



MANAGEMENT'S DISCUSSION AND ANALYSIS

The discussion and analysis are intended to serve as an introduction to the basic financial statements of *Pierce County*. The financial statements provide an overview of county financial activities for the fiscal year ended December 31, 2004. The discussion and analysis should be read in conjunction with the preceding letter of transmittal and the accompanying financial statements.

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial statements presented herein include all of the activities of *Pierce County* using the integrated approach as prescribed by Governmental Accounting Standards Board (GASB) Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – For State and Local Governments. This financial report is comprised of three components; Government-Wide Financial Statements, Fund Financial Statements, and Notes to the Financial Statements. Notes to the Financial Statements provide additional information that is essential to a full understanding of the data presented in the Government-Wide and Fund Financial Statements. Combining statements for certain nonmajor governmental funds and *Internal Service Funds* are presented immediately following the notes to the financial statements. The report also includes other supplementary information designed to enable the reader to gain maximum understanding of county financial activities.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

Government-wide statements are designed to provide readers with a broad overview of *Pierce County* finances in a manner similar to that of a private-sector business.

The statement of net assets presents information on all of the county assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the county is improving or deteriorating.

The statement of activities presents information showing changes in the government's net assets during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will actually result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave). This is intended to summarize and simplify the reader's analysis of the revenues and costs of various county activities and the degree to which activities are subsidized by general revenues.

Both government-wide financial statements distinguish between functions of *Pierce County* principally supported by taxes and intergovernmental revenues (governmental activities) and other functions that are intended to recover all or a significant portion of operating costs through user fees and charges (business-type activities). The governmental activities of the county include general government, public safety, physical environment, legal, judicial, economic environment, transportation, health and human services, and culture and recreation. Business-type activities include water and sewer utilities, solid waste management and the associated landfill reserve, airport, ferry services, and golf course.

FUND FINANCIAL STATEMENTS

Fund financial statements are designed to report information about groupings of related accounts that are used to maintain control over resources that have been segregated for specific activities or objectives. The county, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance related legal requirements. All of the funds of the county can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

GOVERNMENTAL FUNDS

Essentially the same functions reported as governmental activities in the government-wide financial statements are reported in governmental fund financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-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. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities as reported in the government-wide statements.

The county maintains a general fund and several other individual governmental funds organized according to their type (special revenue, debt service, and capital projects). Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the *General Fund*, the *Human Services Fund*, and the *Roads Fund*, all of which are considered to be major funds. Data from the other governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor governmental funds is provided in the form of combining statements elsewhere in this report.

Budgetary comparison statements are presented for the *General Fund*, *Human Services Fund* and the *Roads Fund* to demonstrate the flow of resources in relation to the legally adopted budget.

PROPRIETARY FUNDS

Pierce County maintains two types of proprietary funds; *Enterprise Funds* and *Internal Service Funds*. *Enterprise Funds* are used to report the same functions presented as business-type activities in the government-wide financial statements. Water and sewer utilities, solid waste management, landfill reserve, airport, ferry services, and the golf courses are accounted for in *Enterprise Funds*. *Internal Service Funds* are a fund type used to accumulate and allocate costs internally among the various county functions. *Pierce County* uses *Internal Service Funds* to account for equipment and fleet services, information services, facilities management, radio communications, general services, self-insurance, and workers compensation activities. Because these services predominantly benefit governmental rather than business-type functions, *Internal Service Funds* have been included within governmental activities in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statement, only in more detail. The proprietary fund financial statements provide separate information for the *Sewer Utility* and for the *Landfill Reserve*, both of which are considered to be major funds of the county. Data from the other six *Enterprise Funds* and all eight *Internal Service Funds* are combined into individual, aggregated presentations. Individual fund data for each of these nonmajor proprietary funds is provided in the form of combining statements elsewhere in this report.

FIDUCIARY FUNDS

Resources held for the benefit of parties outside the government are accounted for in fiduciary funds. Because the resources of those funds are not available to support county programs, fiduciary funds are not reflected in the government-wide financial statements. The accounting used for fiduciary funds is much like that used for proprietary funds.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Shown below are condensed versions of the government-wide statements of activities and net assets for both governmental and business-type operations. The government-wide statements are presented in detail in the financial section of this report.

STATEMENT OF ACTIVITIES

The following is a summary of the changes in net assets from the statement of activities:

Condensed Summary of Changes in Net Assets (In Thousands)

