhance the City’s accountability. A graphic is provided to illustrate the composition of the reports.

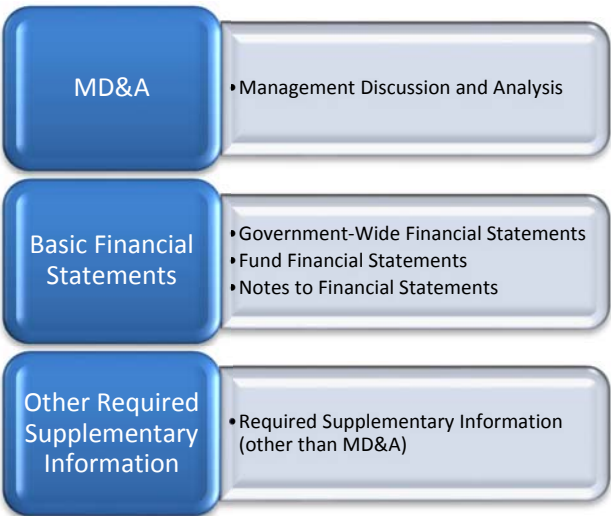
Government-Wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the City of Poulsbo’s finances in a manner similar to a private-sector business. The government-wide financial statements have separate columns for governmental activities and business-type activities. Governmental activities are primarily supported by taxes, charges for services and grants. Business-type activities are primarily self-supporting through user fees and charges.

The statements are presented in a full accrual basis of accounting including all assets, deferred outflows, deferred inflows and liabilities. Revenues are recognized when they are earned and expenses when they are incurred, regardless of when the cash transaction occurred.

The Statement of Net Position presents information on all the City’s assets, liabilities and deferred inflows/outflows, with the difference reported as net position. The Statement of Net Position 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 a useful indicator of improvement or deterioration in the City’s overall financial health.

The Statement of Activities presents information showing how the government’s revenues and expenses impacted net position during 2016. The statement distinguishes revenue generated by specific functions from revenue provided by taxes and other sources not related to a specific function. The revenue generated by specific functions (charges for services, grants and contributions) is compared to the expenses for those functions to show the degree to which each function supports itself or relies on taxes and other general funding sources. This is intended to summarize and simplify the user’s analysis of cost to various governmental services and/or subsidy to various business-type activities. By separating program revenue from general revenue, users of the financial statements can identify the extent to which each program relies on taxes for funding.



The Statement of Net Position and the Statement of Activities are divided into two categories:

- *Governmental Activities* - Most of the City's basic services are reported here, including the police, facilities, parks, planning, engineering and general administration. Taxes (property, sales, and utility) and intergovernmental revenues finance most of these activities.
- *Business-Type Activities* - The City charges a fee to customers to help cover all or most of the costs of certain services provided. The City charges fees to recoup the cost of the operations of water, sewer, storm drain, and solid waste utilities as well as all capital and debt expenses associated with the individual utility.

Fund Financial Statements

The annual financial report includes fund financial statements in addition to the government-wide financial statements. While the government-wide statements present the City finances based on the type of activity, the fund financial statements are presented by fund type. A fund is a fiscal and accounting entity with a self-balancing set of accounts used to account for specific activities or meet certain objectives. Funds are often set up in accordance with special regulations, restrictions or limitations.

The focus is on Major Funds rather than types. A Major Fund has three elements.

- Total assets plus deferred outflows, liabilities plus deferred inflows, revenues, or expenditures/expenses of that individual governmental or enterprise funds are at least ten percent (10%) of the corresponding total (assets, liabilities, etc.) for all funds of that category or type (i.e. governmental, proprietary, or fiduciary); and
- Total assets plus deferred outflows, liabilities plus deferred inflows, revenues, or expenditures/expenses of the individual government fund or enterprise funds are at least five percent (5%) of the corresponding total for all governmental and enterprise funds combined; or
- Any other governmental or enterprise fund the government's officials believe is particularly important

Governmental Funds: Governmental Funds are used to account for essentially the same functions reported as governmental activities in the Government-wide Financial Statements. These reports use a different "basis of accounting" than used in government-wide financial statements. The focus of governmental fund financial statements is on near-term inflows and outflows of available resources and on balances of resources available at the end of the fiscal year. Such information is useful in evaluating near-term financing requirements and immediate fiscal health.

Because the focus of governmental funds is narrower than that of the governmental-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. This provides the reader a better understanding of the long-term impact of the governments near-term financial decisions. To assist with the comparison, reconciliations between the governmental fund statements and the government-wide financial statements are included with the governmental fund Balance Sheet and the governmental fund Statement of Revenues, Expenditures, and Changes in Fund Balances.

The City of Poulsbo maintains budgetary controls over the governmental funds to ensure compliance with state law and council adoption at a fund level.

Proprietary Funds: The City's Proprietary funds are the enterprise funds which provide services to customers. The City uses enterprise funds to account for its water, sewer, solid waste and storm drain activities. The services and necessary capital expenditures are supported by rate payers. Proprietary funds use the same basis of accounting as business-type activities.

Fiduciary Funds: Fiduciary Funds are used to account for resources held for the benefit of parties outside the City. All the City's fiduciary activities are reported in separate Statements of Fiduciary Net Position and consist of Agency funds only. These activities are excluded from the City's government-wide financial statements because the assets cannot be used to finance the City's operations.

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.

Other Information: In addition to the basic financial statements and accompanying notes, this report also contains certain required supplementary information concerning the City of Poulsbo's progress in funding its obligation to provide pension benefits, and lifetime medical benefits to uniformed personnel hired before October 1, 1977. Required supplementary information may be found immediately following the notes to the financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

The Statement of Net Position looks at the City and can serve as a useful indicator of the City's financial position. Table 1 provides a summary comparing the City's net position for 2016 and 2015. Governmental Activities net position has an increase of \$1.7 million. The increase is due to several factors including growing cash balances, increased tax revenues and revenues related to development. Restricted Assets also show an increase primarily in the category restricted for Capital Purpose, which can be attributed to increases in Real Estate Excise Tax and Traffic Impact Fee revenues in 2016 needing to be restricted for specific capital uses. It is also important to highlight the change in assets and liabilities due to the recording of Pension Asset and Pension Obligations in accordance with GASB 68 requirements. These numbers are calculated based on figures provided by Washington State Department of Retirement Systems.

The Business-Type Activities had an increase of \$3.3 million to the Net Position. The increase is due to a combination of several items. Capital assets increased because of increases to construction of capital projects and contributed capital, largely due to increased number of utility connections in 2016. Reduction in liabilities is due to debt principal payments reducing the amount of outstanding debt. An obligation to a local developer for City infrastructure was issued a final payment in 2016. Construction of several business-type facilities including new pump stations, decant and solid waste transfer station, and new mains in congruence with road projects were completed or under construction in 2016. It is also important to highlight the change in assets and liabilities due to the recording of Pension Asset and Pension Obligations in accordance with GASB 68 requirements. These numbers are calculated based on figures provided by Washington State Department of Retirement Systems and can vary based on the states data.

The overall financial position for the City of Poulsbo has improved over the prior year. In 2016, assets exceeded liabilities by \$141 million, an increase of \$5 million or 3.7%. The largest portion of the City's net position, \$120 million or 85% reflects its investment in capital assets (land, buildings, machinery and equipment, infrastructure and intangible); less any related outstanding debt used to acquire those assets. The City's capital assets are used to provide services to citizens. Consequently, these assets are not available for future spending.

Table 1: Condensed Statement of Net Position

	GOVERNMENTAL ACTIVITIES		BUSINESS-TYPE ACTIVITIES		TOTAL PRIMARY GOVERNMENT	
	2016	2015	2016	2015	2016	2015
Current and Other Assets	\$ 10,682,558	\$ 9,545,920	\$ 16,767,947	\$ 16,259,610	\$27,450,505	\$25,805,530
Capital Assets Net	77,546,529	77,473,108	53,110,319	51,506,911	130,656,848	128,980,019
Pension Asset	349,038	615,157	-	-	349,038	615,157
TOTAL ASSETS	88,578,126	87,634,185	69,878,266	67,766,521	158,456,391	155,400,706
Deferred Outflows of	1,434,378	1,076,138	248,931	162,865	1,683,309	1,239,003
Long-term Debt	10,709,798	11,431,890	172,584	742,392	10,882,382	12,174,282
Pension Obligation	3,362,927	2,682,048	1,244,154	999,017	4,607,080	3,681,065
Other Liabilities	2,253,409	2,091,922	894,527	1,534,120	3,147,936	3,626,042
TOTAL LIABILITIES	16,326,134	16,205,860	2,311,265	3,275,529	18,637,399	19,481,389
Deferred Inflows of Resources	67,134	599,844	22,411	154,044	89,545	753,887
NET POSITION						
Net investment in Capital	67,834,718	67,037,545	52,652,252	50,368,250	120,486,970	117,405,795
Restricted	2,416,841	1,931,830	313,400	313,400	2,730,241	2,245,230
Unrestricted (deficit)	3,367,677	2,935,244	14,827,869	13,818,164	18,195,546	16,753,408
TOTAL NET POSITION	\$73,619,236	\$71,904,619	\$67,793,521	\$64,499,813	\$141,412,756	\$136,404,432

The City's total restricted net position amounts to 1.93%. These represent resources which are subject to external restrictions on how they may be used. Much of the amount can be attributed to restrictions for debt purposes, Real Estate Excise Taxes restricted for capital use by RCW and Impact Fees restricted for future development.

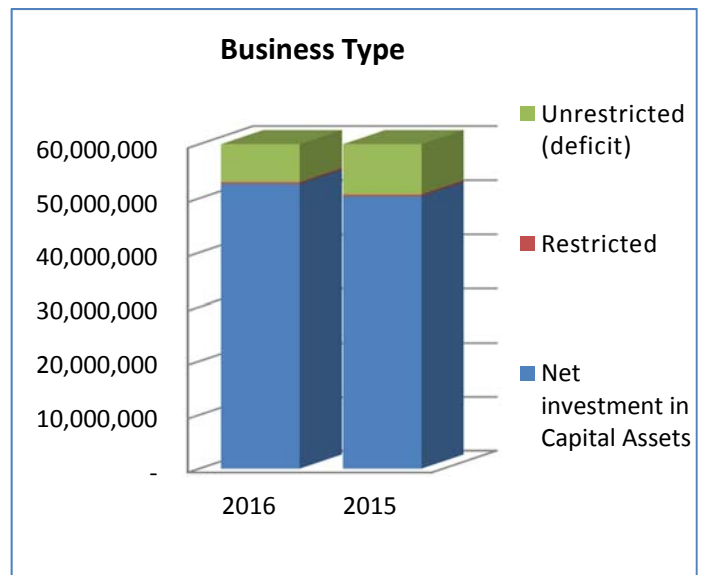
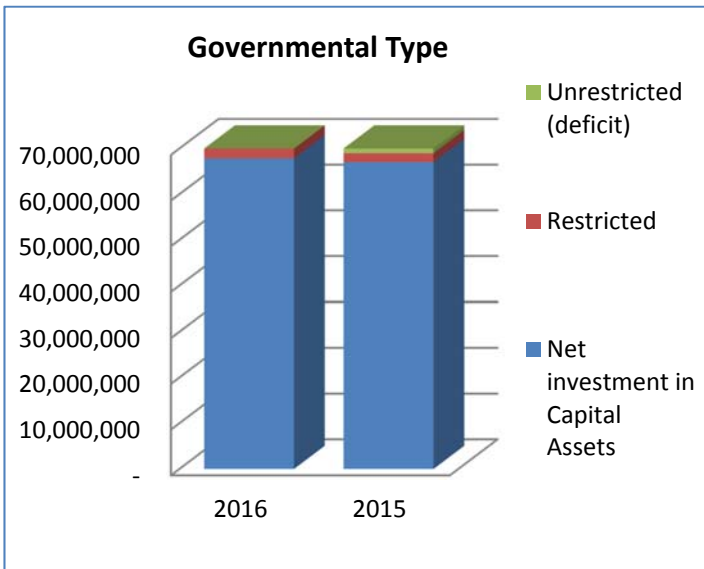


Table 2 illustrates changes in net position for the years 2016 and 2015. This is a condensed version of the Statement of Activities for the City. The revenues for 2016 show a decrease in Capital Grants/Contributions attributed to a combination of grant revenue and contributed capital of infrastructure such as roads and street lights for housing developments which occurred in 2015.

Table 2-Changes in Net Position

	GOVERNMENTAL ACTIVITIES		BUSINESS-TYPE ACTIVITIES		TOTAL PRIMARY GOVERNMENT	
	2016	2015	2016	2015	2016	2015
Revenues						
Program Revenues						
Charges for Services	\$ 2,492,172	\$ 2,152,681	\$ 8,733,046	\$ 8,254,566	\$ 11,225,218	\$ 10,407,247
Operating Grants/Contribr	710,043	605,198	84,948	115,058	794,992	720,256
Capital Grants / Contribr	1,633,211	5,027,389	2,234,980	5,784,476	3,868,191	10,811,865
General Revenues						
Property Taxes	2,264,194	2,191,189	-	-	2,264,194	2,191,189
Retail Sales & Use Tax	3,742,485	3,393,849	-	-	3,742,485	3,393,849
Business Taxes	2,708,005	2,786,469	-	-	2,708,005	2,786,469
Investment Earnings	76,833	40,329	54,780	30,716	131,613	71,045
Other	15,309	12,182	922	14,211	16,231	26,393
Total Revenues	13,642,252	16,209,286	11,108,678	14,199,027	24,750,929	30,408,313
Program Expenses						
General government	1,776,629	1,539,405	-	-	1,776,629	1,539,405
Judicial	383,968	370,046	-	-	383,968	370,046
Security of Per & Prop	3,327,528	3,146,848	-	-	3,327,528	3,146,848
Utilities & Environment	506,396	481,077	-	-	506,396	481,077
Transportation	2,922,462	2,703,349	-	-	2,922,462	2,703,349
Economic Environment	999,731	963,163	-	-	999,731	963,163
Mental & Physical Health	131,162	29,772	-	-	131,162	29,772
Culture & Recreation	1,469,255	1,422,703	-	-	1,469,255	1,422,703
Interest Long-Term Debt	391,781	458,869	-	-	391,781	458,869
Water	-	-	1,692,690	1,670,634	1,692,690	1,670,634
Sewer	-	-	2,686,558	2,531,582	2,686,558	2,531,582
Solid Waste	-	-	1,759,556	1,493,671	1,759,556	1,493,671
Storm Drain	-	-	1,676,166	1,433,190	1,676,166	1,433,190
Total expenses	11,908,913	11,115,232	7,814,970	7,129,077	19,723,883	18,244,309
Excess (deficiency)	1,733,339	5,094,055	3,293,707	7,069,950	5,027,046	12,164,004
Changes in Net Position	1,733,339	5,094,055	3,293,707	7,069,950	5,027,046	12,164,004
Beginning Net Position	71,904,619	69,094,319	64,499,813	58,476,477	136,404,432	127,570,796
Prior Year Adjustments	(18,722)	122,185	-	-	(18,722)	122,185
Prior Period Adjustments	-	(2,405,939)	-	(1,046,614)	-	(3,452,553)
Pension Obligation (GASB 68)						
Ending Net Position	\$ 73,619,236	\$ 71,904,619	\$ 67,793,521	\$ 64,499,813	\$ 141,412,756	\$ 136,404,432

GOVERNMENTAL ACTIVITIES

Revenues

Taxes account for the largest revenue category in the governmental funds, generating 64% of the total revenue. Much of tax revenue is received in the General Fund accounting for 89.9% of the tax revenue. This category tends to receive most attention because of the percentage ratio. Included in this category are sales, property, utility, criminal justice, and gambling taxes. Governmental fund taxes total \$8,714,683

Property tax receipts involve the very predictable effect of the 101% levy lid limitation, and a somewhat more variable consideration of new construction. The assessed valuation for property located within the City limits of Poulsbo for 2016 was \$1,346,103,503. The assessed value showed an increase from the prior year primarily due to new construction of several new housing developments and some commercial development. The property tax amount continued to be affected as the City levied slightly less than the full 1% increase above the highest allowable levy. For 2016, the City's regular property levy tax rate was \$1.69 per \$1,000 of assessed value.

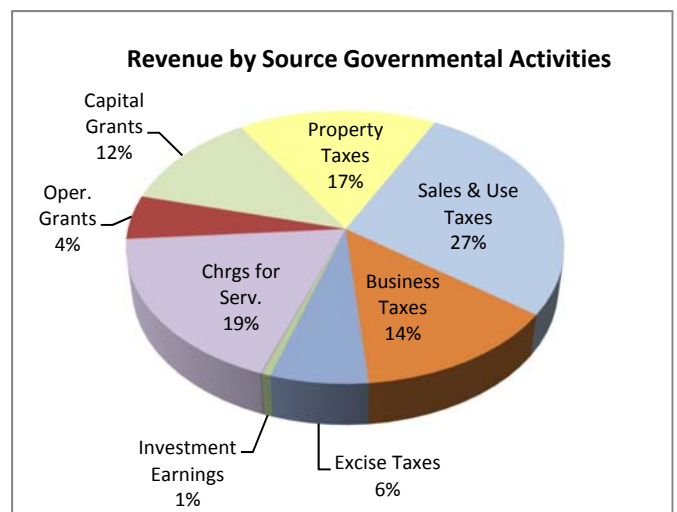
Sales and Use tax revenue, in contrast to property tax, can be a highly fluctuating tax source. The City saw a 7% increase in 2016. The revenue is an anticipated increase over the prior year, due to a growing economy and development. Not only are vacancies minimal in retail establishments, but new retail establishments opened in 2016. Many categories saw increases, with the largest being in Food Services. Existing businesses experienced growing revenues and a new drive up Starbucks opened in 2016 contributing to the increase. Another category increase was Construction, which is consistent with increased revenues related to development. It is anticipated to continue to see growth due to the strategic planning for diversification by the Mayor and Council. Sales tax continues to be the City's largest single source of revenue. The City's sales tax rate is 1% on all retail sales taking place within the City limits.

In 2016, sales tax received in the City's General Fund totaled \$3,437,042. The City's allocates a portion of sales tax revenue to other funds supporting capital equipment purchases.

Much of sales tax revenue (58%) comes from the retail trade category. The next largest sales tax categories are Accommodations and Food Services (12%) and Construction (10%). Retail development continues to be diversified throughout the City with new businesses opening throughout the City and not confined to certain areas.