	Governmental Activities		Business-Type Activities		Total	
	2004	2003 (Restated)	2004	2003	2004	2003 (Restated)
Program Revenues:						
Charges for Services	\$ 51,948	\$ 50,225	\$ 32,065	\$ 28,084	\$ 84,013	\$ 78,309
Operating Grants and Contributions	180,761	172,344	1,280	550	182,041	172,894
Capital Grants and Contributions	11,058	17,793	10,702	7,286	21,760	25,079
General Revenues:						
Taxes	207,922	200,531	211	173	208,133	200,704
Interest and Investment Earnings	7,559	5,869	213	830	7,772	6,699
Other General Revenue	1,675	450	(31)	(189)	1,644	261
Total Revenues	460,923	447,212	44,440	36,734	505,363	483,946
Expenses:						
General Government	28,876	29,878	—	—	28,876	29,878
Public Safety	114,093	110,194	—	—	114,093	110,194
Physical Environment	23,891	22,168	—	—	23,891	22,168
Transportation	43,747	39,622	—	—	43,747	39,622
Legal and Judicial	58,402	55,218	—	—	58,402	55,218
Economic Environment	15,927	16,176	—	—	15,927	16,176
Health and Human Services	100,518	98,065	—	—	100,518	98,065
Culture and Recreation	8,738	8,740	—	—	8,738	8,740
Interest on Long-Term Debt	2,791	2,898	—	—	2,791	2,898
Sewer Utility	—	—	27,441	26,113	27,441	26,113
Solid Waste Landfill Reserve	—	—	—	114	—	114
Solid Waste Management	—	—	3,194	2,881	3,194	2,881
Airport	—	—	476	528	476	528
Ferry Services	—	—	2,687	2,074	2,687	2,074
Golf Course	—	—	1,038	1,014	1,038	1,014
Water Utility	—	—	6	18	6	18
Total Expenses	396,983	382,959	34,842	32,742	431,825	415,701
Change in Net Assets before Transfers and Extraordinary Items						
	63,940	64,253	9,598	3,992	73,538	68,245
Transfers	(1,513)	(289)	1,513	289	—	—
Extraordinary Items	—	4,241	—	(2,471)	—	1,770
Beginning Net Assets (Restated)	772,848	704,643	417,806	415,996	1,190,654	1,120,639
Ending Net Assets	\$ 835,275	\$ 772,848	\$ 428,917	\$ 417,806	\$ 1,264,192	\$ 1,190,654

Financial Highlights

- ✦ Expenses for 2004 totaled approximately \$431.8 million, consisting of \$396.9 million (92%) from governmental activities and \$34.8 (8%) from business-type activities.
- ✦ Total program revenues for all activities were \$287.8 million and funded approximately 67% of the total expenses for *Pierce County*. This is almost the same percentage as in fiscal 2003 (66%). The remaining expenses were financed through general revenues (principally taxes).

- ✦ Only modest changes occurred in expenses, program revenues, and general revenues in 2004 versus 2003.
- ✦ Governmental activities were funded by program revenues of approximately \$243.7 million (61%), with general revenues financing the remaining 39% of governmental activities expenses. This represents a slight decrease in the percentage of expenses paid by program revenues.
- ✦ Business-type activities generated program revenues of approximately \$44 million, which exceeded related expenses by \$9.2 million. Much of this positive margin occurred in the *Sewer Utility*.
- ✦ Total government-wide program revenues plus general revenues equaled \$505.4 million and exceeded total government-wide expenses of \$431.8 million. This resulted in government-wide net assets increasing \$73.5 million during fiscal 2004, which is similar to the increase in net assets for the prior year.
- ✦ A large majority of the increase in government-wide net assets occurred in governmental activities. The increase was due primarily to capital asset acquisitions, including investments in land, buildings, infrastructure, right-of-way, equipment, and construction in progress.

The following table directly compares governmental and business-type activities with associated program revenues:

Comparative Statement of Activities
(in thousands)

Governmental Activities	2004			2003
	Expenses	Program Revenues	Net Revenues (Expenses)	Net Revenues (Expenses) (Restated)
Public Safety	\$ 114,093	\$ 31,173	\$ (82,920)	\$ (77,218)
Legal and Judicial	58,402	19,301	(39,101)	(38,316)
Transportation	43,747	25,582	(18,165)	(8,666)
Health and Human Services	100,518	108,150	7,632	2,730
All Other Programs	80,225	59,560	(20,665)	(21,128)
	<u>\$ 396,985</u>	<u>\$ 243,766</u>	(153,219)	(142,598)
General Revenues			215,644	210,803
Change in Net Assets			<u>\$ 62,425</u>	<u>\$ 68,205</u>

Business-Type Activities	2004			2003
	Expenses	Program Revenues	Net Revenues (Expenses)	Net Revenues (Expenses)
Sewer Utility	\$ 27,441	\$ 35,613	\$ 8,172	\$ 3,890
Solid Waste Management	3,195	3,619	424	30
Ferry Services	2,687	2,728	41	(441)
All Other Programs	1,520	2,087	567	(301)
	<u>\$ 34,843</u>	<u>\$ 44,047</u>	9,204	3,178
General Revenues			1,906	(1,369)
Change in Net Assets			<u>\$ 11,110</u>	<u>\$ 1,809</u>

Financial Highlights

- ✦ As would be expected in governmental activities, the programs which needed the greatest general revenue support were public safety, and the legal and judicial system (total support equal to \$122 million).
- ✦ The gap between total governmental activities expenses and related program revenues increased from \$142.6 million in 2003 to \$153.2 in 2004. Much of this gap growth was caused by increases in roadway system expenses.
- ✦ However, the county generated a \$62.4 million increase in net assets for governmental activities because general revenues were more than sufficient to cover the net gap between expense and program revenues.
- ✦ Business-type activities reported a \$11.1 million increase in net assets, which is considerably more than the 2003 amount of \$1.8 million. The increase was mostly due to the strong fiscal performance of the *Sewer Utility Fund*.