Business Taxes are taxes applied to utilities providing services in the City, including City-owned and privately owned utilities. Overall, these taxes tend to be stable reflecting some growth from year to year and make up 21% of the governmental tax revenue. The utility rate for City water and sewer City owned utilities was reduced from 12% to 9% in 2016 and other City utilities of storm drain and solid waste maintained a 6% rate, consistent with other utility tax rates.

Excise Taxes are admissions tax, leasehold, and real estate excise tax (REET). Most these taxes are due to REET. Revenues fluctuate due to the change in the economy and home sales. There was significant growth (16%) in 2016 over 2015. The City uses the revenue generated by REET to fund debt payments related to the City Hall and transportation capital projects and reserves the remaining amount for future capital projects.



Expenses

General Government services encompass a variety of services including legislative, executive, financial, legal, judicial, personnel, building maintenance, and audit/risk management.

Judicial services provide support of the City's Municipal Court system.

Security of Persons and Property services are provided by the City's Police Department who works to provide professional law enforcement services to keep our citizens and their property safe. Special emphasis is placed on community-oriented programs that will prevent crime and forge a partnership between the officers and the citizens they serve.

Utility and Environment services create a satisfactory living environment for the City's residents. Inspection of private construction projects and coordinating the design of City projects are two examples of physical environment activities.

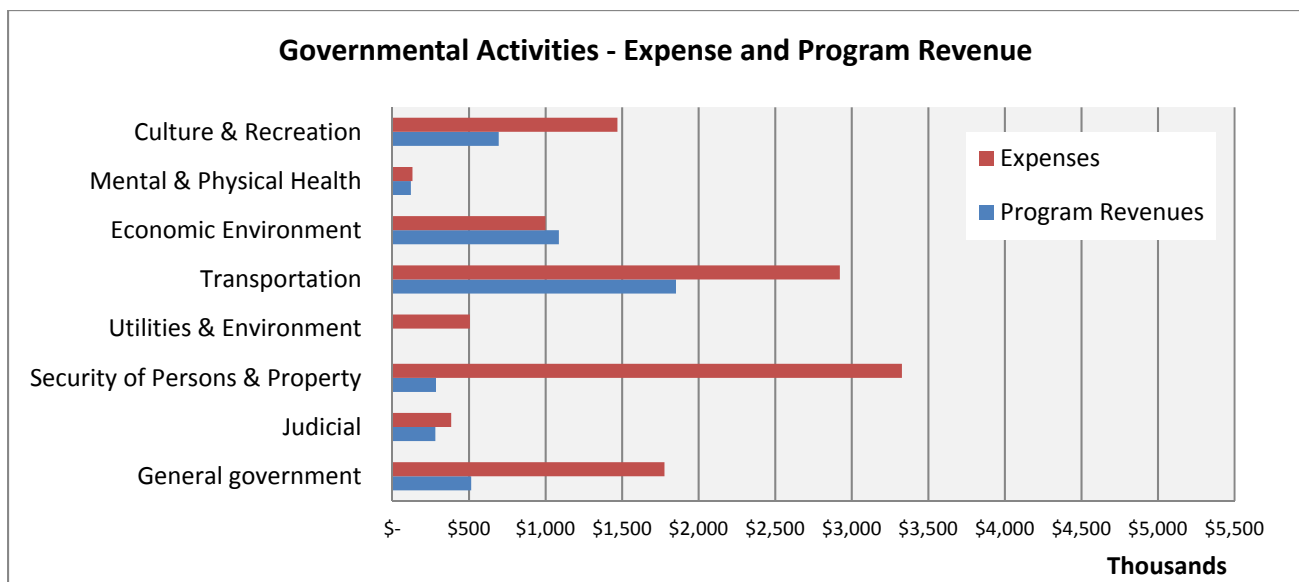
Transportation services provide maintenance of the City's streets, sidewalks, paths and traffic control signs/signals.

Economic Environment services include land use planning, zoning and community development.

Mental and Physical Health services include the City's support for the county's substance abuse program. The City is required by State law to commit 2% of our revenues from liquor profits and liquor tax to this program. The City has a contract with the Kitsap County Health District, which uses a formula based on population and assessed value to determine the City's level of subsidy.

Culture and Recreation services include expenditures for participant recreation programs and maintenance of the park facilities.

The chart below illustrates the surplus or net subsidy required for different, key City governmental-type programs. As illustrated, very few if any governmental activities are supported by direct revenue, which would mean they are largely supported by tax revenue.

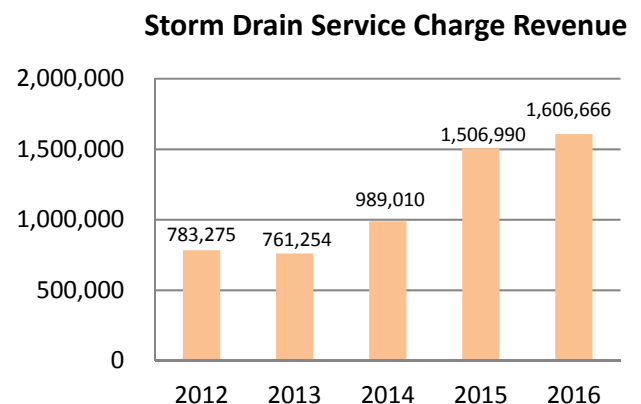
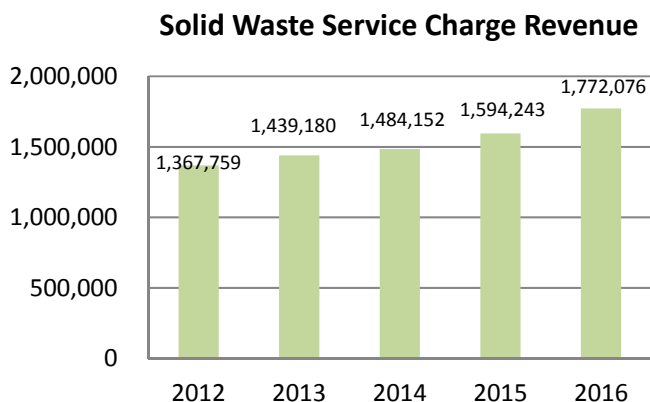
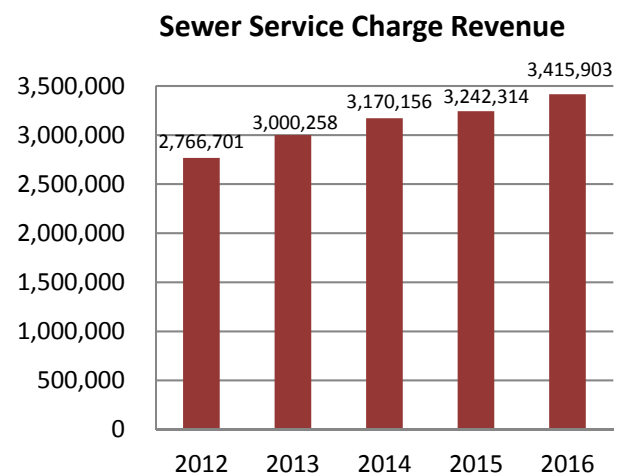
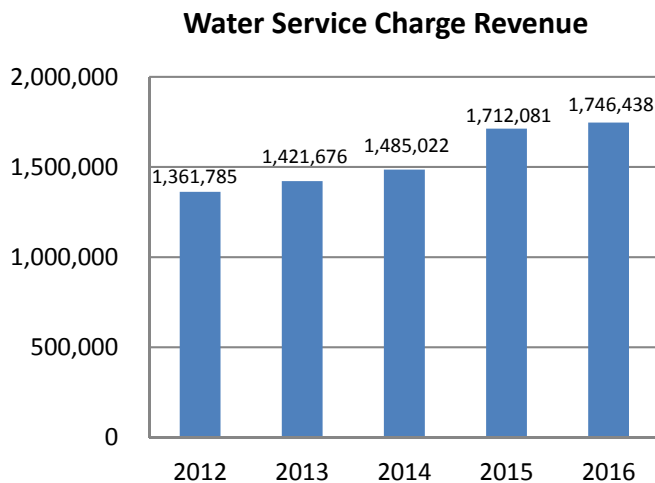


BUSINESS-TYPE ACTIVITY

Enterprise Funds: The City of Poulsbo owns and fully operates four utilities: water, sewer, storm drain, and solid waste/recycle. These utilities are accounted for in four enterprise funds as part of the City's fund structure and operations: 1) water utility fund; 2) sewer utility fund; 3) solid waste utility fund; and 4) storm drain utility fund. These services are supported by user fees, which include generating funds for future capital projects to maintain and provide services to the planned growth.

Key elements of the increases are as follows:

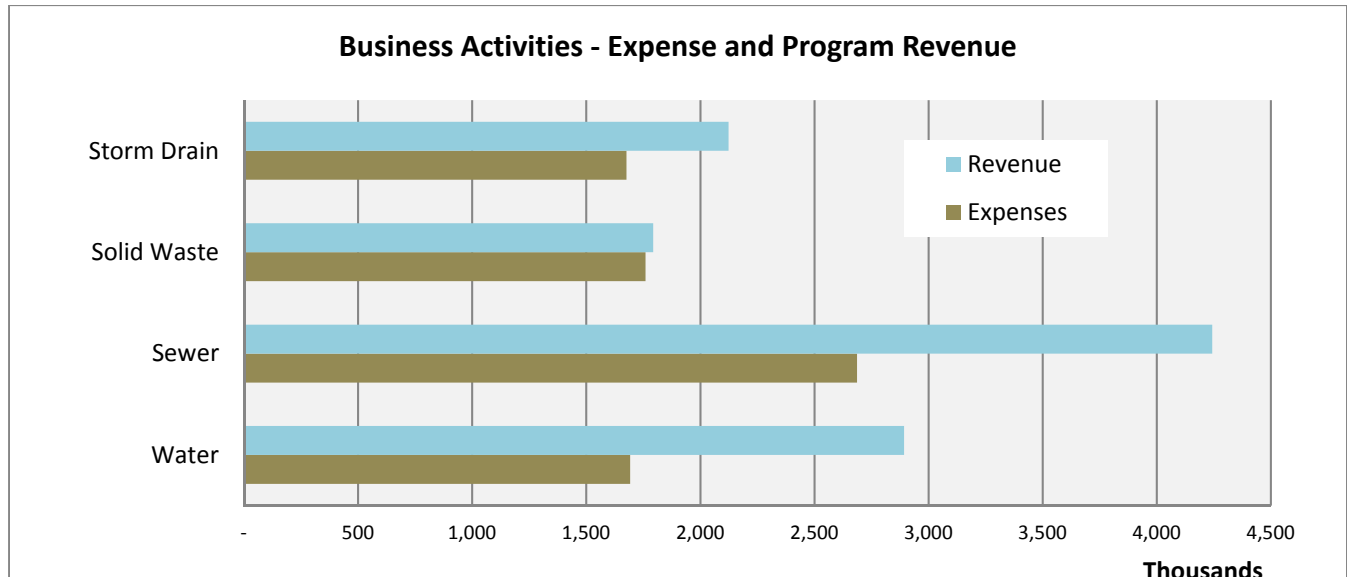
- There was a cost of living adjustment (COLA) for 2016, which resulted in an increase to utility rates creating an increase of revenue in 2016.
- The functional plan update for Storm Drain was completed in 2015 and rates significantly increased to fund operating costs as well as build a reserve balance for anticipated capital improvements.
- The functional plan update for Water was completed in 2015 and rates increased to fund operating costs as well as build a reserve balance for anticipated capital improvements.
- Solid Waste updated their technology and made operational changes so customers were correctly charged for garbage overage. This change is reflected in the 2016 increased revenue.



The City seeks to supplement business activities, as well as governmental activities, through the prudent application of third party funding sources in the form of grants wherever possible. During 2016, business activity program revenues exceeded expenditures because rates were set to accommodate future capital improvements for a fully functioning system and grants received to support both operations and capital projects in the Storm Drain system. Utilities, except for Solid Waste, implemented updated functional plans with rates to fund operating expenses and future improvements. The City conducted a study in 2016 evaluating solid waste services and the feasibility of continuing to provide the service or contract with an outside agency. It was determined the City will continue to provide the service but will be working on creating and implementing a functional plan for this service. Although functional plans cover much longer time frames, rates, at a minimum will be re-evaluated every three years to assure revenues are supporting expenses. The City will continue to address future needs and implementation of new and ever changing regulatory requirements.

Per an agreement with the County, the City will share in a joint project to upgrade the sewer's processing plant which will require payment in the next two years. The City will need to financially support the improvements based on the capacity of the plant owned by the City.

The chart below illustrates the surplus or net subsidy required for the City's business-type programs.



Major Fund Analysis

The City's Funds: Information about the City's major governmental funds begins on page 36. The City, in accordance with GASB 34, performed the major fund calculation and determined the General Fund met the requirements to qualify as major fund. The City decided to also present the Street Reserve Fund as a major fund. Over the next several years there will be substantial funds related to large grant funded transportation projects occurring and felt presenting the fund as a major fund will provide consistent reporting. These funds are accounted for using the modified accrual basis of accounting. As reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances, governmental funds have total revenues of \$13.9 million and expenditures of \$13.2 million.

- **General Fund:** General Fund accounts for the main operating revenues and expenditures of the City's governmental functions. Revenues and expenditures related to Administrative Services, Executive, Legislative, Finance, Police,

Engineering, Planning and Park Maintenance are some of the primary functions of the government accounted for in General Fund. The majority of tax revenues are receipted into the General Fund supporting governmental functions of the City.

The Fund Balance for the General Fund has increased by 3.6%. The City's revenues were greater than expenditures in 2016; increasing the fund balance. Although increased revenues can somewhat be attributed to development, creating one time fees, revenues such as sales tax and utility taxes are increasing because of the growing economy. Transfers to other funds for projects or reserving for future use were greater in 2016, creating more funds for future capital. An additional transfer for transportation was made in 2016 allocating funds for road preservation. The General Fund reserves still maintains a healthy fund balance and meets the criteria of the Financial Management Policy.

Although the use of reserves was anticipated to balance the fund, it was not necessary and reserves were only used for specific one time allocations as approved by City Council through budget amendments. Revenues have shown modest growth in almost every category. Some of contributing factors are:

- Sales tax revenue saw a significant increase in 2016
- Increase in development revenues for new projects constructing in Poulsbo
- Additional grant for mental health services to the City
- Increased revenues for the City's indirect service charge to other funds for services provided by the General Fund

The City maintains the bulk of general reserves in an Assigned Fund Balance which requires a super majority of City Council to approve allocation from the fund balance.

- **Street Reserve Fund:** The fund records revenue and expenditures for capital transportation projects. Resources consist of grants and transfers of general revenues primarily from the General Fund. In 2016, the City completed a pavement restoration program on Hostmark Street and design work for several other projects anticipated for construction in 2017. A very large project on Noll Road is planned over the next several years. It is anticipated to link to state routes, construct a roundabout, enlarge the number of lanes and relocate a transit station to this location. The project continued with the design process and began the right-of-way purchase process. Several right-of-ways will need to be purchased to complete the planned road.
- **Enterprise Funds:** The City's utilities are accounted for in four enterprise funds: 1) water utility fund; 2) sewer utility fund; 3) solid waste utility fund; and 4) storm drain utility fund. The funds are reported on a full-accrual basis, accounting for all assets and liabilities. Revenue is primarily charges for services by rate payers. Rates are developed to support ongoing operation as well as build reserves to support future capital needs. Fund balances remained consistent with the prior year, but slightly increased, due to several factors;
 - In 2016, there were large Capital Grants due a combination of connections fees and housing developments contributing capital in the form of infrastructure improvements.
 - Sewer and Storm Drain Funds saw increases in charges for services as both services had rate increases due to built in cost of living inflators.
 - Solid Waste recognized more revenues due to the ability to better charge customers for extra garbage which had not been done in the past.

BUDGETARY HIGHLIGHTS

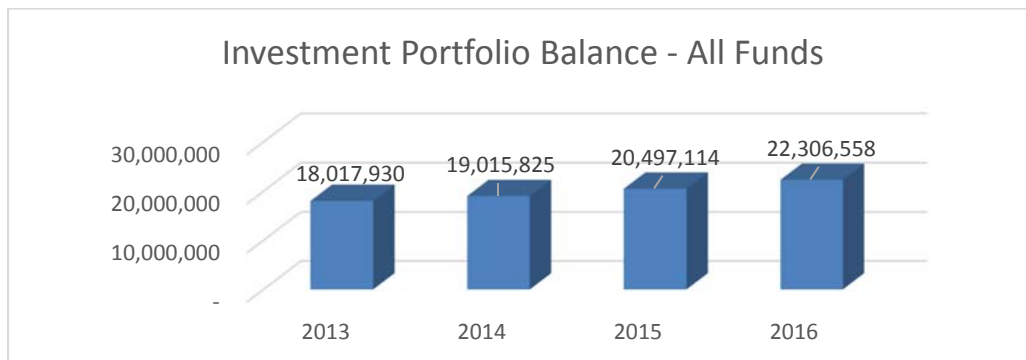
General Fund Budget Analysis: The following is a brief review of the budgeting changes from the adopted to the amended final budget for the General Fund. Please note, budget to actual comparisons start on page 40 for the major General Fund. Budget to Actuals for all other funds begin on page 98. The significant budgetary changes in the General Fund include:

- The final General Fund revenue budget increased by 1.7%, or \$180,950 of the original adopted budget. This was mainly due a new grant for mental health services and an increase in the indirect charges to proprietary funds for services provided by the General Fund.
- The final General Fund expenditure budget increased by approximately 5.2%, or \$587,531. The increase can be attributed to several items, but the main adjustments are:
 - Professional services for Engineering services specific to several ongoing projects such as transportation update, neighborhood streets evaluation and Marine Science Center short plat
 - Professional services to support economic development staffing changes and allocating funds for professional services to address the heavy workload in 2016
 - Overtime for the building department to address the heavy workload in 2016
 - Expenditures related with mental health grant
 - Expenses related to the City's new Code Enforcement officer
 - New rifle sights for the police department
 - Funds for a new Police Chief recruitment process
 - Transfer out to capital reserves to fund a neighborhood streets program
- The General Fund amended budget anticipated the ending Fund Balance to increase \$754,210 over the original projected ending Fund Balance. This increase is primarily due to the actual beginning balance being higher than the original projection.
- Per Council direction, Budget verses Actual is monitored regularly and any variations more than 15% are highlighted. Some areas of variance highlighted were:
 - Revenues related to development fees were larger than anticipated
 - Capital projects and grants were not completed as per projected and most will carry over into 2017
 - Real Estate Excise Taxes were larger than anticipated and higher than the previous trend
 - Unanticipated drug seizure revenues were collected
- Copies of the City's Budget and Budget-in-Brief are available on our website www.cityofpoulsbo.com. The complete budget provides details of the City's plans for using its resources during the biennial cycle and may also be obtained by contacting our Finance Director at 360-394-9720 or dboohier@cityofpoulsbo.com.