STATEMENT OF NET ASSETS

The following is a summary of the government-wide statement of net assets presented in detail in the financial section of this report:

Condensed Statement of Net Assets (in thousands)

	Governmental Activities		Business-Type Activities		Total	
	2004	2003 (Restated)	2004	2003	2004	2003 (Restated)
Current Assets	\$ 286,100	\$ 258,227	\$ 35,613	\$ 30,123	\$ 321,713	\$ 288,350
Restricted Assets/Joint Ventures	599	599	46,002	53,182	46,601	53,781
Capital Assets	670,127	631,455	385,123	381,470	1,055,250	1,012,925
Total Assets	956,826	890,281	466,738	464,775	1,423,564	1,355,056
Current Liabilities	69,158	51,600	7,741	4,290	76,899	55,890
Noncurrent Liabilities	52,393	65,833	30,080	42,679	82,473	108,512
Total Liabilities	121,551	117,433	37,821	46,969	159,372	164,402
Total Net Assets	\$ 835,275	\$ 772,848	\$ 428,917	\$ 417,806	\$ 1,264,192	\$ 1,190,654

Financial Highlights

- ✦ Approximately \$835 million (66%) of total net assets are related to governmental activities, while \$429 million (34%) are related to business-type activities.
- ✦ As indicated earlier, net assets increased by \$74 million in 2004, most of which was generated by governmental activities.
- ✦ Capital assets account for approximately 74% of total assets, and 83% of total net assets. The 2003 percentages were similar.
- ✦ Although total liabilities did not change significantly (in fact they decreased), there was a major shift between current liabilities and noncurrent liabilities. A large part of this was due to a change in calculating how much of compensated absences should be current based upon actual experience. This change by itself resulted in a \$9.3 million switch from noncurrent to current liabilities.

- ✦ Net assets can be further summarized as follows:

Summary of Net Assets
(in thousands)

	Governmental Activities		Business-Type Activities		Total	
	2004	2003 (Restated)	2004	2003	2004	2003 (Restated)
Capital Assets (Net of Related Debt)	\$ 617,878	\$ 578,530	\$ 357,376	\$ 348,531	\$ 975,254	\$ 927,061
Restricted Net Assets	128,819	111,355	39,906	44,037	168,725	155,392
Unrestricted Net Assets	88,578	82,963	31,635	25,238	120,213	108,201
Total Net Assets	<u>\$ 835,275</u>	<u>\$ 772,848</u>	<u>\$ 428,917</u>	<u>\$ 417,806</u>	<u>\$ 1,264,192</u>	<u>\$ 1,190,654</u>

- ✦ Only 11% of governmental activities net assets are unrestricted, while only 7% of the business-type activities net assets are unrestricted.
- ✦ Unrestricted net assets increased by \$12 million in 2004, which will provide resources for future years' operational and capital programs.

FINANCIAL ANALYSIS OF MAJOR COUNTY FUNDS

GENERAL FUND

Revenues. The *General Fund* receives unrestricted county revenue which is used to finance such activities as law enforcement, county detention facilities, the judicial system, planning and development regulation, general governmental services, parks and recreation programs, and various human and health services. Revenue and all other financing sources for the *General Fund* totaled \$234 million in fiscal 2004, representing only a 1.7% increase from the prior year. Revenue categories, with the changes from last fiscal year, are summarized as follows:

Summary of General Fund Revenues and Other Financing Sources
(in thousands)

Category	Amount		Increase (Decrease)	
	2004	2003	Amount	Percent
Revenue:				
Property and Other Taxes	\$ 97,040	\$ 96,829	\$ 211	0.2 %
Sales Tax	44,722	43,695	1,027	2.4 %
Licenses & Permits	7,109	6,586	523	7.9 %
Intergovernmental	37,034	37,205	(171)	(0.5) %
Charges for Services	31,447	31,203	244	0.8 %
Fines and Forfeits	5,145	5,202	(57)	(1.1) %
Interest	6,971	5,567	1,404	25.2 %
Miscellaneous Revenue	1,966	1,878	88	4.7 %
Total Revenue	231,434	228,165	3,269	1.4 %
Other Financing Sources	2,609	2,057	552	26.8 %
Total Funding Sources	<u>\$ 234,043</u>	<u>\$ 230,222</u>	<u>\$ 3,821</u>	1.7 %

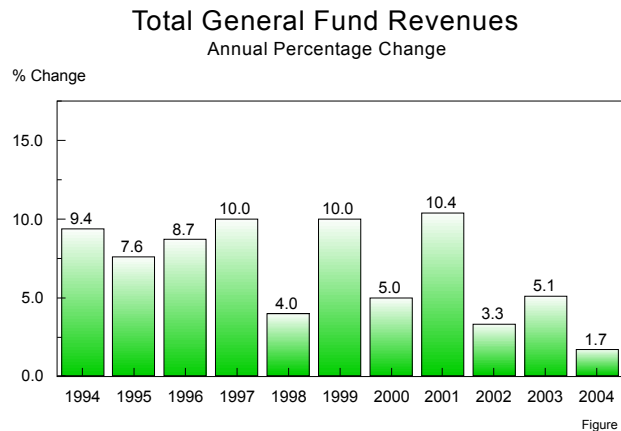
A more detailed discussion of the major changes from the prior year follows:

- ✦ **Property and Other Taxes.** The relatively small growth reflected the fact that settlement of a large outstanding tax case occurred in 2003, which caused last year's revenues to be unusually high.
- ✦ **Licenses and Permits.** The 7.9% increase was due primarily to the continued strong growth in building activity.
- ✦ **Intergovernmental.** These revenues reflected a slight decrease due to the discontinuance of a large police services contract in the fall of 2004.

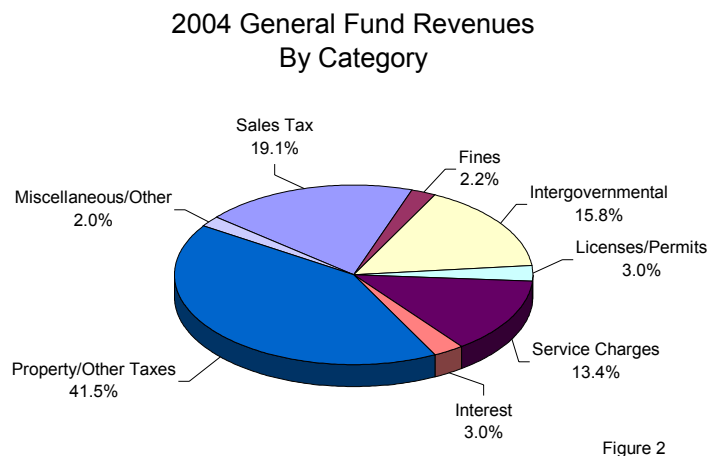
- ✦ **Interest Revenues.** The second half boost in short term interest rates resulted in a significant increase in interest revenues.
- ✦ **Other Financing Sources.** The large increase resulted from timber and land sales.

As shown in the chart below, the 1.7% increase in revenue was the lowest percentage growth in the last decade. Three factors are largely responsible for this low percentage. First, the termination of the aforementioned police services contract by itself resulted in an approximate decline of 1.5%. Second, the 2003 revenues were somewhat inflated due to the previously mentioned settlement of a tax assessment case. Third, property tax revenue growth from existing property are now limited to 1%. Were it not for the first two factors, the revenue increase in 2004 would have been between 3%-4%.

It is likely that revenue increases in the rest of the decade will be below the levels from 1994-2001 due to the continued impact of the voter approved initiative limiting property tax revenue increases to 1%.



The chart below presents the percentage of 2004 revenue by category for the *General Fund*. The chart illustrates our continued dependence on property and sales taxes (a combined 60.6%) as the major revenue sources. During the last ten years the percentage of revenues from such taxes has declined slightly as service charges and intergovernmental revenue percentages have grown. Incorporation of new cities has shifted funding sources from taxes to intergovernmental revenues and service charges resulting from contracts with new cities.



Expenditures. Fiscal 2004 *General Fund* expenditures and transfers out totaled \$234.7 million, representing an increase of \$7.3 million (3.2%) from 2003. All transfers are classified into related functional areas and are included in the comparison of expenditures.

Comparisons of expenditures for the last two years are presented below:

Summary of General Fund Expenditures and Transfers Out
(in thousands)

Functional Area	Amount		Increase (Decrease)	
	2004	2003	Amount	Percent
General Government	\$ 35,142	\$ 32,792	\$ 2,350	7.2 %
Public Safety	113,844	113,163	681	0.6 %
Physical Environment	14,347	13,868	479	3.5 %
Legal and Judicial	58,666	55,557	3,109	5.6 %
Mental and Physical Health	3,246	3,319	(73)	(2.2) %
Culture and Recreation	7,941	7,248	693	9.6 %
Economic Environment	1,535	1,430	105	7.3 %
Total Expenditures and Transfer Outs	<u>\$ 234,721</u>	<u>\$ 227,377</u>	<u>\$ 7,344</u>	3.2 %

The major changes from last year are explained below:

- ✦ **General Government.** The majority of this increase was due to “presidential year” elections expense and building remodel projects.
- ✦ **Culture and Recreation.** The large increase reflects a one-time allocation for a parks trail project.
- ✦ **Economic Environment.** The large increase reflects allocations for additional staffing and job creation studies in the economic development department.

The chart below graphically illustrates relative budget allocations to the various county functional areas. Combined expenditures for public safety, and legal and judicial functions make up 73.5% of total *General Fund* expenditures. The combined percentage for these two major functions would easily exceed 77% if the related general government support costs were all allocated to each department. Similarly, on a combined basis over 80% of the increase in total *General Fund* expenditures over the last ten years occurred in these two major functional areas. The trend is expected to continue over the next few years with increased demand for sheriff services, growing court caseloads, and full operation of the new jail facility.

2004 General Fund Expenditures
By Category

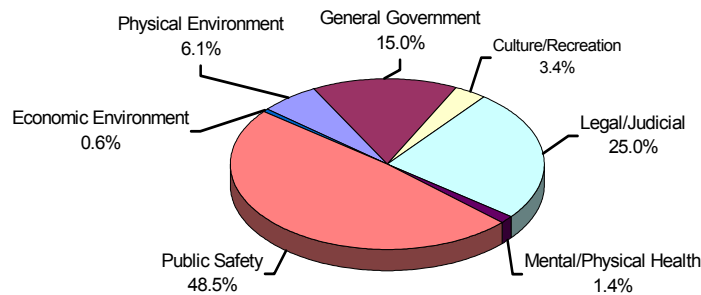
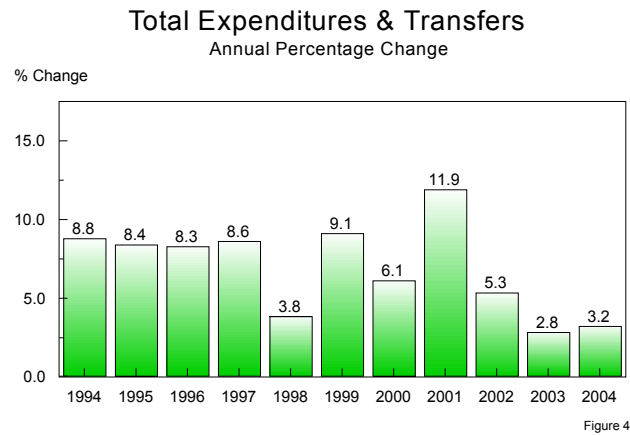