CASH MANAGEMENT

Aggressive efforts to maximize interest earnings of temporary cash reserves have been as successful as the economy allows. The City contracts with an investment broker for professional recommendations to maintain security and liquidity of the City's cash in accordance with the City's certified Investment Policy. The City manages cash accounts by the pooled cash management concept and plans investment maturities to coincide with cash needs. The pool concept provides for investing greater amounts of money at more favorable interest rates, but still maintaining liquidity.

The chart reflects the investment balances as of December 31.



The City has a Financial Management Policy with recommended levels of cash and reserves. The policy calls for 12% of operating revenues and/or 2 months operating cash. These balances are regularly monitored to assure compliance with the requirements of the policy. Use of reserves, which are intended for one time, not ongoing expenditures, requires a super majority of City Council for approval. Ongoing obligations will be built into future budgets supported by City revenues. Monthly, the City Council receives and reviews an extensive variance report including cash levels and budgetary compliance, noting items which are less or greater than the recommended variance. This report is also posted to the City's website.

DEBT ADMINISTRATION

The City participates in various forms of debt, which is summarized as follows: \$9.3 million of a General Obligation (GO) bond type. There are two types of GO debt; those that are retired by tax levies (Voted GO/Levy) and those that, while secured by the tax base, are being retired by revenue from the various sources and funds. The City also has one Public Works Trust Fund loans (PWTF) recorded in Governmental Activities with a principal balance of \$297,473.

Revenue bonds are retired by means of revenue in the proprietary funds. There is no general tax liability for these obligations. Revenue bond debt in utilities is controlled by bond covenants. The outstanding principal amount is \$475,000 with final payment being made in 2017

The City's debt obligations are well within the statutory limits for debt capacity. There are three types of statutory limits on general obligation debt capacity:

1. The first limit is on the amount of general obligation debt that can be incurred without a vote of the people. For this type of debt, a city is limited to 1.5% of its assessed value (\$1,487,955,331), or \$22,319,330;
2. The second statutory limit is the amount of general obligation debt a city may incur for general governmental purposes with a vote of the people. This limit is 2.5% of the assessed value (\$1,487,955,331). For 2017, the City's limit is \$37,198,883 less any amount issued as non-voted debt. At this time, the City does not have any voted debt.
3. The third limit is also calculated as a percentage of assessed value. This statutory limit allows a City to incur general obligation debt of up to an additional 2.5% of its assessed value for bond issues approved by the voters for the purpose of utility improvements and an additional 2.5% for parks or open space development.

To follow is a chart showing the debt limits as of the end of 2016:

This Debt is controlled by assessed Valuation Debt Limits						
			2017 Assessed Valuation	\$ 1,487,955,331	Outstanding Debt	\$ 9,295,000
X	0.025	=	\$ 37,198,883	Limited for Combined Debt	Balance Available	\$ 27,903,883
X	0.015	=	\$ 22,319,330	Limited for Non-Voted Debt	Balance Available	\$ 13,024,330

Additional information on the City's debt is provided in Note 8, "Long-Term Debt" and may be found on page 69 of these statements.

CAPITAL EQUIPMENT AND UPGRADING CAPITAL FACILITIES

The City has a capital threshold of \$5,000. Equipment for governmental services are funded from reserves built in the Capital Acquisition Fund. Fund resources consist of transfers from the General Fund to the Capital Acquisition Fund. The transfer amounts are established by City Council through the budget process. Capital purchases are prioritized and items not falling within the funding levels were delayed or reserves were allocated to purchase necessary capital items.

The City's budget continues to primarily focus on operation and maintenance costs. Annually the City updates the City Improvement Plan (CIP) to prioritize and establish funding sources for capital outlay costs to maintain and upgrade existing infrastructure. With revenue streams continually being challenged, the City has had the fortune of securing grants for many of the capital transportation, park and storm drain projects. The City continues to allocate funds for pavement restoration in the neighborhood streets. Neighborhood streets do not qualify for grant funding, so Council established a funding source and process to maintain infrastructure. In 2016, the existing road inventory was evaluated and in 2017 the City will be testing three different types of road restoration to find the best quality for the best price. The City continually struggles to direct more efforts to building maintenance programs and plan for future renovation and replacement, but does address the requirement during the Capital Improvement Plan process by highlighting the necessary ongoing maintenance costs. The City continues to look for energy savings measures and revenue streams to support ongoing maintenance of City facilities.

The increase in capital assets in 2016 is primarily in business type activities. A project on Hostmark Street, replacing the mains for all utilities was completed in 2016 and the primary contributor of the increase. A project on Noll Road, occurring over several years and phases began the design and right of way purchase process in 2016. The project will primarily be transportation, but will also include infrastructure improvements supporting City utilities. Another contributor to capital assets is contributed capital from new housing developments consisting of retention ponds for storm drain functions and streets throughout developments. There will be many Capital projects in 2017 with much of the focus on sewer pump stations, well replacements and Noll Road corridor as well as new garbage trucks to replace old fleet vehicles. Additional information on the City's capital assets is provided in Note 5, beginning on page 59.

Table 3-Capital Assets at Year End, Net of Depreciation

	GOVERNMENTAL ACTIVITIES		BUSINESS-TYPE ACTIVITIES		<u>TOTAL</u>	
	2016	2015	2016	2015	2016	2015
Land/Intangibles	31,210,860	30,658,826	2,160,490	2,160,490	33,371,350	32,819,316
Buildings	12,956,585	13,304,812	2,483,161	226,685	\$15,439,746	13,531,497
Other Improvements	10,215,852	10,450,869	46,288,603	43,145,043	\$56,504,455	53,595,912
Infrastructure	21,151,025	21,781,858			\$21,151,025	21,781,858
Intangibles (Depreciable)	90,334	112,851	133,879	174,150	\$224,213	287,000
Machinery & Equipment	716,087	669,715	878,694	599,700	\$1,594,781	1,269,415
Work in Progress	1,205,786	494,178	1,165,493	5,200,843	\$2,371,278	5,695,021
Totals	\$77,546,529	\$77,473,108	53,110,319	\$51,506,911	130,656,848	128,980,019

ECONOMIC FACTORS AND POULSBORO IN THE FUTURE

The State of Washington does not have a state personal income tax and therefore the state operates primarily using property, sales, utility, and gas taxes. The City relies on sales, property and utility taxes and a limited array of other permitted taxes, fees, and state and federal grants to support governmental activities.

For the business-type and certain governmental activities (permitting, recreation programs, etc.) the user pays a related fee or associated charge.

Sales tax represents a major revenue source for governmental funds and provides an economic measurement of the local economy. The City has continued to see an increase of more than 5% in sales tax since 2013. The increase is anticipated to continue with new and expanded commercial development occurring in the City. The good news is the increase is diversified and not attributed to one category, helping to sustain and provide assured future revenues. Residential development continued in 2016 and is expected to continue at a strong pace in 2017, with many projects going through the planning and permitting process. At present there is an inventory shortage for housing in both owning and renting. There are several multifamily structures expected to be completed in 2017 helping to provide housing and alleviate some of the demand. Commercial construction continued in 2016 with new establishments expected to open for business in 2017, including a local car wash, a new drive-up Starbucks and paint supply store. The City continues to grow and maintain strong revenues because of diversification and promotion of economic development. The City was able to continue growth, while maintaining a healthy level of reserves. Overall the average sales tax for the five years preceding 2017 reflected a 3% increase. In 2017 the City adopted its first biennial budget and the City Council maintained practice of developing conservative but realistic projections. Past conservative estimates have supported a larger beginning balance as revenues continue to increase.

As the City crossed the 10,000-population threshold, the City is allowed to levy the lower of 1% of the highest allowable levy or Implicit Price Deflator (IPD) for July. In 2017 the IPD was less than 1%, which then requires Council to pass a “substantial need” resolution to levy the full 1%. With healthy revenues and fund balances in 2016 the City Council chose to not take the 1% of the highest allowable levy allowed by law, however, they did pass the “substantial need” resolution to bank the capacity for future levies.

A utility rate of 9% for water and sewer was set for 2016, which was lower than the 2015 rate of 12%. The amount is consistent with the statewide average. The goal of City Council is to review utility tax rates through the budget process and lower the rate to 6% consistent with other utility tax rates. The rates will be decreased to 6% for 2017 and allow utility user rates to minimize future rate increases.

Utility functional plans have been updated or are in the process of updates. A study was conducted in 2016 for the feasibility of the City continuing to operate the Solid Waste Utility. It was determined the City would continue providing solid waste services. A functional plan will be prepared in 2017 and address levels of service and rates to support the services.

The City must participate with the County for sewer plant upgrades, and new regulatory requirements decreasing environmental impacts. Rates and capital plans have been built to support these requirements. The City's share of this capital has been included in the 2017 City Improvement Plan and is anticipated to issue revenue debt for the City's first contribution of approximately \$5 million.

Several large construction projects continued in 2016. Noll Road corridor is much of the City's focus in the future, which will include connectivity of State Route 305, pedestrian and bicycle safety and a future location of Kitsap Transit Transfer Station. Several right of ways must be purchased, which will occur in 2017. Much of the project is grant funded, but may require a General Obligation debt issue for the City's match. The City is still actively looking for grants to support the additional funding requirement.

The City received a local grant spanning through mid-2017. This has allowed the City to proactively address the growing population with mental health issues. The program directs persons to available resources to help and support keeping them out of the legal system. It is anticipated the City will apply for continued grant funding allowing personnel to continue to support the City's Court and Police Department needs.

The City's estimated population in 2016 is 10,210 growing by 260 people or 2.6% as reported by the Office of Financial Management (OFM). Since the City's population has now crossed the 10,000 threshold, the City is classified as a Class A city adding legal requirements. The City has and will continue to address additional requirements from the change. The primary impact was related to the property tax increase, but other changes will not be much of an impact as most of the requirements have been standard operation for the City. Daytime population is much higher and will continue to grow as Poulsbo becomes a destination for many county residents to shop, obtain medical treatments and send students to school for all grade levels including College. This continues to be a challenge for utilities to provide services in peak hours. The City has an agreement with Kitsap Public Utility District (KPUD) providing the ability to purchase water and provide water services in new development areas in the west end of the City, adjacent to their service area. At this point it has not been necessary for the City to purchase additional water, but new developments in the City's formally annexed area are serviced by the KPUD for water services. This will continue to allow development but not tax the City's water system for fire protection and peak hours. The City also provides sewer, garbage and storm drain service and receives utility tax for these services.

Washington continues to be a state impacted by tax limiting initiatives and a struggling state budget. The City receives funds related to liquor sales in two different distributions. The first is liquor profits and the second is liquor excise tax. Both are distributed as a state shared revenue, based on population. The state reduced the shared excise taxes to support the state budget. Amounts have been reinstated to cities, but still not at the funding level prior to the reductions. Cities tried to request full restoration, but the state budget was adopted without fully restoring funding. It is anticipated funding in the next couple years will stay consistent with the 2016 level. Funds distributed to Poulsbo are not substantial, so although it is an impact, it is slight.

A possible change to retirement rates for Law Enforcement personnel is being proposed for the state to not supplement the rate, but local agencies to fund the entire rate. This could be a substantial increase of almost 3% to retirement rates for our law enforcement personnel.

The Mayor and City Council continue to be proactive with other agencies to monitor and lobby for regulations to minimize the impact to the City, and provide funds for City services. The City continues to support a possible street utility to provide funding to maintain streets and pay for growing electricity charges related to street lights. The City will continue to work with surrounding agencies for sharing of service opportunities and minimize expenses.

An allowable fee the City may be able to implement through councilmatic action or a larger amount by the voters is Transportation Benefit District Fees. The fees must be used for transportation expenditures clearly defined upon implementation. The Council continues to discuss this option in conjunction with the transportation plan update. Once passed the fee cannot be collected for 6 months. Three surrounding Cities within Kitsap County have implemented the fee. With property tax revenue growth limited, but growing needs for transportation improvements, this will continue to be explored.

A large change for the State of Washington, contradictory to federal laws, passed by voters is the legalization of marijuana, not only for medicinal but recreational use. A state excise tax and license fees will be imposed on retailers. The majority of funds will remain at the state level. Allocation of shared revenues was established in 2015, but only distributed back to localities who allow the retail establishments for sale of legal recreational marijuana. Sales are subject to retail sales tax and distributed back to the local agencies in their sales tax distributions. At this time there are no existing businesses located in the City of Poulsbo, and formal council action was passed to not allow any of these establishments to operate within the City limits, so the City will not be a recipient of the state shared revenue.

The local Olympic Community College has partnered with Western Washington University to offer four-year programs allowing citizens the option for an affordable and local degree program. City Council is working collaboratively with local organizations to market and emphasize this asset, bringing more citizens and businesses to our local area. The College is growing the number of 4-year degree programs and in 2016 has added a Cyber Security degree.

The City has changed the lease for the Marine Science Center building to be held with Western Washington University to operate the program. The City is working on correcting the boundary lines of the building with the intention of giving the building to Western Washington University to use for educational purposes. This will eliminate any building maintenance or operation expenditures and allow citizens to continue to benefit from a Marine Science program.

The City is correcting property lines for the Library operated by the County Library district. The intention is for the Library to take ownership of the library building and all associated maintenance and operational costs of the building.

The level of taxes, fees and charges for services (including development related mitigation fees) will have a bearing on the City's competitive ability to encourage retail, office, residential, and industrial development to locate in their jurisdiction. 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.

Request for Financial Information

This financial report is designed to provide our citizens, taxpayers, creditors and investors with a general overview of the City's finances and to show the City's accountability for the monies it receives. Any questions about this report or requests for additional financial information should be addressed to the Finance Department, City of Poulsbo, 200 NE Moe Street, Poulsbo, Washington, 98370. Personal inquiries may be directed to Jana Brown, Accounting Manager at (360) 394-9721, jbrown@cityofpoulsbo.com or Deborah Booher, Finance Director at (360) 394-9720, dbooher@cityofpoulsbo.com.

**STATEMENT OF NET POSITION
DECEMBER 31, 2016**

	Primary Government		
	Governmental Activities	Business-Type Activities	Total
Assets			
Cash and Cash Equivalents	\$ 1,335,434	\$ 1,353,148	\$ 2,688,583
Investments	7,626,964	14,275,178	21,902,142
Receivables: <i>Net of Uncollectibles</i>			
Taxes	1,049,826	-	1,049,826
Customer Accounts	183,597	756,559	940,156
Special Assessments	16,539	-	16,539
Other Receivables	106,103	-	106,103
Due from Other Governments	114,349	15,923	130,272
Materials and Supplies Inventory	4,947	52,239	57,185
Prepaid Items	-	1,500	1,500
Restricted Assets:			
Investments	91,016	313,400	404,416
Note Receivable	153,784	-	153,784
Capital Asset not being depreciated:			
Land & Right of Ways	31,210,860	2,160,490	33,371,350
Construction in Progress	1,205,786	1,165,493	2,371,278
Capital Assets (net of accumulated depreciation):			
Buildings and Structures	12,956,585	2,483,161	15,439,746
Other Improvements	31,366,878	46,288,603	77,655,480
Machinery and Equipment	716,087	878,694	1,594,781
Intangibles	90,334	133,879	224,213
Pension Asset	349,038	-	349,038
Total Assets	88,578,126	69,878,266	158,456,391
Deferred Outflows of Resources			
Deferred Amount of Refunding	605,929	16,933	622,862
Pension	828,449	231,998	1,060,447
Total Deferred Outflows of Resources	1,434,378	248,931	1,683,309
Liabilities			
Current Payables:			
Accounts/Claims	537,726	209,815	747,540
Employee Wages	371,601	73,537	445,138
Interest	33,066	38,372	71,438
Due to other Governments	74,368	-	74,368
Unearned Revenues	99,500	4,076	103,575
Customer Deposits	357,466	74,552	432,018
Long-Term Liabilities:			
Due within one year	779,683	494,176	1,273,859
Due in more than one year	10,709,798	172,584	10,882,382
Pension Obligation	3,362,927	1,244,154	4,607,080
Total Liabilities	16,326,134	2,311,265	18,637,399
Deferred Inflows of Resources			
Pension	67,134	22,411	89,545
Total Deferred Inflows of Resources	67,134	22,411	89,545
Net Position			
Net Investment in Capital Assets	67,834,718	52,652,252	120,486,970
Restricted for:			
Capital Purpose	2,022,601	-	2,022,601
Drug Enforcement	65,362	-	65,362
Criminal Justice	94,946	-	94,946
Promoting Downtown Businesses	48,360	-	48,360
Promoting Tourism	76,460	-	76,460
City Beautification-Expendable	1,850	-	1,850
City Beautification-Nonexpendable	91,016	-	91,016
Debt Service	16,246	313,400	329,646
Unrestricted	3,367,677	14,827,869	18,195,546
Total Net Position	\$ 73,619,236	\$ 67,793,521	\$ 141,412,756

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

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2016**

Page 1 of 2

		Program Revenues		
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Governmental activities:				
General government	\$ 1,776,629	\$ 370,369	\$ 143,862	\$ -
Judicial	383,968	279,232	745	-
Security of Persons & Property	3,327,528	133,347	150,772	-
Utilities & Environment	506,396	3,400	-	-
Transportation	2,922,462	82,592	219,860	1,549,664
Economic Environment	999,731	1,087,421	-	-
Mental & Physical Health	131,162	-	120,227	-
Culture & Recreation	1,469,255	535,811	74,578	83,546
Interest on Long-Term Debt	391,781	-	-	-
Total Governmental Activities	11,908,913	2,492,172	710,043	1,633,211
Business-Type Activities:				
Water	1,692,690	1,857,036	-	1,035,502
Sewer	2,686,558	3,460,657	9,347	773,422
Solid Waste	1,759,556	1,793,421	-	-
Storm Drain	1,676,166	1,621,933	75,601	426,057
Total Business-Type Activities	7,814,970	8,733,046	84,948	2,234,980
Total Primary Government	\$ 19,723,883	\$ 11,225,218	\$ 794,992	\$ 3,868,191

General Revenues:

Property Taxes
Retail Sales & Use Taxes
Business and Occupation Taxes
Excise Taxes
Unrestricted Interest & Investment Earnings
Gain (loss) on disposal of capital assets

Total General Revenues

Change in Net Position

Net Position Beginning of Year

Prior Period Adjustments

Net Position End of Year

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

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2016**

Page 2 of 2

Net (Expenses) Revenue and Changes in Net Position			
Primary Government			
Governmental	Business-Type		
Activities	Activities	Total	
\$ (1,262,398)	-	\$ (1,262,398)	
(103,991)	-	(103,991)	
(3,043,408)	-	(3,043,408)	
(502,996)	-	(502,996)	
(1,070,346)	-	(1,070,346)	
87,690	-	87,690	
(10,935)	-	(10,935)	
(775,320)	-	(775,320)	
(391,781)	-	(391,781)	
(7,073,487)	-	(7,073,487)	
-	1,199,847	1,199,847	
-	1,556,867	1,556,867	
-	33,865	33,865	
-	447,425	447,425	
-	3,238,005	3,238,005	
(7,073,487)	3,238,005	\$ (3,835,482)	
2,264,194	-	2,264,194	
3,742,485	-	3,742,485	
1,841,119	-	1,841,119	
866,886	-	866,886	
76,833	54,780	131,613	
15,309	922	16,231	
8,806,826	55,702	8,862,528	
1,733,339	3,293,707	5,027,046	
71,904,619	64,499,813	136,404,432	
(18,722)	-	(18,722)	
\$ 73,619,236	67,793,521	\$ 141,412,756	

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

**BALANCE SHEET-GOVERNMENTAL FUNDS
DECEMBER 31, 2016**

	General Fund	Street Reserve Fund	Non-Major Governmental Funds	Total Governmental Funds
Assets				
Cash and Cash Equivalents	\$ 543,077	\$ 321,421	\$ 470,937	\$ 1,335,434
Investments	3,828,015	845,048	2,953,901	7,626,964
Receivables:				
Taxes	6,378	-	55,389	61,767
Accounts	9,114	-	-	9,114
Special Assessments	-	-	16,539	16,539
Due from other govern units	48,637	58,364	7,347	114,349
Inventories	4,947	-	-	4,947
Cash and Investments-Restricted	-	-	91,016	91,016
Total Assets	4,440,168	1,224,832	3,595,129	9,260,129
Deferred Outflows of Resources	-	-	-	-
Total Assets and Deferred Outflows of Resources	\$ 4,440,168	\$ 1,224,832	\$ 3,595,129	\$ 9,260,129
Liabilities				
Accounts Payable	349,642	77,692	110,392	537,726
Payroll Payable	357,056	1,272	13,273	371,601
Unearned Revenues	87,407	-	12,093	99,500
Custodial Accounts	357,466	-	-	357,466
Total Liabilities	1,151,571	78,964	135,757	1,366,292
Deferred Inflows of Resources	-	-	-	-
Fund Balances				
Nonspendable fund balance	7,597	-	91,016	98,613
Restricted fund balance	-	-	2,325,825	2,325,825
Assigned fund balance	2,174,924	1,145,868	1,042,531	4,363,323
Unassigned fund balance	1,106,077	-	-	1,106,077
Total Fund Balances	3,288,597	1,145,868	3,459,372	7,893,837
Total Liabilities, Deferred Inflows of Resources and Fund Balances	\$ 4,440,168	\$ 1,224,832	\$ 3,595,129	\$ 9,260,129

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

**RECONCILIATION OF TOTAL GOVERNMENTAL FUND BALANCES TO
NET POSITION OF GOVERNMENTAL ACTIVITIES
December 31, 2016**

Total Governmental Fund Balances: \$ 7,893,837

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

Capital assets used in governmental activities are not financial resources and therefore are not reported in the governmental funds. 77,546,529

These assets consist of:

Land	\$	31,210,860	
Buildings and structures		17,115,446	
Improvements		46,879,658	
Machinery and Equipment		3,178,969	
Construction in Progress		1,205,786	
Intangibles		647,486	
Less: Accumulated Depreciation		(22,691,675)	

Other Assets that are not available to pay for current-period expenditures and therefore are not reported in governmental funds. 3,205,845

Long-term liabilities, including bonds payable are not due and payable in the current period and therefore are not reported in the governmental funds.

Interest Payable	33,066		
Long-term Liabilities	14,993,910	(15,026,976)	

Net Position of governmental activities		<u>\$ 73,619,236</u>	
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The notes to the financial statements are an integral part of this statement.

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016

	General Fund	Street Reserve Fund	Non-Major Governmental Funds	Total
Revenues				
Taxes	\$ 7,801,969	\$ -	\$ 875,462	\$ 8,677,430
Licenses and Permits	886,385	-	14,800	901,185
Intergovernmental	301,171	475,684	273,426	1,050,282
Charges for Services	2,521,626	-	452,769	2,974,396
Fines and Forfeitures	70,774	-	-	70,774
Interest and Other Earnings	70,892	1,414	9,914	82,219
Miscellaneous	92,473	-	94,367	186,840
Total Revenues	11,745,290	477,098	1,720,738	13,943,125
Expenditures				
Current:				
General Government	3,108,256	-	-	3,108,256
Security of Persons & Property	3,120,582	-	31,714	3,152,296
Utilities and Environment	532,379	-	-	532,379
Transportation	651,482	-	795,088	1,446,570
Economic Environment	898,672	-	111,816	1,010,489
Mental and Physical Health	131,162	-	-	131,162
Culture and Recreation	1,128,766	-	94,803	1,223,569
Debt Service:				
Principal	-	-	709,368	709,368
Interest & Other Charges	-	-	373,098	373,098
Capital Outlay	-	810,783	668,528	1,479,311
Total Expenditures	9,571,301	810,783	2,784,416	13,166,499
<i>Excess of Revenues Over (Under) Expenditures</i>	<i>2,173,989</i>	<i>(333,685)</i>	<i>(1,063,678)</i>	<i>776,626</i>
Other Financing Sources (Uses)				
Transfers In	5,000	775,500	2,122,411	2,902,911
Transfers Out	(2,078,487)	(5,000)	(819,424)	(2,902,911)
Sale of Capital Assets	7,649	-	-	7,649
Insurance Recoveries	5,206	-	-	5,206
Total Other Financing Sources and Uses	(2,060,632)	770,500	1,302,987	12,855
<i>Net Change in Fund Balances</i>	<i>113,356</i>	<i>436,815</i>	<i>239,309</i>	<i>789,481</i>
<i>Fund Balances Beginning of Year</i>	<i>3,175,241</i>	<i>709,053</i>	<i>3,238,785</i>	<i>7,123,079</i>
<i>Prior Year Adjustment</i>	<i>-</i>	<i>-</i>	<i>(18,722)</i>	<i>(18,722)</i>
Fund Balances End of Year	\$ 3,288,597	\$ 1,145,868	\$ 3,459,372	\$ 7,893,837

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

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2016**

Net change in Fund balance--total governmental funds	\$	789,481
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Amounts reported for Governmental activities in the statement of activities are different because:

Government 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 expenditure.

This is the amount of capital outlays		1,479,311
This is the amount of depreciation		(2,098,757)
This is the amount of Gain (Loss) on Capital Assets		7,661

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the government funds.		274,063
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Developers construct and then contributed capital infrastructure assets to the City. These assets are reported on the statement of activities but not reported in the fund statements.		685,208
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Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net position. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net position. This is the amount by which repayments exceeded proceeds.

Principal payments		709,368
Bond Proceeds		-
Premium on Bonds Sold		-

Some expenses reported in the statement of activities do not require the use of the governmental funds.		(112,995)
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Change in net position of governmental activities	\$	<u>1,733,339</u>
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The notes to the financial statements are an integral part of this statement

**STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2016**

	ORIGINAL BUDGET	FINAL BUDGET	ACTUAL	VARIANCE WITH FINAL BUDGET POSITIVE (NEGATIVE)
Revenues				
Taxes	\$ 7,282,339	\$ 7,282,339	\$ 7,801,969	\$ 519,630
Licenses and Permits	587,130	587,130	886,385	299,255
Intergovernmental	161,669	220,023	301,171	81,148
Charges for Services	2,119,067	2,229,929	2,521,626	291,697
Fines and Forfeitures	75,200	75,200	70,774	(4,426)
Interest and Other Earnings	46,000	46,000	70,892	24,892
Miscellaneous	78,121	84,855	92,473	7,618
Total Revenues	10,349,526	10,525,476	11,745,290	1,219,814
Expenditures				
Current:				
General Government	3,308,856	3,334,273	3,108,256	226,016
Security of Persons & Property	3,113,629	3,139,479	3,120,582	18,897
Utilities and Environment	513,632	513,632	532,379	(18,747)
Transportation	537,785	651,834	651,482	352
Economic Environment	925,552	981,967	898,672	83,295
Mental and Physical Health	14,864	70,718	131,162	(60,444)
Culture and Recreation	1,131,830	1,139,274	1,128,766	10,508
Total Expenditures	9,546,148	9,831,177	9,571,301	259,876
Excess of Revenues Over Expenditures	803,378	694,299	2,173,989	1,479,690
Other Financing Sources (Uses)				
Transfers in	37,000	42,000	5,000	(37,000)
Transfers out	(1,775,987)	(2,078,487)	(2,078,487)	-
Sale of Capital Assets	-	-	7,649	7,649
Insurance Recoveries	-	-	5,206	5,206
Total Other Financing Sources (Uses)	(1,738,987)	(2,036,487)	(2,060,632)	(24,145)
Net Change in Fund Balance	(935,609)	(1,342,188)	113,356	1,455,544
Fund Balance Beginning of Year	2,001,759	3,162,550	3,175,241	12,691
Fund Balance End of Year	\$ 1,066,150	\$ 1,820,362	\$ 3,288,597	\$ 1,468,235

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

**STATEMENT OF NET POSITION
PROPRIETARY FUNDS
AS OF DECEMBER 31, 2016**

	Business-type Activities Enterprise Funds				
	Water	Sewer	Solid Waste	Storm Drain	Total
Assets					
Current Assets:					
Cash and Cash Equivalents	\$ 475,851	\$ 285,068	\$ 395,321	\$ 196,908	\$ 1,353,148
Investments	4,149,177	7,405,172	1,456,624	1,264,205	14,275,178
Accounts Receivable	131,834	311,612	169,088	144,025	756,559
Due from Other Governments	-	-	-	15,923	15,923
Inventories	45,771	6,468	-	-	52,239
Prepaid	500	500	250	250	1,500
Total Current Assets	4,803,132	8,008,820	2,021,284	1,621,311	16,454,547
Noncurrent Assets:					
Restricted cash, cash equivalents, and invests.:					
Revenue bond covenant investment	68,948	244,452	-	-	313,400
Capital Assets Not Being Depreciated:					
Land	331,186	414,874	191,213	1,223,217	2,160,490
Construction in Progress	515,366	335,575	22	314,530	1,165,493
Capital Assets:					
Buildings and Structures	272,226	441,491	876,953	1,316,700	2,907,371
Intangibles	106,678	114,209	12,229	188,845	421,961
Other Improvements	19,720,168	29,229,737	9,098	14,960,241	63,919,244
Machinery and Equipment	599,562	1,091,997	933,018	358,925	2,983,502
Less: Accumulated Depreciation	(5,969,827)	(9,960,219)	(696,770)	(3,820,926)	(20,447,742)
Total Noncurrent Assets	15,644,308	21,912,116	1,325,763	14,541,532	53,423,719
Total Assets	20,447,440	29,920,936	3,347,047	16,162,842	69,878,266
Deferred Outflows of Resources					
Deferred Amount of Refunding	3,725	13,208	-	-	16,933
Deferred Outflow - Pension	67,467	43,402	48,345	72,784	231,998
Total Deferred Outflows of Resources	71,193	56,609	48,345	72,784	248,931
Liabilities					
Current Liabilities					
Accounts payable	52,835	106,232	85,647	38,638	283,352
Accrued interest payable	7,487	30,885	-	-	38,372
Rev. bonds payable	104,500	370,500	-	-	475,000
Unearned Revenue	3,541	168	202	164	4,076
Custodial	6,464	68,088	-	-	74,552
Compensated Absences	5,159	4,532	4,984	4,501	19,176
Total Current Liabilities	179,986	580,405	90,833	43,303	894,527
Noncurrent Liabilities:					
Rev. bonds payable	-	-	-	-	-
Compensated absences	46,430	40,790	44,852	40,512	172,584
Pension Obligation	361,582	232,340	259,111	391,121	1,244,154
Total Noncurrent Liabilities	408,013	273,130	303,963	431,633	1,416,738
Total Liabilities	587,999	853,535	394,796	474,936	2,311,265
Deferred Inflows of Resources					
Deferred Inflow - Pension	6,513	4,185	4,667	7,045	22,411
Total Deferred Inflows of Resources	6,513	4,185	4,667	7,045	22,411
Net Position					
Net Investment in capital assets	15,474,585	21,310,372	1,325,763	14,541,532	52,652,252
Restricted for debt service	68,948	244,452	-	-	313,400
Unrestricted	4,380,588	7,565,002	1,670,165	1,212,114	14,827,869
Total Net Position	\$ 19,924,121	\$ 29,119,826	\$ 2,995,928	\$ 15,753,645	\$ 67,793,521

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

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016**

	Business-type Activities Enterprise Funds				
	Water	Sewer	Solid Waste	Storm Drain	Total
Operating Revenues:					
Charges for Services	\$ 1,746,438	\$ 3,415,903	\$ 1,772,076	\$ 1,606,666	\$ 8,541,082
Other Operating Revenues	110,537	44,611	21,322	15,259	191,729
Total Operating Revenues	1,856,975	3,460,513	1,793,398	1,621,925	8,732,811
Operating Expenses:					
Depreciation	443,147	686,073	61,274	460,426	1,650,920
Salaries and Wages	329,849	294,854	255,865	392,157	1,272,723
Personnel Benefits	149,414	127,189	113,037	199,605	589,245
Supplies	132,077	61,589	73,936	24,456	292,057
Services	399,450	565,024	681,554	311,836	1,957,863
Intergovernmental Services and Payments	229,746	919,664	573,985	287,824	2,011,218
Total Operating Expenses	1,683,682	2,654,393	1,759,650	1,676,304	7,774,028
Operating Income (Loss)	173,293	806,120	33,748	(54,379)	958,783
Nonoperating Revenues (Expenses):					
Interest and Other Earnings	12,602	37,275	3,316	1,587	54,780
Interest Expense	(9,065)	(32,139)	-	-	(41,204)
State Grants	-	-	-	86,869	86,869
Federal Grants	-	-	-	127,142	127,142
Insurance Recoveries	117	9,464	117	146	9,843
Proceeds from sale of Capital Assets	-	922	-	-	922
Total Nonoperating Revenue (Expenses)	3,654	15,522	3,433	215,744	238,353
Income (loss) Before Contributions	176,947	821,643	37,181	161,366	1,197,136
Capital Contributions	1,035,502	773,422	-	287,647	2,096,571
Change in Net Position	1,212,449	1,595,064	37,181	449,012	3,293,707
Total Net Position Beginning of Year	18,711,671	27,524,761	2,958,747	15,304,633	64,499,813
Total Net Position End of Year	\$ 19,924,121	\$ 29,119,826	\$ 2,995,928	\$ 15,753,645	\$ 67,793,521

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

**STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016**

Page 1 of 2

Business-type Activities Enterprise Funds					
	Water	Sewer	Solid Waste	Storm Drain	Total
Cash Flows from Operating Activities					
Receipts from customers and users	\$ 1,856,358	\$ 3,393,577	\$ 1,782,631	\$ 1,679,984	\$ 8,712,551
Payments for interfund services provided	(229,746)	(919,664)	(573,985)	(287,824)	(2,011,218)
Payments to suppliers	(546,371)	(626,235)	(767,452)	(473,820)	(2,413,878)
Payments to employees	(479,459)	(433,135)	(366,382)	(556,895)	(1,835,871)
Net cash provided (used) by operating activities	600,782	1,414,543	74,812	361,445	2,451,583
Cash Flows From Noncapital Financing Activities					
State & Federal Grants	-	-	-	214,011	214,011
Proceeds from Insurance Claims	117	9,464	117	146	9,843
Net cash provided (used) by noncapital and related financing activities	117	9,464	117	214,157	223,854
Cash Flows from Capital and Related Financing Activities					
Proceeds from Capital Debt					
Capital contributions	732,234	653,468	-	39,039	1,424,742
Purchase of capital assets	(121,392)	(500,617)	-	(30,100)	(652,109)
Acquisition and construction of capital assets	(636,433)	(1,092,198)	(34,639)	(492,930)	(2,256,200)
Principal paid on capital debt	(100,540)	(596,987)	-	-	(697,527)
Interest paid on capital debt	(7,074)	(25,080)	-	-	(32,154)
Net cash provided (used) by capital and related financing activities	(133,205)	(1,561,413)	(34,639)	(483,991)	(2,213,249)
Cash Flows from Investing Activities					
Proceeds from sales and maturities of investments	2,646,722	5,446,698	1,883,957	452,141	10,429,518
Purchase of investment	(3,106,765)	(5,235,169)	(1,916,526)	(851,744)	(11,110,203)
Interest and dividends received	12,602	37,275	3,316	1,587	54,780
Net cash used by investing activities	(447,441)	248,805	(29,253)	(398,016)	(625,905)
Net increase in cash and cash equivalents	20,254	111,398	11,037	(306,405)	(163,716)
Cash and cash equivalents Beginning of Year	455,597	173,670	384,284	503,313	1,516,864
Cash and cash equivalents End of Year	\$ 475,851	\$ 285,068	\$ 395,321	\$ 196,908	\$ 1,353,148

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

**STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016**

Page 2 of 2

	Business-type Activities Enterprise Funds				
	Water	Sewer	Solid Waste	Storm Drain	Total
Reconciliation of operating income to net cash provided (used) by operating activities:					
Operating Income (Loss)	\$ 173,293	\$ 806,120	\$ 33,748	\$ (54,379)	\$ 958,783
Adjustments to reconcile operating income to net cash provided (used) by operating activities					
Depreciation	443,147	686,073	61,274	460,426	1,650,920
(Increase) decrease in accounts receivable	(1,873)	(22,462)	(10,756)	58,046	22,956
(Increase) decrease in inventories	(14,845)	521	-	-	(14,323)
Increase (decrease) in accounts payable	(6,339)	(7,885)	(11,979)	(130,654)	(156,857)
Increase (decrease) in Custodial Funds	1,200	(44,623)	-	-	(43,423)
Increase (decrease) in Pension Funds	(2,018)	(7,149)	(1,124)	20,797	10,506
Increase (decrease) in compensated absences payable	8,217	3,947	3,649	7,209	23,021
Total Adjustments	427,489	608,423	41,064	415,824	1,492,800
Net Cash Provided By Operating Activities	\$ 600,782	\$ 1,414,543	\$ 74,812	\$ 361,445	\$ 2,451,583
Noncash investing, financing and capital activities					
Capital Contributions by Developers	303,268	120,876		248,608	672,751
Investment Earnings Unrealized	(2,983)	(375)	(3,586)	(3,661)	(10,605)

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

**STATEMENT OF FIDUCIARY NET POSITION
AGENCY FUND
DECEMBER 31, 2016**

Agency Fund	
Assets	
Cash and cash equivalents	\$ 90,486
Investments	92,242
Accounts Receivable	53
Total Assets	182,781
Deferred Outflows of Resources	
	-
Liabilities	
Accounts Payable and accrued expenses	4,136
Retainage Payable	72,813
Custodial funds	105,832
Total Liabilities	182,781
Deferred Inflows of Resources	
	-
Net Position	\$ -

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 Poulsbo have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The significant accounting policies are described below.