Figure 3

As previously indicated, total 2004 expenditures and transfers increased 3.2% from 2003 activity. The 2004 percentage increase was among the lowest in the last ten years, reflecting the downward trend in revenues discussed earlier. Corresponding percentage increases from prior years are presented below:

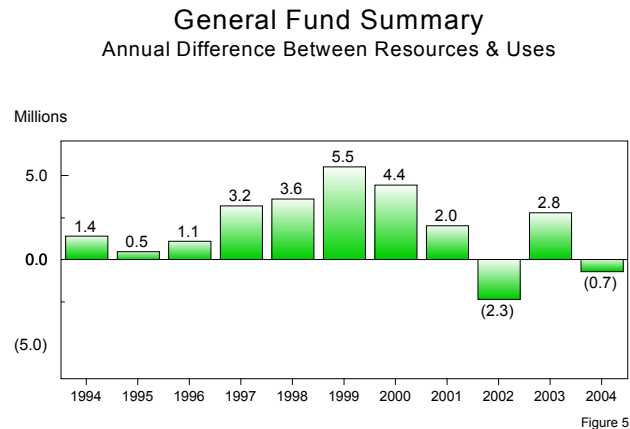


The 2004 "bottom-line" fiscal result for the *General Fund* was slightly negative, generating a "deficit" of \$678,000 summarized as follows:

Summary of General Fund Changes in Fund Balance
(in thousands)

Revenues	\$ 231,434	
Expenditures	<u>223,621</u>	
Excess of Revenues Over Expenditures		\$ 7,813
Other Financing Sources (Uses), Net		<u>(8,491)</u>
Change in Fund Balance		<u><u>(678)</u></u>

The following graph illustrates the relationship between resources (including all revenues and transfers in) and uses (including all expenditures and transfers out) for 2004 and the past ten years. The trend has been generally positive; with resources exceeding uses every year except 2002 and 2004. Most of the "deficits" in 2002 and 2004 were attributable to one-time allocations for a new computerized appraisal and tax system, and building remodel expenses.



Budget Comparisons. The original *General Fund* budget passed by the County Council totaled \$232.6 million. During the year the budget was increased by \$4.9 million for the following reasons:

- ✦ An increase of \$703,830 in miscellaneous current expense for the purchase of a building which was rented by several county departments.
- ✦ A \$20,000 allocation for printing expenses in the County Council's office.
- ✦ A \$173,395 allocation for various community projects and services as specified by the County Council.
- ✦ Increases totaling \$4,025,457 reflecting various grants, service contracts, and election cost reimbursements which are essentially self-funding.

The above budget increases were financed as follows:

Use of Fund Balance	\$ 897,225
Grants, Service Contracts, and Election Cost Reimbursement	<u>4,025,457</u>
Total Budget Increase Financing	<u><u>\$ 4,922,682</u></u>

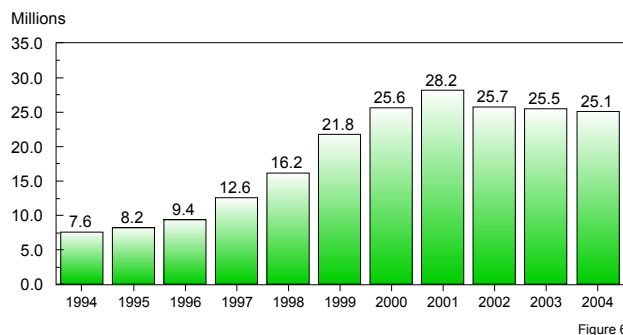
There was only one significant variance between the final approved expenditure budget of \$237.5 million and the actual expenditures of \$234.7 million. That was in the sheriff's department, which under spent its total budget by \$1 million due to the early termination of a large city police services contract.

General Fund Balance. The unreserved fund balance for the *General Fund* was approximately \$25.1 million at December 31, 2004, reflecting a slight decrease of approximately \$400,000 from 2003. This decrease resulted from the aforementioned operating "deficit" of \$678,000, partially offset by a decline in Reserves of \$217,000.

Fund balance serves several purposes for the county. It provides working capital until the receipt of first half property tax payments at the end of April. During the first four months of each year the *General Fund* expends approximately \$25 million more for payroll and services than is received in revenues. Fund balance provides the necessary cash to finance normal activities without borrowing. Fund balance also provides a reserve for unanticipated emergency expenditures. Finally, fund balance can be used to support subsequent budgets, especially to finance one-time expenditures.

The graph below illustrates the trend in the unreserved fund balance over the past decade. The trend has been mostly positive, providing a fund balance "cushion" to meet the needs referenced above.

Unreserved General Fund Balance



The figure below illustrates the trend in unreserved fund balance as a percent of budget. The county goal is to maintain an unreserved fund balance which is between 5% and 8% of current *General Fund* budget. At the end of 2004 the unreserved fund balance represented 10.6% of the 2004 budget. Approximately \$4.4 million of this fund balance has been budgeted to support the 2005 budget (primarily for one-time items). Should 2005 actual revenues and expenditures occur as budgeted; the unreserved percentage will be reduced to an estimated 8.8% at the end of 2005.

Unreserved General Fund Balance as a Percent of the General Fund Budget

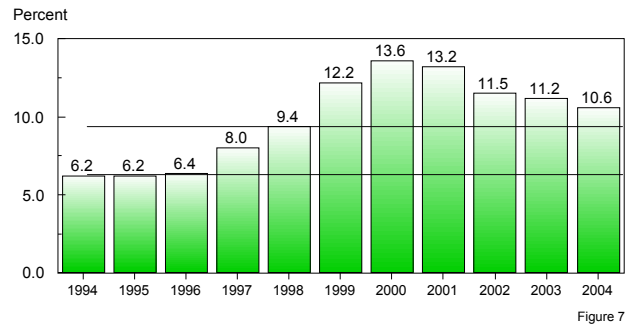


Figure 7

ROADS FUND

The county *Roads Fund* finances the road maintenance, traffic control, general engineering, and general administrative activities for all county roads and bridges. This fund also allocates significant monies (\$20 million in fiscal 2004) to support major road construction and transportation building projects. All these activities totaled \$61 million in fiscal 2004. The major funding sources for these activities are property taxes (\$36.9 million), and gasoline tax revenues from the state (\$9.4 million).

A summary for the last five years of all revenues and other financing sources versus expenditures and other uses follows:

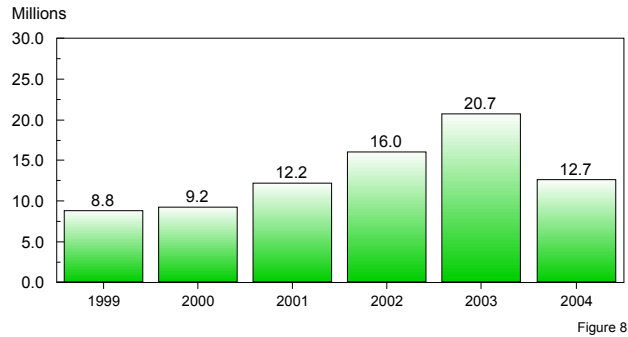
Five Year Summary of Roads Fund Revenues and Expenditures
(in thousands)

	2000	2001	2002	2003	2004
Revenues/Sources	\$ 47,548	\$ 47,346	\$ 48,920	\$ 51,931	\$ 52,947
Expenditures/Uses	47,104	44,291	45,204	48,053	60,952
Revenues/Sources Over (Under) Expenditures/Uses	\$ 444	\$ 3,055	\$ 3,716	\$ 3,878	\$ (8,005)

The large increase in expenditures in 2004 (and hence the “deficit”) was the result of larger than usual allocations to the roads construction funds for road projects, improvements to the road maintenance shop facilities, and a potential new transportation services administration building.

The fund balances for the *Roads Fund* over this time period are shown below. These balances will be used in subsequent years to maintain a solid road maintenance program, and to provide monies for capital improvement projects.

Road Fund Balance

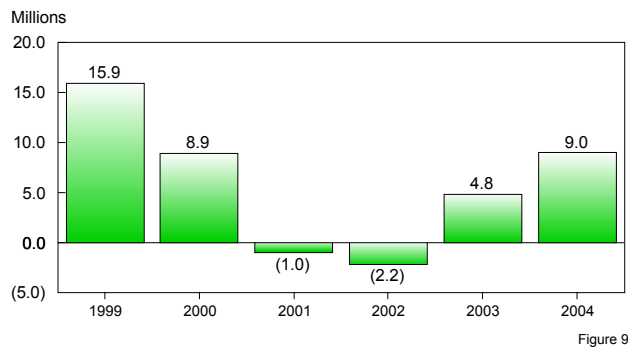


HUMAN SERVICES FUND

The *Human Services Fund* provides financing for the county programs dealing with aging and long-term care, mental health, chemical dependency, and developmental disabilities. The vast majority of the financing is derived from state and federal grants.

As the figures below indicate, we have seen a significant fluctuation in the fiscal status of this fund. This is primarily due to: a) maintaining existing programs and services as federal and state funding levels were decreased (2000-2002); b) the receipt of substantial monies in 2003 from successfully concluded litigation regarding claims previously disallowed by the state; and c) a build-up of stabilization reserves in 2004.

Human Services Fund Balance



SEWER UTILITY FUND

The *Sewer Utility* is by far the county's largest enterprise fund, with total customer accounts of approximately 48,500. The primary source of operating revenue is from service charges collected from residential and commercial customers using wastewater collection and treatment services. Residential customers are billed on a bimonthly basis and commercial customers on a monthly basis. Secondary sources of operating revenue are provided from permit and plan review fees, and from miscellaneous billings.