For the reporting year ended December 31, 2016, the City has implemented the following new standards issued by the Governmental Accounting Standards Board (GASB):

Statement No. 72 Fair Value Measurement and Application. This statement defines fair value and provides guidance for determining a fair value measurement for financial reporting purposes.

Statement No. 79 Certain External Investment Pools and Pool Participants. This statement establishes criteria for an external investment pool to qualify for making the election to measure all its investments at amortized cost for financial reporting purposes. Certain provisions of Statement 79 related to portfolio quality, custodial credit risk, and shadow pricing are not effective until fiscal year 2017.

A. REPORTING ENTITY

The City of Poulsbo, located in Kitsap County, Washington, was incorporated in 1908. It operates under the laws of the State of Washington applicable to code cities with a Mayor-Council form of government. A full-time mayor and seven council members, all elected at large for four-year terms, administer the City. The City provides what are considered general government services including public safety, streets, parks and recreation, planning and zoning, permits and inspection, general administrative, water, sanitary sewer collection, solid waste collection and storm drainage services.

The City's Comprehensive Annual Financial Report (CAFR) includes all funds, agencies and boards controlled by, or dependent on, the City. Control by or dependence on the City was determined on the basis of financial accountability, budget adoption, taxing authority, outstanding debt service secured by revenues or general obligations of the City, obligations of the City to finance any deficits that may occur, or receipt of significant subsidies from the City.

B. BASIS OF PRESENTATION-GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

The City's basic financial statements consist of government-wide statements, including a statement of net position and a statement of activities, and fund financial statements, which provide a more detailed level of financial information.

The government-wide financial statements 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* presents changes in the government-wide net position by function or program. It focuses on expenses rather than expenditures and shows to what extent direct program revenues offset expenses for a given function. Our policy is to allocate indirect costs to a specific function. Program revenues include: 1) charges to customers or applicants who purchase, use or directly benefit from a program; and 2) grants and contributions that are restricted for the purpose of operational or capital use for a particular program. Taxes and other items such as investment interest, not restricted for specific programs, are reported on the statement as general revenues. The comparison of direct expenses with program revenues identifies the extent to which each function is self-financing, or draws from the general revenues of the City.

The *Statement of Net Position* presents the financial condition of the City's governmental and business-type activities at year-end. It reports all financial and capital assets including infrastructure and all liabilities, including current and long-term.

During the year, the City segregates transactions related to certain City functions or activities into separate funds in order to aid financial management and to demonstrate legal compliance. Fund financial statements are designed to present financial information of the City at this more detailed level and include statements for governmental, proprietary, and fiduciary funds, even though the fiduciary funds are excluded from the government-wide statements. In the basic financial statements, the governmental and enterprise fund financial statements focus on major funds. Major individual government 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 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. 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 assessment 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 Fund* is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The *Street Reserve Fund* was established to make improvements to the transportation system. Funding is from State and Federal grants and operating transfers.

The City reports the following major proprietary funds:

The *Water Fund* accounts for providing water services. Its revenues are mostly received from service charges and system connection charges. Expenses are for maintenance and operations of a water supply, storage and distribution system. This fund also reflects the operation of revenue bonds outstanding, the funds available for redemption of bonds, cumulative reserve and construction funds.

The *Sewer Fund* accounts for providing sewer services. Its revenues are mostly received from service charges and system connection charges. Expenses are for maintenance and extensions of drainage, sewer service facilities, maintaining sewer collection and transmission systems. This fund also reflects the operation of revenue bonds outstanding, the funds available for redemption of bonds, cumulative reserve and construction funds.

The *Solid Waste Fund* accounts for operations of the collection and transportation of solid waste. Its revenues are received from service charges. Expenses are made up of the cost of collection and disposal of solid waste.

The *Storm Drain Fund* accounts for the operation, construction, and maintenance of the storm water management system.

Additionally, the City reports the following fund types:

Special Revenue Funds account for the proceeds of specific revenue sources to finance specific activities as required by law or administration regulation. Their revenues are earmarked to finance certain activities or functions.

Debt Service Funds account for resources accumulated and payment made for principal and interest on the general government debt except those required to be accounted for in another fund.

Capital Project Funds account for the acquisition or development of capital facilities for governmental activities. The major sources of revenue are from proceeds from general obligation bonds, grants, and contributions from other funds.

Agency funds account for assets held by the City as an agent for private individuals or other governments. Agency funds are custodial in nature (assets equal liabilities) and do not involve the measurement of the results of operation.

Permanent Funds account for resources that are legally restricted to the extent that only the earnings, and not the principal, may be used for specific purposes that support the City's programs and benefit the City and its citizens. The City has one *Permanent fund*, the Bernice Borgen Beautification Fund. The fund accounts for a trust established from Ms. Borgen's estate of an original donation of \$90,002 in 2000 and an additional contribution of \$1,014 in 2002. Only the interest earned on this donation can be used for beautification of the City. The City Council has the authority to determine what these expenditures will be. As of year-end, funds available for expenditure are \$1,850. This amount also represents the designated unrealized investment earnings.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Direct expenses of the functional categories are included in the government-wide statement of activities while indirect expense allocations are eliminated (\$1,280,660 in 2016) Exceptions to this general rule are payments-in-lieu of taxes and other charges between the government's utility 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 or applicants for goods, services or privileges provided, 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. Likewise, general revenues include all taxes.

Proprietary funds distinguish operating revenues and expenses from non-operating 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 proprietary funds are the charges for goods and services. Operating expenses for enterprise funds and internal service funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenue and expenses not meeting this definition are reported as non-operating revenues and expenses.

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

D. ASSETS, LIABILITIES, AND NET POSITION OR EQUITY

1. Cash and Investments

It is the City's policy to invest all temporary cash surpluses. At December 31, 2016, the City was holding \$ 2,688,583 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.

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.

The City reports its deposit and investment risk disclosures in accordance with GASB 40 (see note 3).

All investments are stated at fair value as of December 31, 2016.

2. Receivables

The City of Poulsbo recognizes receivables in its various funds using the accounting basis required for that fund. These receivables are as follows:

Property Taxes

The City's annual property tax levy is billed and collected by Kitsap County. Taxes collected by the County, but not remitted to the City by year-end, are reported as receivables. Taxes are levied and become a lien on the first day of the calendar year. When property taxes become three years' delinquent, the County is required by State statute to foreclose on the property.

Accounts Receivable

Customer Accounts Receivable consist of amounts owed by private individuals or organizations for goods and services provided. Uncollectable amounts are considered immaterial and the direct write-off method is used.

Special Assessments

Special assessments are recorded when levied. Special assessments receivable consists of current and delinquent assessments and related interest and penalties. Deferred assessments consist of unbilled special assessments that are liens against the property benefited.

3. Interfund Transactions

During the course of normal operations, the City has numerous transactions between City funds. Interfund transactions such as buying goods and services are recorded as revenues and expenditures. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the financial statements. Transfers between funds are included as "other financing sources or uses." Interfund loans, when applicable, are recorded as receivables in the lending fund and payables in the borrowing fund. The City had no interfund loans in 2016.

The City levies a utility tax on the revenues of its own enterprise funds (Water/Sewer, Solid Waste, and Storm Drain). On the fund statements, these taxes are recorded as an expense in enterprise funds, and as revenue in the General Fund.

Other interfund transfers at December 31, 2016 were as follows:

Transfers Out:				
Transfers In:	Street		Non-Major	Total
	General Fund	Reserve Fund	Gov'l	
General Fund	-	5,000	-	5,000
Street Reserve Fund	500,500	-	275,000	775,500
Non-Major Gov'l Funds	1,577,987	-	544,424	2,122,411
Total Transfers	\$ 2,078,487	\$ 5,000	\$ 819,424	\$ 2,902,911

4. Amounts Due to and from Other Governmental Units

These receivables reflect measurable and available intergovernmental charges for services rendered by, or to, the City for, or by, another government unit.

5. Inventories

Inventories are defined as assets which may be held for internal consumption or for resale. On the government-wide financial statements, inventories are presented at cost on a first-in, first-out basis and are recorded as expenditures when consumed rather than when purchased. On the fund financial statements, the City uses the following policies in valuing and recording inventory items that are used:

- a. Inventories are valued at cost using the average cost method. The costs of inventories in the governmental fund types are recorded as expenditures when consumed rather than when purchased.
- b. In proprietary funds, a perpetual inventory is maintained in which the cost is capitalized when inventory items are purchased, and expensed when the item is consumed. The average cost method of valuation which approximates market is used to value the inventory. A physical inventory is taken at year-end.

6. Restricted Assets

Restricted Assets include resources reserved for construction and debt service in enterprise funds. Certain proceeds of the enterprise fund revenue bonds, as well as certain resources set aside for their repayment are classified as restricted assets on the balance sheet because they may be maintained in separate accounts and their use is limited by applicable bond covenants. The amount listed in the governmental funds represents the permanent trust fund.

7. Note Receivable

Note Receivable consists of the amount owed to the City from the Poulsbo Historical Society for a portion of real estate sold to house the Poulsbo Historical Museum.

8. Capital Assets

The City defines a capital asset as assets with an initial, individual cost of \$5,000 or greater and an estimated life in excess of three years. Capital assets include property, equipment, and infrastructure (i.e. roads, bridges, sidewalks, and similar items).

In the fund financial statements, these assets are accounted for and reported based on the measurement focus of the fund. In other words, in the governmental funds, acquired capital assets are accounted for as expenditures when the asset is purchased. In the proprietary funds, the expense is capitalized and the current year's depreciation is reported as the expense.

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated assets are valued at estimated fair market value at time of acquisition. Where historical cost is not known, assets are recorded at estimated historical costs. The City maintains a capitalization threshold of \$5,000. The City's infrastructure consists of roads, bridges, storm sewers, and water and sewer distribution and collection systems. Improvements are capitalized but the costs of normal maintenance and repairs, not adding to the value of the asset or materially extending an asset's life, are not. Property, plant, and equipment of the primary government are depreciated using the straight-line method and reported in the government-wide statements and proprietary funds using the following estimate useful lives:

	<u>Estimated Useful Life in Years</u>
Buildings and Improvements	10-100
Equipment	3-25
Roads-collectors and residential	30
Water and Sewer distribution and collection systems	40

9. Compensated Absences

It is the City's policy to permit employees to accumulate earned, but unused, vacation leave up to a maximum of 240 hours. Vacation pay is payable to the maximum upon resignation, retirement, or the death of an employee. Compensatory time is accruable to a maximum of 80 hours.

Sick leave accumulation is unlimited, but the annual accrual could be elected to be cashed out for 50% once a 1,000-hour balance is reached. All sick leave is payable upon resignation, retirement or the death of an employee for 50% up to a maximum balance of 1,200 hours.

In accordance with GASB Statement No. 16, the City accrues vacation pay and no liability is recorded for non-vesting accumulating rights to receive sick pay benefits. However, a liability is recognized for that portion of the accumulating sick leave benefits that it is estimated will be taken as termination leave prior to resignation. This provides for the termination pay for eligible employee's vacation and 50% percent of their sick leave to a maximum of 1,200 hours accrued.

The entire compensated absence liability is reported on the government-wide financial statements. In the proprietary funds, the entire amount of compensated absences is reported as a fund liability.

In prior years, the General Fund and proprietary funds have typically been used to liquidate these liabilities.

10. Pensions and OPEB

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of all state sponsored pension plans and additions to/deductions from those plans' fiduciary net position have been determined on the same basis as they are reported by the Washington State Department of Retirement Systems. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Lifetime full medical coverage is provided to uniformed Police and Fire personnel who became members of the Law Enforcement Officers and Fire Fighters (LEOFF 1) retirement system prior to October 1, 1977. A liability for the accumulated unfunded actuarially required contribution is reported in the Statement of Net Position. The actual medical costs are reported as expenditures in the year they are incurred.

11. Custodial Accounts

These accounts reflect the liability for net monetary assets being held by the City in its trustee or agency capacity.

12. Accrued Liabilities and Long-Term Obligations

All payables, accrued liabilities and long-term obligations are reported in the government-wide financial statements. Also, all payables, accrued liabilities and long-term obligations payable from proprietary funds are reported on the proprietary fund financial statements.

In general, governmental fund payables and accrued liabilities, those once incurred, are paid in a timely manner and in full from current financial resources, are reported as obligations of the funds. When due, bonds, capital leases, and long-term loans are recognized as a liability on the governmental fund financial statements.

13. Unearned Revenues

Unearned revenues consist of receivables for charges for services to be recognized in the following year or funds paid in advance by customers for services to be recognized in the following year.

14. Fund Balance Classification

In the fund financial statements, governmental funds report fund balances based on the extent to which the City is bound to observe constraints on the use of the governmental funds' resources. Fund balances are classified in the following manner:

- *Nonspendable* - includes amounts that are either 1) not in spendable form, or 2) legally or contractually required to be maintained intact. Inventories, prepaid items, and permanent trusts are classified as nonspendable fund balances.
- *Restricted* - includes amounts which are constrained for specific purposes that are 1) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments, or 2) imposed by law through enabling legislation.

- *Committed* - includes amounts that can be used for specific purposes with constraints imposed by formal action of the highest level of decision-making authority. The authorization specifying the purposes for which committed funds can be used should have the consent of both the legislative and executive branches of government. The City operates under a Mayor-Council form of government. As Executive Officer, the Mayor supervises the administrative process of the City and works with the City Council. The City Council enacts ordinances and resolutions that may impose, modify or rescind fund balance commitments. (The City does not have any committed balances)
- *Assigned* - includes amounts that are intended to be used for specific purposes, but are neither restricted nor committed. The authority for assignment of funds is not required to be the government's highest level of decision making authority. Furthermore, the constraints imposed on the use of assigned amounts are more easily removed or modified than those imposed on committed fund balances. The City Council may authorize executive officers to assign fund balances for specific purposes through Council files, ordinances and resolutions.
- *Unassigned* - includes amounts that are not assigned to other funds and do not meet the criteria for being classified as restricted, committed, or assigned. Fund balances that can be utilized for economic stabilization, emergencies and contingencies that do not qualify as restricted or committed are reported as unassigned.

The primary flow assumption utilized by the City is: 1) Restricted, 2) Committed, 3) Assigned, 4) Unassigned. However, prior to the commencement of any project, the flow assumption is reviewed to ensure that the proper resources are being used. The following is the breakdown:

	Nonspendable Purposes	Restricted Purposes	Assigned Purposes	Unassigned Purposes	Totals
<u>General Fund</u>					
General Government	\$ 7,597	\$ -	\$ -	\$ 1,106,077	\$ 1,113,674
Stabilization Fund			1,949,924		1,949,924
Legal Reserves			225,000		225,000
Subtotals, General Fund	7,597	-	2,174,924	1,106,077	3,288,597
<u>Street Reserve Fund</u>					
Transportation Improvements			1,145,868		1,145,868
Subtotals, City Street Fund	-	-	1,145,868	-	1,145,868
<u>Other Governmental Funds</u>					
Transportation Improvements		1,115,819	185,897		1,301,716
Parks Improvements		299,656	210,355		510,011
Cemetery Improvements			54,936		54,936
Capital Equipment			566,767		566,767
Capital Improvements		607,125			607,125
Drug Enforcement		65,362			65,362
Criminal Justice		94,946	24,576		119,522
Promote Downtown Businesses		48,360			48,360
Promoting Tourism		76,460			76,460
City Beautification	91,016	1,850			92,866
Debt Service		16,246			16,246
Subtotals, Other Governmental Funds	91,016	2,325,825	1,042,531	-	3,459,372
Totals	\$ 98,613	\$ 2,325,825	\$ 4,363,323	\$ 1,106,077	\$ 7,893,837

15. Minimum Fund Balances

The City has formally adopted a minimum fund balance policy because it is the belief adequate reserve levels are a necessary component of the City's overall financial management strategy and a key factor in external agencies' measurement of the City's financial strength.

General Fund

It will be the policy of the city to maintain a General Fund Reserve at a level of at least equal to twelve percent (12%) of the total General Fund budgeted operating revenue, excluding the beginning fund balance and identified one-

time revenue. This shall be in addition to the maintenance of two months operating cash within the General Fund itself.

These operating reserves are maintained to:

- address temporary revenue shortfalls;
- payment of approved expenditures due to cash flow shortage;
- reserves for expenditures deemed necessary by the Mayor and City Council; and
- temporary short-term interfund loans.

Annual contribution will be budgeted from General Fund resources as available to maintain the target reserve level.

Capital Reserve Funds

The city shall maintain capital reserve funds to provide funding for the six years Capital Improvement Plan, less proprietary fund projects. The use of any funds within the Capital Improvement Funds shall be approved by the City Council.

Contributions to the capital reserve funds will be made as per the budget recommendations set by the City Council.

All expenditures drawn from reserve accounts shall require prior Council super-majority approval unless previously specifically authorized by the City Council for expenditure in the annual budget

NOTE 2: STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. BUDGETARY INFORMATION

In 2016, the City prepared an annual budget in accordance with the Revised Code of Washington (RCW) 35.33 that is on a basis consistent with accounting principles generally accepted in the United States of America. All funds except custodial agency funds and permanent funds are budgeted to the fund level. Annual appropriated budgets are adopted for all funds and lapse at the end of each year. However, some of the special revenue and capital funds may carry forward budgeted amounts beyond the year for completion of certain projects.

Budget amounts shown in the basic financial statements include the original budget amount and all appropriation transfers and adjustments approved by the City Council, as required. The Mayor is authorized to approve intra-fund budget transfers from one department to another or between line items of the same department. Only the City Council has the authority to increase a given fund's budget. This is executed by City ordinance.

In addition to authorizing the budget, the City Council approves the Capital Improvement Plan. This is a five-year plan for capital project expenditures and anticipated revenue sources. Expenditures and revenue for these projects are budgeted in the Capital Project Funds.