The financial results for fiscal 2004 and the preceding year are compared below:

Summary of Sewer Utilities Net Assets

	Amount		Increase (Decrease)	
	2004	2003	Amount	Percent
Current and Other Assets	\$ 59,906,426	\$ 61,549,983	\$ (1,643,557)	(2.7) %
Capital Assets	357,745,635	355,671,466	2,074,169	0.6 %
Total Assets	417,652,061	417,221,449	430,612	0.1 %
Long-Term Liabilities	21,275,310	28,560,402	(7,285,092)	(25.5) %
Other Liabilities	7,369,487	7,516,029	(146,542)	(1.9) %
Total Liabilities	28,644,797	36,076,431	(7,431,634)	(20.6) %
Net Assets				
Invested in Capital Assets - Net of Related Debt	333,647,845	324,676,784	8,971,061	2.8 %
Restricted	34,712,163	40,837,808	(6,125,645)	(15.0) %
Unrestricted	20,647,256	15,630,426	5,016,830	32.1 %
Total Net Assets	\$ 389,007,264	\$ 381,145,018	\$ 7,862,246	2.1 %

Summary of Sewer Utilities Revenues, Expenses, and Changes in Net Assets

	Amount		Increase (Decrease)	
	2004	2003	Amount	Percent
Operating Revenues	\$ 25,022,500	\$ 22,790,885	\$ 2,231,615	9.8 %
Nonoperating Revenues	1,399,978	1,331,992	67,986	5.1 %
Total Revenues	26,422,478	24,122,877	2,299,601	9.5 %
Operating Expenses	16,913,185	15,880,896	1,032,289	6.5 %
Depreciation	10,722,030	10,401,739	320,291	3.1 %
Nonoperating Expenses	1,270,423	674,124	596,299	88.5 %
Total Expenses	28,905,638	26,956,759	1,948,879	7.2 %
Loss before transfers, contributions and extraordinary item	(2,483,160)	(2,833,882)	350,722	12.4 %
Transfers	(245,391)	(179,426)	(65,965)	36.8 %
Capital Contributions	10,590,797	7,152,368	3,438,429	48.1 %
Extraordinary Item	-	(2,471,225)	2,471,225	100.0 %
Change in Net Assets	7,862,246	1,667,835	6,194,411	371.4 %
Beginning Net Assets	381,145,018	379,477,183	1,667,835	0.4 %
Ending Net Assets	\$ 389,007,264	\$ 381,145,018	\$ 7,862,246	2.1 %

Financial Highlights

- ✦ Total assets at year end were \$417.7 million and exceeded liabilities of \$28.6 million, yielding total net assets of \$389 million. Total net assets increased by \$7.9 million or 2.1% from last year. Of the total net assets, \$20.6 million was unrestricted and available to support short-term operations or to fund capital improvement projects.
- ✦ The largest portion of the Utility’s net assets (86%) reflects its investment in capital assets (i.e., sewer pipe, buildings, machinery and equipment, etc.), less any related debt.
- ✦ The Utility invested \$32.3 million in the acquisition of property, plant and equipment during the year.
- ✦ The Utility transferred completed projects with a cost of \$31.8 million from construction work in progress during the year. This included completion of the \$25.3 million Spanaway Loop Pump Station Bypass sewer pipeline and the \$3 million Primary and Bioselector Modifications at the Chambers Creek Wastewater Treatment Plant.
- ✦ No new debt was issued. Revenue bond debt was reduced by \$6.9 million, including \$4 million that was called in advance of scheduled maturity dates. Bonds outstanding at year end total \$24.1 million. Of this amount, \$11.1 million is due within the next 5 years.
- ✦ Operating revenues increased by \$2.2 million or 9.8% to \$25 million. The increase for the year reflects the 8.1% rate increase implemented in January 2004 and normal growth in the Utility’s customer base.
- ✦ Operating expenses (excluding depreciation) increased by \$1 million or 6.5% to \$16.9 million. There were moderate increases in salaries and benefits but a higher level of costs for replacement, repairs and maintenance due to the increasing age of utility plant and equipment.
- ✦ Capital contributions increased by \$3.4 million or 48.1% to \$10.6 million, compared to \$7.2 million for 2003. This increase was principally due to strong development activity in the county in 2004, evidenced by a 5.3% increase in customer accounts.

NONMAJOR SPECIAL REVENUE FUNDS (COMBINED)

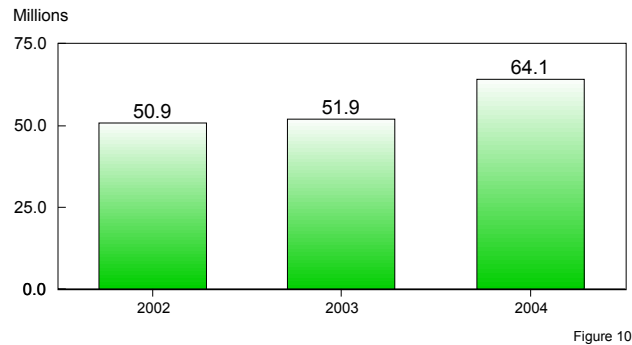
The *Nonmajor Special Revenue Funds* (34 funds) had a positive fiscal year in 2004.

Combined Revenues	\$ 72,149,868
Combined Expenditures	<u>59,316,448</u>
Excess Revenues over Expenditures	\$ 12,833,420
Combined Other Sources (Uses)	<u>(657,155)</u>
Net Change in Fund Balance	<u><u>\$ 12,176,265</u></u>

The largest increases in fund balances occurred in the *Conservation Futures Fund* (\$1.9 million - fewer major land purchases) and the *Second Real Estate Tax Roads Fund* (\$4.4 million – projects in design phase).

The combined fund balances at the end of the last three fiscal years are as show below. A large portion of these balances (\$24.7 million) has been allocated in the 2005 budget, most for one time capital projects.

Non-Major Special Revenue Funds Balance



CAPITAL ASSETS

The county investment in capital assets for governmental and business-type activities totals \$1.055 billion at December 31, 2004. This investment in capital assets includes land, infrastructure, buildings and other improvements, furnishings, equipment, as well as construction in progress. Additional information on *Pierce County* capital assets can be found in Note 5 to the financial statements.

Total capital assets for the county increased by \$42.3 million in fiscal 2004 as follows:

Summary of Capital Asset Activity (in thousands)

Asset Category	Governmental Activities		Business-Type Activities	
	2004 Changes	Ending Asset Values	2004 Changes	Ending Asset Values
Land and Land Rights	\$ 1,462	\$ 85,319	\$ 148	\$ 47,447
Buildings and Systems	4,171	112,338	3,135	88,824
Improvements Other Than Buildings	1,302	3,396	1,237	12,698
Machinery and Equipment	854	60,206	518	41,928
Infrastructure	8,369	313,898	33,079	336,480
Construction In Progress	30,465	208,302	(23,286)	5,634
Avigation Rights	-	-	-	562
Accumulated Depreciation	(7,954)	(113,334)	(11,178)	(148,452)
Total Capital Assets, Net	<u>\$ 38,669</u>	<u>\$ 670,125</u>	<u>\$ 3,653</u>	<u>\$ 385,121</u>

Highlights

- ✦ Most of the increase in capital assets occurred in the governmental activities funds (\$38.7 million).

- ✦ Most of the asset increases for the governmental activities were in construction in progress, with the majority being for the following types of projects (in millions, excluding depreciation): roadways (\$19 million); parks and recreation facility (\$8.5 million); and surface water management improvements (\$4.5 million).
- ✦ Other major increases for governmental activities were for building purchases and infrastructure (mostly road improvements).
- ✦ Conversely, most of the changes in business-type assets reflected the transfer of completed projects from construction in progress to infrastructure for sewer utility related projects.
- ✦ The gross increase in governmental activities capital assets (\$46.6 million) was greatly in excess of related capital asset depreciation (\$7.9 million), while the gross increase in business-type activities capital assets (\$14.8 million) was only slightly higher than related capital asset depreciation (\$11.2 million).

BONDED DEBT ADMINISTRATION

The ratios of net direct tax supported bonded debt to assessed valuation and to population (per capita) present useful indicators of the relative county debt burden. The ratios at December 31, 2004 follow:

	<u>Ratio of Debt To Assessed Valuation</u>	<u>Debt Per Capita</u>
Net Direct Tax Supported Bonded Debt*	0.0010	\$ 67.19

* Defined as Limited and Unlimited General Obligation Bonds net of assets available in *Debt Service Funds* for payment of principal.

Comparable ratios based on assessed valuation and per capita from Standard and Poors Public Finance for 2003 are .70 and \$463.70, respectively, for all other counties. This comparison dramatically illustrates the relatively low debt burden enjoyed by *Pierce County* residents.

A summary of outstanding bond debt is presented below:

Summary of Outstanding Bond Debt (in thousands)

	<u>December 31, 2003</u>	<u>Debt Issued</u>	<u>Debt Retired</u>	<u>December 31, 2004</u>
General Obligation Bonds	\$ 53,532	\$ -	\$ 2,959	\$ 50,573
Sewer Revenue Bonds	31,015	-	6,915	24,100
Total Bond Debt	<u>\$ 84,547</u>	<u>\$ -</u>	<u>\$ 9,874</u>	<u>\$ 74,673</u>

In the next five years, the county will retire 24% of the general obligation bond debt (\$12 million), and 46% of the sewer revenue bond debt (\$11 million). In the next ten years, the retirement amounts are 50%, or \$25 million, and 72%, or \$17 million, respectively.

In July 2004 the county entered into a construction loan agreement with the Washington State Public Works Board to provide financing for 85% of the cost of constructing a new ferry vessel. The maximum amount of the loan is \$7.058 million. The repayment is to be made in 20 equal principal installments at the rate of .5% interest. As of year end the county had drawn \$1.412 million on the loan.

In July 2004 the county issued \$17 million in limited tax general obligation revolving line of credit grant and bond anticipation notes (LOC). The LOC will be used to provide for cash payments during the construction of four specific Parks and Recreation Department projects. At year end, the county had drawn down \$2.215 million on the LOC.

The *Sewer Utility Fund* is required to maintain a revenue bond debt service coverage ratio of 1.25 times the aggregate annual debt service of the utility's bonds outstanding. The revenue bond coverage ratio was 6.93 for 2003 and 2.69 for 2004.

The Moody's Investor Service bond ratings are Aa-3 for *Pierce County* limited tax general obligation bonds and A-1 for its sewer revenue bonds. The Standard & Poor's bond ratings are AA- for both *Pierce County* limited tax general obligation bonds and the sewer revenue bonds. These ratings are exceptionally high for a county and indicate to investors that *Pierce County* bonds are a good investment risk. Additional information on county long-term debt can be found in Note 6 to the financial statements.

REQUEST FOR INFORMATION

This financial report is designed to provide various interested parties with a general overview of county finances and to show the county's accountability for the money it receives. Questions concerning the information provided in this report or requests for additional financial information should be addressed to Pierce County Budget & Finance, 615 South 9th Street, Tacoma, Washington, 98405.