The calendar below outlines the process for preparing, reviewing and adopting the annual budget:

MAY – JULY

- Capital Improvement team begins process to update Capital Improvement Plan (CIP)

JULY – AUGUST

- Council meets to review and set budgetary policies
- Budgetary packets with instruction and initial allocations provided
- Revenues are reviewed and forecasted
- Departments meet with Council committees to finalize recommended budget proposals
- Department budget proposals submitted to Finance Department

SEPTEMBER – DECEMBER

- Budget submission reviewed with Mayor
- Mayor's proposed preliminary budget prepared and distributed to Council

- Public Hearings held
- CIP presented to Council
- Additional funding & New Program requests reviewed
- Property tax levy set
- Department budgets presented to full Council for review and discussion
- Preliminary budget with all changed prepared and distributed

DECEMBER

- Final review and adoption of budget

The final budget, as adopted, is published within the first three months of the new budget year and distributed to various governmental agencies as well as to the local library to be available to the citizens and all interested members of the public and is published on the City's website; www.cityofpoulsbo.com.

In 2017, the City has taken a progressive step to implement its first biennial budget.

B. BUDGETARY COMPLIANCE

In 2016, there were no City funds that reported actual expenditures above budgeted appropriations. Though specific line items may be exceeded, no fund's appropriations can be legally exceeded. It should be noted, however, that the "Statement of Revenues, Expenditures and Changes in Fund Balances" including the comparisons of "Budget and Actual," could be misinterpreted due to its format and, by so doing, lead one to believe that budgeted expenditures have been exceeded. The City budgets not only expenditures but also "Beginning Fund Balances" so as to maintain a budget in balance with receipts and disbursements. By increasing expenditure appropriations by the budget values for these items, it can be seen that no City fund has exceeded its legally established appropriation. All budgets lapse at year-end.

Encumbrance accounting is used in all city funds for budgetary control only. Encumbrances (e.g., purchase orders) lapse at year end and, if necessary, are re-appropriated in the following year.

NOTE 3: DEPOSITS AND INVESTMENTS

A. Deposits

Custodial Credit Risk

Custodial credit risk is the risk associated with the failure of a depository financial institution. In the event of a depository financial institution's failure, it is the risk that the city would not be able to recover its deposits or collateralized securities that are in the possession of the outside parties.

The City's bank deposits and certificates of deposit are entirely covered by the Federal Depository Insurance Corporation (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the State of Washington Public Deposit Protection Commission (WPDPC). The FDIC insures the first \$250,000 of the City's deposits. The deposit balances over \$250,000 are collateralized by the WPDPC.

As of December 31, 2016, the carrying amount of the City's change funds, petty cash, and bank demand deposit accounts with financial institutions was the following:

Cash	
FDIC or PDPC insured bank deposits	\$ 3,283,448
In-transit items	(414,787)
Custodial funds held in agency funds	(182,728)
Petty Cash on hand	2,650
Total Cash	<u>2,688,583</u>

B. Investments

The City pools cash from all sources and all funds, and invests its pooled idle cash according to the State of Washington's law and the City's Investment Policy approved by City Council. The basic principles underlying the City's investment philosophy are to ensure the safety of public funds, ensure sufficient funds are available to meet current expenditures, and achieve a reasonable rate of return on investments. Qualifying investments include obligations of the United States government, Treasury and Agency securities, bankers' acceptances, certificates of deposit and repurchase agreements.

Investments measured at Amortized Cost

The City's deposits with the Washington State Local Government Investment Pool (LGIP) are managed by the Washington State Office of the Treasurer. The LGIP is comparable to a Rule 2a7-pool recognized by the Securities and Exchange Commission. A 2a7-like-pool is an external investment pool that is not registered with the SEC as an investment company but nevertheless has a policy that it will, and does, operate in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940. Rule 2a7 allows SEC-registered mutual funds to use amortized cost, which approximates fair value, to report net assets and compute share prices.

As of December 31, 2016 the City held the following investments at amortized Cost:

Washington State Local Government Inv. Pool	\$ 4,135,385
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Investments measured at Fair Value

The City categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure fair value of the assets. Level 1 inputs are quoted prices in an active market for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are significant unobservable inputs. All the investments are measured using level 1 inputs.

The following is a summary of the fair value investments of the City as of December 31, 2016:

Investments	Valuation Measurement Method	Fair Value 12/31/16	Maturities		Total
			Less Than One Year	One to Three Years	
US agency securities					
US Treasury Bills, Notes & Bonds	Level 1	\$ 8,716,415	\$ 5,982,993	\$ 2,733,423	\$ 8,716,415
Federal Farm Credit Bank	Level 1	746,327		746,327	746,327
Federal Home Loan Bank	Level 1	2,987,019	749,757	2,237,262	2,987,019
Federal Home Loan Mortgage Corp	Level 1	2,095,550	599,978	1,495,572	2,095,550
Federal National Mortgage Association	Level 1	3,625,862	1,000,647	2,625,215	3,625,862
Total Investments		\$ 18,171,173	\$ 8,333,374	\$ 9,837,799	\$ 18,171,173

Custodial Credit Risk

For investments, this is the risk that in the event of a failure of the counterparty to an investment transaction (typically a broker-dealer) the City would not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The City limits its exposure by only purchasing insured or registered investments, and by the control of a third-party custodian to hold the securities for safekeeping.

Interest Rate Risk

As a means of limiting its exposure to interest rate risk, the City diversifies its investments by security type and institution, and limits holdings in any one type of investment with any one issuer. The City coordinates its investment maturities to closely match cash flow needs and restricts the maximum investment term to less than five year from the purchase date.

Credit Risk

State law and City policy limit investment to those authorized by the State Statute including commercial paper,

bankers' acceptances, and corporate bonds. It is the City's policy to limit its credit risk by only investing in commercial paper or bankers' acceptances with a credit rating of A1 or P1.

Concentration of credit risk

In accordance with its investment policy, the City will diversify its investments by security type and institution. With the exception of U.S. Treasury securities and authorized pools, no more than twenty-five percent of the City's total investment portfolios will be invested in a single security type or with a single financial institution.

Investment Type	Fair Value	Maturity Duration	% of Portfolio	S&P Rating
Investments				
US agency securities				
US Treasury Bills, Notes & Bonds	\$ 8,716,415	0.84	39%	AA+
Federal Farm Credit Bank	\$ 746,327	1.74	3%	AA+
Federal Home Loan Bank	2,987,019	1.38	13%	AA+
Federal Home Loan Mortgage Corp	2,095,550	0.83	9%	AA+
Federal National Mortgage Association	3,625,862	1.02	16%	AA+
Washington State Local Government Inv. Pool	4,135,385		19%	
Total Investments	22,306,558	1.16	100%	

NOTE 4: PROPERTY TAXES

The City may levy up to \$3.60 per \$1,000 of assessed valuation for general governmental services, however, that amount is reduced by the Kitsap County Library and Kitsap County Fire District 18 annexations. The Library District may levy up to a maximum of \$.50 and Fire District 18 may levy up to a maximum of \$1.50 per \$1,000 of assessed valuation.

This amount may also be reduced subject to the following limitations:

- Washington State RCW 84.55.010 limits the growth of regular property taxes to one percent per year or IPD, whichever is less, after adjustments for new construction and annexations, unless an increase greater than this limit is approved by the voters. If the assessed valuation increases by more than one percent due to revaluation, the levy rate will be decreased.
- The Washington State Constitution limits the total regular property taxes to one percent of assessed valuation, or \$10 per \$1,000 of the market value of a property. If the taxes of all districts exceed this amount, each is proportionately reduced until the total is at or below the one percent limit.

For property taxes to be collected in 2016, the City's levy for general governmental services was \$1.685960 per \$1,000 on the assessed valuation of \$1,346,103,503 for a total of \$2,269,477.

The Kitsap County Treasurer acts as agent to collect property taxes levied in the county for all taxing authorities. Collections are distributed after the end of each month.

Property Tax Calendar

Jan 1	Taxes are levied and become an enforceable lien against properties
Feb 14	Tax statements are mailed
April 30	First of two equal installment payments is due
May 31	Assessed value of property is established at 100% of market value for next year's levy
Oct 31	Second installment is due

During the year, property tax revenues are recognized when cash is collected. At year-end, property tax revenues are recognized for collections to be distributed by the County Treasurer in January. No allowance for uncollectible taxes is established because delinquent taxes are considered fully collectible.

NOTE 5: CAPITAL ASSETS

All reported capital assets of the City are depreciated. Improvements are depreciated over the remaining useful lives of the related capital assets. Useful lives for infrastructure were estimated based on the City's historical records of necessary improvements and replacement.

Capital asset activity for the primary government for the year ended December 31, 2016, was as follows:

	BEGINNING BALANCE	INCREASES	DECREASES	ENDING BALANCE
Governmental-Type Activities				
Capital assets, not being depreciated:				
Land	\$ 10,819,687	\$ 552,033	\$ -	\$ 11,371,720
Intangible - Right of Way	19,839,139	-	-	19,839,139
Construction Work in Progress	494,178	993,281	(281,672)	1,205,786
Total capital assets not being depreciated	31,153,004	1,545,314	(281,672)	32,416,645
Capital assets, being depreciated:				
Buildings	17,115,446	-	-	17,115,446
Other Improvements	14,826,943	700,088	-	15,527,031
Machinery and Equipment	3,023,447	208,649	(53,128)	3,178,969
Intangible	647,486	-	-	647,486
Infrastructure	31,352,627	-	-	31,352,627
Total capital assets being depreciated	66,965,949	908,738	(53,128)	67,821,559
Less accumulated depreciation for:				
Buildings	(3,810,635)	(348,227)	-	(4,158,861)
Other Improvements	(4,376,074)	(935,105)	-	(5,311,179)
Machinery and Equipment	(2,353,732)	(162,077)	52,928	(2,462,881)
Intangible	(534,636)	(22,516)	-	(557,152)
Infrastructure	(9,570,769)	(630,832)	-	(10,201,602)
Total accumulated depreciation	(20,645,846)	(2,098,757)	52,928	(22,691,675)
Total capital assets, being depreciated, net	46,320,104	(1,190,020)	(200)	45,129,884
Governmental activity capital assets, net	\$ 77,473,108	\$ 355,294	\$ (281,872)	\$ 77,546,529

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

Governmental activities:

General Government	\$ 312,975
Security of Persons and Property	62,244
Utilities and Environment	2,889
Transportation	1,482,536
Economic Environment	-
Culture and Recreation	238,114
Total depreciation expense - governmental activities	\$ 2,098,757

	BEGINNING BALANCE	INCREASES	DECREASES	ENDING BALANCE
Business-Type Activities				
Capital assets, not being depreciated:				
Land	\$ 2,160,490	\$ -	\$ -	\$ 2,160,490
Construction Work in Progress	5,200,843	2,066,966	(6,102,316)	1,165,493
Total capital assets not being depreciated	7,361,333	2,066,966	(6,102,316)	3,325,983
Capital assets, being depreciated:				
Buildings	637,738	2,269,633	-	2,907,371
Other Improvements	59,338,202	4,581,042	-	63,919,244
Machinery and Equipment	2,573,835	439,003	(29,336)	2,983,502
Intangible	421,961	-	-	421,961
Total capital assets being depreciated	62,971,735	7,289,679	(29,336)	70,232,078
Less accumulated depreciation for:				
Buildings	(411,053)	(13,157)	-	(424,210)
Other Improvements	(16,193,159)	(1,437,482)	-	(17,630,641)
Machinery and Equipment	(1,974,134)	(160,010)	29,336	(2,104,809)
Intangible	(247,811)	(40,271)	-	(288,082)
Total accumulated depreciation	(18,826,157)	(1,650,920)	29,336	(20,447,742)
Total capital assets, being depreciated, net	44,145,578	5,638,758	-	49,784,336
Business-type activity capital assets, net	\$ 51,506,911	\$ 7,705,724	\$ (6,102,316)	53,110,319

Depreciation expense was charged Business-Type Activities of the primary government as follows:

Business-type activities:

Water	\$ 443,147
Sewer	686,073
Solid Waste	61,274
Storm Drain	460,426
Public Works Administration	
Total depreciation expense - business-type activities	\$ 1,650,920

NOTE 6: EMPLOYEE RETIREMENT AND PENSION PLANS

The following table represents the aggregate pension amounts for all plans subject to the requirements of the GASB Statement 68, Accounting and Financial Reporting for Pensions for the year 2016:

Aggregate Pension Amounts - All Plans	
Pension liabilities	\$ (4,607,080)
Pension assets	\$ 349,038
Deferred outflows of resources	\$ 1,060,447
Deferred inflows of resources	\$ (89,545)
Pension expense/expenditures	\$ 683,072

State Sponsored Pension Plans

Substantially all City of Poulsbo's 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 and defined contribution retirement plans. The state Legislature establishes, and amends, laws pertaining to the creation and administration of all public retirement systems.

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 98540-8380

Or the DRS CAFR may be downloaded from the DRS website at www.drs.wa.gov.

Public Employees' Retirement System (PERS)

PERS members include elected officials; state employees; employees of the Supreme, Appeals and Superior Courts; employees of the legislature; employees of district and municipal courts; employees of local governments; and higher education employees not participating in higher education retirement programs. PERS is comprised of three separate pension plans for membership purposes. PERS plans 1 and 2 are defined benefit plans, and PERS plan 3 is a defined benefit plan with a defined contribution component.

PERS Plan 1 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service. The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service. Members retiring from active status prior to the age of 65 may receive actuarially reduced benefits. Retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries. PERS 1 members were vested after the completion of five years of eligible service. The plan was closed to new entrants on September 30, 1977.

Contributions

The **PERS Plan 1** member contribution rate is established by State statute at 6 percent. The employer contribution rate is developed by the Office of the State Actuary and includes an administrative expense component that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates. The PERS Plan 1 required contribution rates (expressed as a percentage of covered payroll) for 2016 were as follows:

PERS Plan 1		
Actual Contribution Rates:	Employer	Employee*
PERS Plan 1	6.23%	6.00%
PERS Plan 1 UAAL	4.77%	6.00%
Administrative Fee	0.18%	
Total	11.18%	6.00%

* For employees participating in JBM, the contribution rate was 12.26%

PERS Plan 2/3 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service for Plan 2 and 1 percent of AFC for Plan 3. The AFC is the average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 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 benefit that is reduced by a factor that varies according to age for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions:

- With a benefit that is reduced by three 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 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five 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 credit. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit. Other PERS Plan 2/3 benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the CPI), capped at three percent annually and a one-time duty related death benefit, if found eligible by the Department of Labor and Industries. PERS 2 members are vested after completing five years of eligible service. 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 12 months of that service are earned after age 44.

PERS Plan 3 defined contribution benefits are totally dependent on employee contributions and investment earnings on those contributions. PERS Plan 3 members choose their contribution rate upon joining membership and have a chance to change rates upon changing employers. As established by statute, Plan 3 required defined contribution rates are set at a minimum of 5 percent and escalate to 15 percent with a choice of six options. Employers do not contribute to the defined contribution benefits. PERS Plan 3 members are immediately vested in the defined contribution portion of their plan.

Contributions

The **PERS Plan 2/3** employer and employee contribution rates are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. The Plan 2/3 employer rates include a component to address the PERS Plan 1 UAAL and an administrative expense that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and Plan 3 contribution rates. The PERS Plan 2/3 required contribution rates (expressed as a percentage of covered payroll) for 2016 were as follows:

PERS Plan 2/3		
Actual Contribution Rates:	Employer 2/3	Employee 2*
PERS Plan 2/3	6.23%	6.12%
PERS Plan 1 UAAL	4.77%	
Administrative Fee	0.18%	
Employee PERS Plan 3		varies
Total	11.18%	6.12%

* For employees participating in JBM, the contribution rate was 15.30%

The city's actual PERS plan contributions were \$224,037 to PERS Plan 1 and \$292,611 to PERS Plan 2/3 for the year ended December 31, 2016.

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

LEOFF membership includes all full-time, fully compensated, local law enforcement commissioned officers, firefighters, and as of July 24, 2005, emergency medical technicians. LEOFF is comprised of two separate defined benefit plans.

LEOFF Plan 1 provides retirement, disability and death benefits. Retirement benefits are determined per year of service calculated as a percent of final average salary (FAS) as follows:

- 20+ years of service – 2.0% of FAS
- 10-19 years of service – 1.5% of FAS
- 5-9 years of service – 1% of FAS

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 ten years of service. Members are eligible for retirement with five years of service at the age of 50. Other benefits include duty and non-duty disability payments, a cost-of living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries. LEOFF 1 members were vested after the completion of five years of eligible service. The plan was closed to new entrants on September 30, 1977.

Contributions

Starting on July 1, 2000, **LEOFF Plan 1** employers and employees contribute zero percent, as long as the plan remains fully funded. The LEOFF Plan 1 had no required employer or employee contributions for fiscal year 2015. Employers paid only the administrative expense of 0.18 percent of covered payroll.

LEOFF Plan 2 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the final average salary (FAS) per year of service (the FAS is based on the highest consecutive 60 months). Members are eligible for retirement with a full benefit at 53 with at least five years of service credit. 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 three percent for each year prior to age 53. Otherwise, the benefits are actuarially reduced for each year prior to age 53. LEOFF 2 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the CPI), capped at three percent annually and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries. LEOFF 2 members are vested after the completion of five years of eligible service.

Contributions

The **LEOFF Plan 2** employer and employee contribution rates are developed by the Office of the State Actuary to fully fund Plan 2. The employer rate included an administrative expense component set at 0.18 percent. Plan 2 employers and employees are required to pay at the level adopted by the LEOFF Plan 2 Retirement Board. The LEOFF Plan 2 required contribution rates (expressed as a percentage of covered payroll) for 2016 were as follows:

LEOFF Plan 2		
Actual Contribution Rates:	Employer	Employee
State and local governments	5.05%	8.41%
Administrative Fee	0.18%	
Total	5.23%	8.41%
Ports and Universities	8.41%	8.41%
Administrative Fee	0.18%	
Total	8.59%	8.41%

The City of Poulsbo's actual contributions to the plan were \$ 80,293 for the year ended December 31, 2016.

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 the state fiscal year ending June 30, 2016, the state contributed \$60,375,158 to LEOFF Plan 2. The amount recognized by the city as its proportionate share of this amount is \$53,239

Actuarial Assumptions

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2016 with a valuation date of June 30, 2015. The actuarial assumptions used in the valuation were based on the results of the Office of the State Actuary's (OSA) *2007-2012 Experience Study*.

Additional assumptions for subsequent events and law changes are current as of the 2015 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2016. Plan liabilities were rolled forward from June 30, 2015, to June 30, 2016, reflecting each plan's normal cost (using the entry-age cost method), assumed interest and actual benefit payments.

- **Inflation:** 3% total economic inflation; 3.75% salary inflation
- **Salary increases:** In addition to the base 3.75% salary inflation assumption, salaries are also expected to grow by promotions and longevity.
- **Investment rate of return:** 7.5%

Mortality rates were based on the RP-2000 report's Combined Healthy Table and Combined Disabled Table, published by the Society of Actuaries. The OSA applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100 percent Scale BB. Mortality rates are applied on a generational basis; meaning, each member is assumed to receive additional mortality improvements in each future year throughout his or her lifetime.

There were minor changes in methods and assumptions since the last valuation.

- For all systems, except LEOFF Plan 2, the assumed valuation interest rate was lowered from 7.8% to 7.7%. Assumed administrative factors were updated.
- Valuation software was corrected on how the nonduty disability benefits for LEOFF Plan 2 active members is calculated.
- New LEOFF Plan 2 benefit definitions were added within the OSA valuation software to model legislation signed into law during the 2015 legislative session.

Discount Rate

The discount rate used to measure the total pension liability for all DRS plans was 7.5 percent.

To determine that rate, an asset sufficiency test included an assumed 7.7 percent long-term discount rate to determine funding liabilities for calculating future contribution rate requirements. (All plans use 7.7 percent except LEOFF 2, which has assumed 7.5 percent). Consistent with the long-term expected rate of return, a 7.5 percent future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue being made at contractually required rates (including PERS 2/3, PSERS 2, SERS 2/3, and TRS 2/3 employers, whose rates include a component for the PERS 1, and TRS 1 plan liabilities). Based on these assumptions, the pension plans' fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.5 percent was used to determine the total liability.

Long-Term Expected Rate of Return

The long-term expected rate of return on the DRS pension plan investments of 7.5 percent was determined using a building-block-method. The Washington State Investment Board (WSIB) used a best estimate of expected future rates of return (expected returns, net of pension plan investment expense, including inflation) to develop each major asset class. Those expected returns make up one component of WSIB's capital market assumptions. The WSIB uses the capital market assumptions and their target asset allocation to simulate future investment returns at various future times. The long-term expected rate of return of 7.5 percent approximately equals the median of the simulated investment returns over a 50-year time horizon.

Estimated Rates of Return by Asset Class

Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2016, are summarized in the table below. The inflation component used to create the table is 2.2 percent and represents the WSIB's most recent long-term estimate of broad economic inflation.

Asset Class	Target Allocation	% Long-Term Expected Real Rate of Return Arithmetic
Fixed Income	20%	1.70%
Tangible Assets	5%	4.40%
Real Estate	15%	5.80%
Global Equity	37%	6.60%
Private Equity	23%	9.60%
	100%	

Sensitivity of NPL

The table below presents the City of Poulsbo's proportionate share of the net pension liability calculated using the discount rate of 7.5 percent, as well as what the City of Poulsbo's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (6.5 percent) or 1-percentage point higher (8.5 percent) than the current rate.

	1% Decrease 6.50%	Current Discount 7.50%	1% Increase 8.50%
PERS 1	2,524,182	2,093,195	1,722,303
PERS 2/3	4,628,516	2,513,886	(1,308,623)
LEOFF 1	(22,908)	(38,564)	(51,945)
LEOFF 2	870,655	(310,474)	(1,200,702)

Pension Plan Fiduciary Net Position

Detailed information about the State's pension plans' fiduciary net position is available in the separately issued DRS financial report.

Pension Liabilities (Assets), Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At June 30, 2016, the City of Poulsbo reported a total pension liability of \$ 4,607,080 and total pension asset of \$349,038 for its proportionate share of the net pension liabilities as follows:

	Liability (or Asset)
PERS 1	\$ 2,093,195
PERS 2/3	2,513,886
LEOFF 1	(38,564)
LEOFF 2	(310,474)

The amount of the liability/(asset) reported above for LEOFF Plan 2 reflects a reduction for State pension support provided to the City. The amount recognized by the city as its proportionate share of the net pension liability/(asset), the related State support, and the total portion of the net pension liability/(asset) that was associated with the city were as follows:

	LEOFF 1 Asset	LEOFF 2 Asset
Employer's proportionate share	\$ 38,564	\$ 310,474
State's proportionate share of the net pension asset associated with the employer	260,843	202,407
TOTAL	\$ 266,407	\$ 512,881

At June 30, the City of Poulsbo's proportionate share of the collective net pension liabilities was as follows:

	Proportionate Share 6/30/15	Proportionate Share 6/30/16	Change in Proportion
PERS 1	0.037386%	0.038976%	0.001590%
PERS 2/3	0.048290%	0.049929%	0.001639%
LEOFF 1	0.005085%	0.003743%	-0.001342%
LEOFF 2	0.053889%	0.053380%	-0.000509%

Employer contribution transmittals received and processed by the DRS for the fiscal year ended June 30 are used as the basis for determining each employer's proportionate share of the collective pension amounts reported by the DRS in the *Schedules of Employer and Nonemployer Allocations* for all plans except LEOFF 1.

LEOFF Plan 1 allocation percentages are based on the total historical employer contributions to LEOFF 1 from 1971 through 2000 and the retirement benefit payments in fiscal year 2016. Historical data was obtained from a 2011 study by the Office of the State Actuary (OSA). In fiscal year 2016, the state of Washington contributed 87.12 percent of LEOFF 1 employer contributions and all other employers contributed the remaining 12.88 percent of employer contributions. LEOFF 1 is fully funded and no further employer contributions have been required since June 2000. If the plan becomes underfunded, funding of the remaining liability will require new legislation. The allocation method the plan chose reflects the projected long-term contribution effort based on historical data.

In fiscal year 2016, the state of Washington contributed 39.46 percent of LEOFF 2 employer contributions pursuant to RCW 41.27.726 and all other employers contributed the remaining 60.54 percent of employer contributions.

The collective net pension liability (asset) was measured as of June 30, 2016, and the actuarial valuation date on which the total pension liability (asset) is based was as of June 30, 2015, with update procedures used to roll forward the total pension liability to the measurement date.

Pension Expense

For the year ended December 31, 2016, the City of Poulsbo recognized pension expense as follows:

	Pension Expense
PERS 1	\$ 198,895
PERS 2/3	375,553
LEOFF 1	8,456
LEOFF 2	100,168
TOTAL	\$ 683,072

Deferred Outflows of Resources and Deferred Inflows of Resources

At December 31, 2016, the city reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

PERS 1	Deferred Outflows of Resources	Deferred Inflows of Resources
Net difference between projected and actual investment earnings on pension plan investments	52,703	-
Contributions subsequent to the measurement date	114,609	-
TOTAL	\$ 167,312	\$ -

PERS 2/3	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 133,863	\$ (82,987)
Net difference between projected and actual investment earnings on pension plan investments	307,627	
Changes of assumptions	25,983	-
Changes in proportion and differences between contributions and proportionate share of contributions	74,451	
Contributions subsequent to the measurement date	149,689	-
TOTAL	\$ 691,612	\$ (82,987)

LEOFF 1	Deferred Outflows of Resources	Deferred Inflows of Resources
Net difference between projected and actual investment earnings on pension plan investments	3,920	-
TOTAL	\$ 3,920	\$ -

LEOFF 2	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 42,543	\$ -
Net difference between projected and actual investment earnings on pension plan investments	111,566	-
Changes of assumptions	1,171	-
Changes in proportion and differences between contributions and proportionate share of contributions	3,432	(6,558)
Contributions subsequent to the measurement date	38,891	-
TOTAL	\$ 197,602	\$ (6,558)

Deferred outflows of resources related to pensions resulting from the city's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2017. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31	PERS 1
2017	(12,977)
2018	(12,977)
2019	48,402
2020	30,254

Year ended December 31	PERS 2/3
2017	27,371
2018	27,371
2019	255,166
2020	149,029

Year ended December 31	LEOFF 1
2017	(810)
2018	(810)
2019	3,395
2020	2,145

Year ended December 31	LEOFF 2
2017	(2,389)
2018	(2,389)
2019	91,312
2020	62,595
2021	3,026

NOTE 7: RISK MANAGEMENT

The city of Poulsbo is a member of the Washington Cities Insurance Authority (WCIA).

Utilizing Chapter 48.62 RCW (self-insurance regulation) and Chapter 39.34 RCW (Interlocal Cooperation Act), nine cities originally formed WCIA on January 1, 1981. WCIA was created for the purpose of providing a pooling mechanism for jointly purchasing insurance, jointly self-insuring, and / or jointly contracting for risk management services. WCIA has a total of 168 Members.

New members initially contract for a three-year term, and thereafter automatically renew on an annual basis. A one-year withdrawal notice is required before membership can be terminated. Termination does not relieve a former member from its unresolved loss history incurred during membership.

Liability coverage is written on an occurrence basis, without deductibles. Coverage includes general, automobile, police, public officials' errors or omissions, stop gap, and employee benefits liability. Limits are \$4 million per occurrence self-insured layer, and \$16 million per occurrence in the re-insured excess layer. The excess layer is insured by the purchase of reinsurance and insurance and is subject to aggregate limits. Total limits are \$20 million per occurrence subject to aggregate sublimits in the excess layers. The Board of Directors determines the limits and terms of coverage annually.

Insurance for property, automobile physical damage, fidelity, inland marine, and boiler and machinery coverage are purchased on a group basis. Various deductibles apply by type of coverage. Property coverage is self-funded from the members' deductible to \$750,000, for all perils other than flood and earthquake, and insured above that to \$300 million per occurrence subject to aggregates and sublimits. Automobile physical damage coverage is self-funded from the members' deductible to \$250,000 and insured above that to \$100 million per occurrence subject to aggregates and sublimits.

In-house services include risk management consultation, loss control field services, and claims and litigation administration. WCIA contracts for certain claims investigations, consultants for personnel and land use issues, insurance brokerage, actuarial, and lobbyist services.

WCIA is fully funded by its members, who make annual assessments on a prospectively rated basis, as determined by an outside, independent actuary. The assessment covers loss, loss adjustment, and administrative expenses. As outlined in the interlocal, WCIA retains the right to additionally assess the membership for any funding shortfall.

An investment committee, using investment brokers, produces additional revenue by investment of WCIA's assets in financial instruments which comply with all State guidelines.

A Board of Directors governs WCIA, which is comprised of one designated representative from each member. The Board elects an Executive Committee and appoints a Treasurer to provide general policy direction for the

organization. The WCIA Executive Director reports to the Executive Committee and is responsible for conducting the day to day operations of WCIA.

The City workers' comprehensive insurance is purchased through the State Labor and Industries program, Unemployment is purchased through Washington State Employment Security, and Health insurance is purchased for staff through Northwest Administrators. The City does not self-insure for any services.

In the past three years, there have been no settlements that exceeded coverage.

NOTE 8: LONG-TERM DEBT

The City issues general obligation and revenue bonds to finance the purchase of capital assets and the construction of infrastructure. Bonded indebtedness has also been entered into (currently and in prior years) to advance refund several general obligation and revenue bonds. General obligation bonds have been issued for general government and are being repaid from the applicable resources. The revenue bonds are being repaid by proprietary fund revenues. The city is also liable for state loans that were entered into for the construction of street infrastructure. These loans are considered obligations of the general government and are being repaid with general governmental revenue sources.

A. BONDS

General Obligation Bonds are a direct obligation of the City for which its full faith and credit are pledged. Debt service is paid from the Debt Service Funds. Debt service for voter-approved issues is funded by special property tax levies. Debt service for non-voted issues is funded from the regular property taxes.

As of December 31, 2016, the governmental long-term debt of the City consisted of the following:

Issuance Date	Purpose	Original Issue	Interest Rates	Maturity Date	Debt Outstanding
2009	Limited GO Bonds: Issued to provide funds for the City Hall Project being constructed at 200 Moe St, which consists of a 30,000 sq ft City Hall facility.	6,015,000	1.4-5.5%	2018	380,000
2010	LOCAL Program GO Bonds: Issued to provide funds to purchase the Park and Rec building.	310,000	4.10%	2030	240,000
2012	Limited GO Bonds: Issued to provide funds to prepay the 2010 Anticipation Note used for City Hall final construction and to refund 2003 GO Bond	2,455,000	.04-3.50%	2031	1,725,000
2015	2015 GO Debt: Refunded 2005 GO Bond and callable portion of the 2009 GO Bond	7,320,000	2-4%	2033	6,950,000
Total					\$ 9,295,000

Revenue Bonds are payable from revenues generated by the Water/Sewer Enterprise Fund.

As of December 31, 2016, the long-term debt payable from proprietary fund resources consisted of the following:

Issuance Date	Purpose	Original Issue	Interest Rates	Maturity Date	Debt Outstanding
2005	Refunding of 1998 Water/Sewer Revenue Bonds	3,134,000	3.45%	2017	475,000
Total					\$ 475,000

B. PUBLIC WORKS TRUST FUND LOANS

State of Washington Public Works Trust Fund Loans (PWTF) are an intergovernmental loan from the Public Works Board to undertake local public works projects. These loans are a direct responsibility of the City. Poulsbo currently has one such loan. The PWTF loan of \$1,406,930 which will be repaid from governmental funds, is for Front Street reconstruction.

As of December 31, 2016, the long-term debt payable for the PWTF loan consisted of the following:

Issuance Date	Purpose	Original Issue	Interest Rates	Maturity Date	Debt Outstanding
2000	Street Improvements to Front Street	1,406,930	3.0%	2020	297,473
Total					\$ 297,473

C. DEBT SERVICE REQUIREMENTS TO MATURITY FOR PRIMARY GOVERNMENT

Year Ended	General Obligation Bonds Governmental Activities			Revenue Bonds Business-Type Activities		
	Principal	Interest	Total	Principal	Interest	Total
Dec 31						
2017	655,000	343,020	998,020	475,000	16,388	491,388
2018	575,000	324,430	899,430	-	-	-
2019	595,000	306,141	901,141	-	-	-
2020	610,000	288,710	898,710	-	-	-
2021	630,000	265,810	895,810	-	-	-
2022-2026	3,190,000	946,256	4,136,256	-	-	-
2027-2031	2,310,000	418,713	2,728,713	-	-	-
2032-2033	730,000	44,200	774,200	-	-	-
	\$ 9,295,000	\$ 2,937,280	\$ 12,232,280	\$ 475,000	\$ 16,388	\$ 491,388

Public Works Trust Fund Loans						
Year Ended	Governmental Activities			Business-Type Activities		
	Principal	Interest	Total	Principal	Interest	Total
Dec 31						
2017	74,368	8,924	83,292	-	-	-
2018	74,368	6,693	81,061	-	-	-
2019	74,368	4,462	78,830	-	-	-
2020	74,368	2,231	76,599	-	-	-
	\$ 297,473	\$ 22,310	\$ 319,784	\$ -	\$ -	\$ -

D. Arbitrage Rebate

Rebatable arbitrage is defined by the Internal Revenue Service Code Section 148 as earnings on investments purchased from the gross proceeds of a bond issue that are in excess of the amount that would have been earned if the investments were invested at a yield equal to the yield on the bond issue. The rebatable arbitrage must be paid to the federal government. The City of Poulsbo monitors its investments to restrict earnings to a yield less than the bond issue, and therefore limit any arbitrage liability. As of December 31, 2016, the City has no arbitrage rebate liability.

E. LONG-TERM LIABILITIES

1. Long-term liability activity:

	Beginning Balance	Additions	Reductions	Ending Balance
Governmental Activities				
Bonds payable:				
General obligation bonds	\$ 9,930,000	\$ -	\$ 635,000	\$ 9,295,000
Less Unamortized Bond Discount	(20,607)	-	(2,534)	(18,073)
Plus Unamortized Bond Premium	793,920	-	50,579	743,341
Pension/OPEB Obligation	3,059,739	3,424,211	2,682,048	3,801,902
Compensated Absences	813,758	667,933	674,558	807,134
Due to Other Governmental Units	371,841	-	74,368	297,473
Total Governmental activity long-term liabilities	\$ 14,948,651	\$ 4,092,144	\$ 4,114,019	\$ 14,926,776
Business-type Activities				
Bonds payable:				
Revenue Bonds	\$ 932,000	\$ -	\$ 457,000	\$ 475,000
Pension/OPEB Obligation	999,017	1,244,154	999,017	1,244,154
Compensated Absences	168,739	140,366	117,345	191,760
Notes Payable	240,527	-	240,527	-
Total Business-type activity long-term liabilities	\$ 2,340,283	\$ 1,384,520	\$ 1,813,889	\$ 1,910,914

2. Liabilities due within one year:

Date of Issue	Liabilities Due Within One Year - Governmental Activities	Due within one year
2015	2015 GO Debt: Refunded 2005 GO Bond and callable portion of the 2009 GO Bond	265,000
2012	Limited GO Bonds: Issued to provide funds to prepay the 2010 Anticipation Note used for City Hall final construction and to refund 2003 GO Bond	190,000
2010	Certificate of Participation to finance the acquisition of the Parks and Recreation facility.	15,000
2009	Limited GO Bonds: Issued to provide funds to finance the City Hall Project being constructed at 200 Moe St, which consists of a 30,000 square foot City Hall facility, including civil site work and architecture and engineering costs	185,000
2000	Due to Other Governmental Units(PWTF)-Street Improvements to Front Street	74,368
	Unamortized premium on GO Bond	46,504
	Unamortized Bond Discount	(2,534)
	Compensated Absences	80,713
Total Governmental Activities		\$ 854,051

Date of Issue	Liabilities Due Within One Year - Business-Type Activities	Due within one year
2005	Water/Sewer Refunded Revenue Bonds	475,000
	Compensated Absences	19,176
Total Business-Type Activities		\$ 494,176

NOTE 9: CONTINGENCIES AND COMMITMENTS

LITIGATION

As of December 31, 2016, there were several damage claims and lawsuits pending against the City. In the opinion of management, the City's insurance policies and/or legal reserves are adequate to pay all known or pending claims, suits and other actions in which payment is considered probable (see Note 7- Risk Management). At this time, there are no judgements against the City, and the City has no material contingent liabilities for which it does not also have insurance coverage. As a result, the City has not recorded any contingent liabilities because management believes that it is not probable that payment will be required.

GRANTS

The City participates in federal-and state- assisted grant programs. These programs are subject to compliance audits by the grantors and their representatives. The audits of these programs for or including the year ended December 31, 2016, have not yet been conducted. Accordingly, the City's compliance with applicable grant requirements will be established at some future date. The amount, if any, of expenditures that may be disallowed by the granting agencies cannot be determined at this time, although the City expects such amounts, if any, to be immaterial.

Contractual Commitments

As of December 31, 2016, the City had 14 significant contractual obligations with the following balances:

<u>Project</u>	<u>Vendor</u>	<u>Amount</u>
Storm Drain Review	Parametrix	\$ 4,763.88
P&R Roof Repair	Garland/DBS Inc.	41,934.29
Liberty Bay Waterfront Trail	Parametrix	18,622.34
Noll Road Phase III Design	Parametrix	96,442.24
Noll Road ROW	Parametrix	234,909.77
Finn Hill Road Improvements	Sealaska	47,255.90
Raab Park Water Tank Replace - design	Gray & Osborne	23,144.84
Viking Ave PRV	Olympic Peninsula Const.	361,266.62
Viking Ave PRV Eng Support	Gray & Osborne	867.46
Poulsbo Village Pump - Design	CHS Engineers, LLC	26,447.24
Liberty Bay Pump - Design	CHS Engineers, LLC	20,051.61
I&I Study	RH2	15,830.96
Anderson Pkwy Phase II	Sealaska	18.00
Raingarden and LID Assistance	KC Conservation District	13,378.73
		<u>\$ 904,933.88</u>

CONTRACTUAL CONTINGENCIES

The City's annexation to Fire District #18 in 1999 carried with it two contingencies. The first contingency was the City's obligation to continue paying off the General Obligation bonds for the Fire Hall which were paid off in 2008. The second contingency is to reimburse to the Fire District any leave cashed out by employees that was accrued before the annexation. The City's portion of the reimbursement is calculated at fifty percent of the cash out. The outstanding leave balance of \$2,803 is included with the City's compensated absences.

As discussed in Note 8, Long-Term Debt, the City is contingently liable for repayment of refunded debt.

NOTE 10: JOINT VENTURES

The City, Kitsap County, and the Kitsap Regional Library agreed back in 1997 to be jointly responsible for the improvement of the library with the City being the lead agency for the construction management. The City owns the building and grounds which is reflected in the Government-Wide Statement of Net Position. The City is responsible for its continued maintenance and the Kitsap Regional Library is responsible for running the day to day

operations of the library within the building.

Any capital improvements needed will be funded out of the Facilities Fund like all other City owned properties. Routine maintenance costs are funded out of the General Fund central services budget.

The financials for the Kitsap Regional Library are available at 1301 Sylvan Way, Bremerton, Washington 98310. Contact: Dan Baer, Chief Financial Officer (360) 405-9137 or on their website www.krl.org.

NOTE 11: POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS

Plan Description

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 under a defined benefit healthcare plan administered by the City. The member's 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 the City's employee medical insurance program. Under the authorization of the LEOFF Disability Board, direct payment is made for other retiree medical expenses not covered by standard medical plan benefit provisions. A separate post-employment benefit plan report is not available. As of December 31, 2016, the City has two retired members in this group.

Funding Policy

Funding for LEOFF retiree healthcare costs is provided entirely by the City as required by RCW. The City currently funds post-employment healthcare benefits on a pay-as-you-go basis. The city finances the plan by purchasing medical insurance and self-funding deductibles and co-pays not covered by the insurance. The expenditures are budgeted in the Police annual operating budget. The city reimburses 100% of the amount of validated claims for medical, dental, vision and hospitalization costs incurred by the retirees.

Annual OPEB Cost and Net OPEB Obligation

The City's annual other post-employment benefit (OPEB) cost is calculated based upon the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB No. 45. The ARC represents a level of funding that if paid on an ongoing basis is projected to cover the normal cost each year and amortized any unfunded actuarial liabilities over a period of ten years as of December 31, 2016.

Actuarial Methods and Assumptions

The City used the alternative measurement method permitted under GASB Statement No. 45. Actual retirement ages are used for the City's two LEOFF members who benefit for the purpose of determining the Actuarial accrued liability (AAL) and normal cost. The mortality rate is assumed following the LEOFF 1 mortality rates used in the June 30, 2014 actuarial valuation report issued by the Office of the Washington State Actuary (OSA). Healthcare costs and trends were determined by Milliman and used by OSA in the state-wide LEOFF 1 medical study performed in 2013 and using a 1% medical inflation rate. The results were based on grouped data with 4 active groupings and 4 inactive groupings. The actuarial cost method used to determine the AAL was Projected Unit Credit. The AAL and NOO are amortized on an open basis as a level dollar over 15 years with an annual budget growth of 2%. Since everything is paid as the expenses are incurred there are no investments held. These assumptions are individually and collectively reasonable for the purposes of this valuation.

The following charts show the trends and assumptions used by Milliman in the assumptions:

Medical Inflation Trend Over Age 65 w/Excise Tax			Medical Inflation Trend Under Age 65 w/Excise Tax			Annual Medical Cost by Age		
Medical		Long-Term Care	Medical		Long-Term	Age	Non-Medicare	Medicare
2012	7.0%	4.8%	2012	7.0%	4.8%	57	\$12,776	N/A
2013	7.5%	4.8%	2013	7.5%	4.8%	62	\$16,401	N/A
2014	6.2%	4.8%	2014	6.2%	4.8%	67	N/A	\$10,947
2015	5.8%	4.8%	2015	5.8%	4.8%	72	N/A	\$12,134
2016	5.7%	4.8%	2016	5.7%	4.8%	77	N/A	\$13,133
2017	12.9%	4.8%	2017	24.7%	4.8%	82	N/A	\$13,791
2018	6.3%	4.8%	2018	6.2%	4.8%	87	N/A	\$14,119
2019	6.5%	4.8%						
2020+	5.6%	4.8%						

The following table shows the components of the City's annual OPEB cost for the year, the amount contributed to the plan, and changes in the City's net OPEB. The net OPEB obligation (NOO) of \$365,358 is included as a long-term liability on the Statement of Position.

<u>Determination of Annual Required Contribution:</u>	<u>Year Ending 2012</u>	<u>Year Ending 2013</u>	<u>Year Ending 2014</u>	<u>Year Ending 2015</u>	<u>Year Ending 2016</u>
Normal Cost at Year End	\$0	\$0	\$0	\$0	\$0
Amorization of Unfunded Actuarial Accrued Liability (UAAL)	60,895	57,308	84,506	108,950	97,114
Annual Required Contribution	\$60,895	\$57,308	\$84,506	\$108,950	\$97,114
<u>Determination of Net OPEB Obligation:</u>					
Annual Required Contribution	\$60,895	\$57,308	\$84,506	\$108,950	\$97,114
Interest prior year Net OPEB Obligation	6,161	7,233	7,332	9,218	12,163
Adjustments to ARC	(12,747)	(14,966)	(16,485)	(20,728)	(27,349)
Annual OPEB Cost	\$54,309	\$49,575	\$75,352	\$97,440	\$81,929
Contributions	(30,476)	(27,017)	(28,184)	(23,824)	(20,645)
Increase in Net OPEB Obligations	\$23,833	\$22,558	\$47,168	\$73,616	\$61,284
Net OPEB Obligation-Beginning of Year	\$136,900	\$160,732	\$183,290	\$230,458	\$304,075
NET OPEB Obligation-End of Year	\$160,732	\$183,290	\$230,458	\$304,075	\$365,358

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

Year Ending	Annual OPEB Cost	Contribution as a Percentage of OPEB Cost	Net OPEB Obligation
12/31/2012	54,309	56.1%	160,732
12/31/2013	49,575	54.5%	183,290
12/31/2014	75,352	37.4%	230,458
12/31/2015	97,440	24.4%	304,075
12/31/2016	81,929	25.2%	365,358

Funded Status and Funding Progress

As of December 31, 2016, the most recent actuarial valuation date, the plan was 0% funded. The actuarial accrued liability (AAL) for benefits was \$1,079,756 and the actuarial value of the assets was \$0 resulting in a UAAL of \$1,079,756. Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with

past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial liabilities for benefits.

NOTE 12: PRIOR PERIOD ADJUSTMENTS

Adjustments related to prior periods were a result of corrections made to the following funds that were considered to be of a material value:

Fund #	Fund Description	Governmental Statement Amount	Government-Wide Statement Amount	Reason
101	City Street Fund	\$ 9,714.90	\$ 9,714.90	Prior year adjustment due to grant revenue received unexpectedly for a prior year expense.
123	Transportation Development Fund	(36,633.99)	(36,633.99)	Prior year adjustment for funds transferred for mitigation in error
131	Historic Downtown Fund	1,224.20	1,224.20	Prior year adjustment due to overpayment made for advertising
191	Police Restricted Fund	6,741.50	6,741.50	Prior year adjustment for marine vessel grant recorded in the incorrect fund
204	Non-Voted General Obligation Debt Fund	231.15	231.15	Prior year adjustment due to overpayment made for debt service costs.
		<u>\$ (18,722.24)</u>	<u>\$ (18,722.24)</u>	

NOTE 13: RECONCILIATION OF NET INVESTMENT IN CAPITAL ASSETS

Governmental Activities:

Capital Assets, Net of Depreciation	\$ 77,546,529
General Obligation Bonds Payable	(9,295,000)
Unamortized premium on Bonds	(743,341)
Unamortized discount on Bonds	18,073
Deferred Outflows - Loss on Refunding	605,929
Due to Other Governments	<u>(297,473)</u>

Net Investment in Capital Assets

\$ 67,834,718

Business-Type Activities:

Capital Assets, Net of Depreciation	\$ 53,110,319
Revenue Bonds Payable	(475,000)
Deferred Outflows - Loss on Refunding	<u>16,933</u>

Net Investment in Capital Assets

\$ 52,652,252

NOTE 14: SUBSEQUENT EVENTS

On June 4, 2014, the City Council approved the sale of the commercial property known as the "Old City Hall Site" at 19050 Jensen Way NE, Poulsbo, Washington for \$1.2 million. The sale was contingent on securing approval by Kitsap County, a feasibility study for site plan approval on intended development, segregation of property, demolition of existing building and proof of hazardous substances study. This agreement and subsequent closing date has been extended due to remedial action needed discovered during demolition, which was completed. The final closing occurred on April 24th, 2017. After providing Kitsap County with their share of the proceeds, the Council have allocated funds to be reserved for early redemption of the debt issued for the new city hall. The remaining proceeds will be devoted to both capital improvements and to replenish the revenue stabilization reserves fund balance.

On June 10, 2015, the City Council approved the sale of the commercial property known as the "Old Police Station" at 367 NE Hostmark Street, Poulsbo, Washington for \$900,000. The sale was contingent on obtaining a site plan approval for a planned development. The original agreement was rescinded when the purchaser failed to provide escrow at the same time Washington State Department of Ecology established the proper Ordinary High Water Mark

alignment on the property diminishing the amount of land available for planned development. On January 30, 2017, the City Council approved a new agreement of sale for \$825,000. A \$50,000 promissory note was provided contingent on 120-day feasibility period. The Council allocated proceeds may be used for early redemption of the debt issued for the purpose of the construction of the new city hall. The remaining proceeds of this sale will be devoted to both capital improvements and to replenish the revenue stabilization reserves fund balance.

REQUIRED SUPPLEMENTARY INFORMATION
LEOFF I RETIREE MEDICAL BENEFITS
SCHEDULE OF FUNDING PROGRESS
December 31, 2016

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b-a)/c]
12/31/2010	\$ -	\$ 662,910	\$ 662,910	0%	-	N/A*
12/31/2011	\$ -	\$ 684,261	\$ 684,261	0%	-	N/A*
12/31/2012	\$ -	\$ 653,990	\$ 653,990	0%	-	N/A*
12/31/2013	\$ -	\$ 615,465	\$ 615,465	0%	-	N/A*
12/31/2014	\$ -	\$ 939,567	\$ 939,567	0%	-	N/A*
12/31/2015	\$ -	\$ 1,211,345	\$ 1,211,345	0%	-	N/A*
12/31/2016	\$ -	\$ 1,079,756	\$ 1,079,756	0%	-	N/A*

* Since the covered payroll is \$0, the UAAL as a percentage of covered payroll cannot be defined

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Proportionate Share of the Net Pension Liability
PERS 1
As of June 30, 2016
Last 3 years

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Employer's proportion of the net pension liability (asset)	0.036729%	0.037386%	0.038976%
Employer's proportionate share of the net pension liability	<u>\$ 1,850,241</u>	<u>\$ 1,955,635</u>	<u>\$ 2,093,195</u>
Total	<u><u>\$ 1,850,241</u></u>	<u><u>\$ 1,955,635</u></u>	<u><u>\$ 2,093,195</u></u>
Employer's covered employee payroll	\$ 4,045,587	\$ 4,285,003	\$ 4,671,276
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	46%	46%	45%
Plan fiduciary net position as a percentage of the total pension liability	61.19%	59.10%	57.03%

See notes to Required Supplementary Information

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Proportionate Share of the Net Pension Liability
PERS 2/3
As of June 30, 2016
Last 3 years

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Employer's proportion of the net pension liability (asset)	0.047289%	0.048290%	0.049929%
Employer's proportionate share of the net pension liability	<u>\$ 955,881</u>	<u>\$ 1,725,429</u>	<u>\$ 2,513,886</u>
Total	<u><u>\$ 955,881</u></u>	<u><u>\$ 1,725,429</u></u>	<u><u>\$ 2,513,886</u></u>
Employer's covered employee payroll	\$ 4,045,587	\$ 4,285,003	\$ 4,671,276
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	23.63%	40.27%	53.82%
Plan fiduciary net position as a percentage of the total pension liability	93.29%	89.20%	85.82%

See notes to Required Supplementary Information

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Proportionate Share of the Net Pension Liability
LEOFF 1
As of June 30, 2016
Last 3 years

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Employer's proportion of the net pension liability (asset)	0.005043%	0.005085%	0.003743%
Employer's proportionate share of the net pension liability	<u>\$ (61,161)</u>	<u>\$ (61,282)</u>	<u>\$ (38,564)</u>
Total	<u><u>\$ (61,161)</u></u>	<u><u>\$ (61,282)</u></u>	<u><u>\$ (38,564)</u></u>
Employer's covered employee payroll	0	0	0
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	N/A	N/A	N/A
Plan fiduciary net position as a percentage of the total pension liability	126.91%	127.36%	123.74%

See notes to Required Supplementary Information

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Proportionate Share of the Net Pension Liability
LEOFF 2
As of June 30, 2016
Last 3 years

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Employer's proportion of the net pension liability (asset)	0.052340%	0.053889%	0.053380%
Employer's proportionate share of the net pension liability	\$ (694,574)	\$ (553,871)	\$ (310,474)
State's proportionate share of the net pension liability (asset) associated with the employer	<u>\$ (453,820)</u>	<u>\$ (366,222)</u>	<u>\$ (202,407)</u>
Total	<u><u>\$ (1,148,394)</u></u>	<u><u>\$ (920,093)</u></u>	<u><u>\$ (512,881)</u></u>
Employer's covered employee payroll	\$ 1,456,576	\$ 1,564,053	\$ 1,617,108
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	47.69%	35.41%	19.20%
Plan fiduciary net position as a percentage of the total pension liability	116.75%	111.67%	106.04%

See notes to Required Supplementary Information

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Employer Contributions
PERS 1
As of December 31, 2016
Last 3 years

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Statutorily or contractually required contributions	\$ 167,996	\$ 199,036	\$ 224,037
Contributions in relation to the statutorily or contractually required contributions	<u>(167,996)</u>	<u>(199,036)</u>	<u>(224,037)</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Covered employer payroll	\$ 4,152,711	\$ 4,510,640	\$ 4,696,806
Contributions as a percentage of covered employee payroll	4.05%	4.41%	4.77%

See notes to Required Supplementary Information

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Employer Contributions
PERS 2/3
As of December 31, 2016
Last 3 years

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Statutorily or contractually required contributions	\$ 208,036	\$ 255,711	\$ 292,611
Contributions in relation to the statutorily or contractually required contributions	<u>(208,036)</u>	<u>(255,711)</u>	<u>(292,611)</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Covered employer payroll	\$ 4,152,711	\$ 4,510,640	\$ 4,696,806
Contributions as a percentage of covered employee payroll	5.01%	5.67%	6.23%

See notes to Required Supplementary Information

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Employer Contributions
LEOFF 1
As of December 31, 2016
Last 3 years

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Statutorily or contractually required contributions	0	0	0
Contributions in relation to the statutorily or contractually required contributions	<u>0</u>	<u>0</u>	<u>0</u>
Contribution deficiency (excess)	<u>0</u>	<u>0</u>	<u>0</u>
Covered employer payroll	0	0	0
Contributions as a percentage of covered employee payroll	0.00%	0.00%	0.00%

See notes to Required Supplementary Information

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Employer Contributions
LEOFF 2
As of December 31, 2016
Last 3 years

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Statutorily or contractually required contributions	\$ 78,406	\$ 80,712	\$ 80,293
Contributions in relation to the statutorily or contractually required contributions	<u>(78,406)</u>	<u>(80,712)</u>	<u>(80,293)</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Covered employer payroll	\$ 1,552,594	\$ 1,598,225	\$ 1,589,968
Contributions as a percentage of covered employee payroll	5.05%	5.05%	5.05%

See notes to Required Supplementary Information

Notes to Required Supplementary Information – Pensions Year Ended December 31, 2016

Note 1 – Information provided

There are no City employees participating in the PERS 1 or LEOFF 1 plans in 2016; therefore, there is no covered payroll reported under LEOFF 1.

PERS 1 employer contributions include the PERS 1 employer contributions of PERS 2 and PERS 3, which are required to fund the unfunded actuarially accrued liability pursuant to RCW 41.45.060. LEOFF 1 is fully funded, and no further employer contributions have been required since June 2000. If the plan becomes underfunded, funding of the remaining liability will require new legislation.

The City's proportionate share of the PERS 2/3 plan increased 0.001639% or \$788,456, totaling 0.049929% or \$2,513,886. This results in the percentage of covered employee payroll in the City's proportionate share increasing 13.55%.

The City's proportionate share of the LEOFF 2 plan decreased 0.000509% or \$243,397, totaling 0.053380% or \$310,474. This results in the percentage of covered employee payroll in the City's proportionate share decreasing 16.21%. The State's proportionate share of the LEOFF 2 plan also decreased \$163,815, totaling \$202,407.

Note 2 – Significant errors

There were no changes of benefit terms, significant changes in the employees covered under the benefit terms or in the use of different assumptions.

Note 3 – Employer contribution rate changes

There were no changes in employer contribution rates in 2016.

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.

The results of our work are widely distributed through a variety of reports, which are available on our [website](#) and through our free, electronic [subscription](#) service.

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

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