



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, 2005. 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, an airport, ferry services, and three golf courses.

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	
	2005	2004	2005	2004	2005	2004
Program Revenues:						
Charges for Services	\$ 60,642	\$ 51,948	\$ 35,137	\$ 32,065	\$ 95,779	\$ 84,013
Operating Grants and Contributions	156,041	180,761	642	1,280	156,683	182,041
Capital Grants and Contributions	6,295	11,058	15,320	10,702	21,615	21,760
General Revenues:						
Taxes	221,340	207,922	285	211	221,625	208,133
Interest and Investment Earnings	8,499	7,559	557	213	9,056	7,772
Other General Revenue	1,033	1,675	—	(31)	1,033	1,644
Total Revenues	<u>453,850</u>	<u>460,923</u>	<u>51,941</u>	<u>44,440</u>	<u>505,791</u>	<u>505,363</u>
Expenses:						
General Government	38,424	28,876	—	—	38,424	28,876
Public Safety	118,726	114,093	—	—	118,726	114,093
Physical Environment	31,397	23,891	—	—	31,397	23,891
Transportation	64,561	43,747	—	—	64,561	43,747
Legal and Judicial	61,355	58,402	—	—	61,355	58,402
Economic Environment	18,284	15,927	—	—	18,284	15,927
Health and Human Services	85,742	100,518	—	—	85,742	100,518
Culture and Recreation	10,241	8,738	—	—	10,241	8,738
Interest on Long-Term Debt	1,489	2,791	—	—	1,489	2,791
Sewer Utility	—	—	30,259	27,441	30,259	27,441
Solid Waste Landfill Reserve	—	—	40	—	40	—
Solid Waste Management	—	—	4,204	3,194	4,204	3,194
Airport	—	—	539	476	539	476
Ferry Services	—	—	2,457	2,687	2,457	2,687
Golf Course	—	—	1,766	1,038	1,766	1,038
Water Utility	—	—	92	6	92	6
Total Expenses	<u>430,219</u>	<u>396,983</u>	<u>39,357</u>	<u>34,842</u>	<u>469,576</u>	<u>431,825</u>
Change in Net Assets before Transfers	23,631	63,940	12,584	9,598	36,215	73,538
Transfers	177	(1,513)	(177)	1,513	—	—
Change in Net Assets	<u>23,808</u>	<u>62,427</u>	<u>12,407</u>	<u>11,111</u>	<u>36,215</u>	<u>73,538</u>
Net Assets - Beginning of Year	<u>835,274</u>	<u>772,848</u>	<u>428,916</u>	<u>417,805</u>	<u>1,264,190</u>	<u>1,190,652</u>
Net Assets - End of Year	<u>\$ 859,082</u>	<u>\$ 835,274</u>	<u>\$ 441,323</u>	<u>\$ 428,916</u>	<u>\$ 1,300,405</u>	<u>\$ 1,264,190</u>

Financial Highlights

- ✦ Total Expenses for 2005 totaled approximately \$469.6 million, consisting of \$430.2 million (92%) for governmental activities and \$39.4 (8%) for business-type activities.
- ✦ The increase in Total Expenses was 8.7%, with governmental activities increasing by 8.4% and business type activities by 13.0%.

- ✦ Total Program Revenues for all activities were \$274.1 million and funded approximately 58% of the total expenses for Pierce County. This is well below the 67% from 2004, and was due to a large decline in Human Services and Transportation grant funding. The remaining expenses were financed through general revenues (principally taxes).
- ✦ The most significant change in Expenses was an increase in Transportation (a large contribution of road assets due to a city annexation) and a decrease in Human Services due to grant funding reductions.
- ✦ Governmental activities were funded by program revenues of approximately \$223 million (52%), with general revenues financing the remaining 48% of governmental activities expenses. This represents a 9% decrease in the percentage of expenses paid by program revenues.
- ✦ Business-type activities generated program revenues of approximately \$51.1 million, which exceeded related expenses by \$11.7 million. Most of this positive margin occurred in the *Sewer Utility*.
- ✦ Total government-wide program revenues plus general revenues equaled \$505.8 million and exceeded total government-wide expenses of \$469.6 million. This resulted in government-wide net assets increasing \$36.2 million during fiscal 2005, which is approximately half of the increase in net assets for the prior year.

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

Comparative Statement of Activities
(in thousands)

Governmental Activities	2005				2004
	Expenses	Program Revenues		Net Revenues (Expenses)	Net Revenues (Expenses) <small>(Restated)</small>
		Charges For Services	Grants And Contributions		
Public Safety	\$ 118,725	\$ 5,062	\$ 24,639	\$ (89,024)	\$ (82,920)
Legal and Judicial	61,355	11,836	9,136	(40,383)	(39,101)
Transportation	64,561	1,279	20,497	(42,785)	(18,165)
Health and Human Services	85,742	706	81,716	(3,320)	7,632
All Other Programs	99,836	41,759	26,348	(31,729)	(20,665)
	<u>\$ 430,219</u>	<u>\$ 60,642</u>	<u>\$ 162,336</u>	(207,241)	(153,219)
General Revenues				231,049	215,644
Change in Net Assets				<u>\$ 23,808</u>	<u>\$ 62,425</u>

Business-Type Activities	2005				2004
	Expenses	Program Revenues		Net Revenues (Expenses)	Net Revenues (Expenses)
		Charges For Services	Grants And Contributions		
Sewer Utility	\$ 30,259	\$ 28,479	\$ 13,556	\$ 11,776	\$ 8,172
Solid Waste Management	4,204	2,975	258	(971)	424
Ferry Services	2,458	1,659	2,098	1,299	41
All Other Programs	2,436	2,024	50	(362)	567
	<u>\$ 39,357</u>	<u>\$ 35,137</u>	<u>\$ 15,962</u>	11,742	9,204
General Revenues				665	1,906
Change in Net Assets				<u>\$ 12,407</u>	<u>\$ 11,110</u>

Financial Highlights

- ✦ As would be expected in governmental activities, programs requiring the greatest general revenue support were public safety, and the legal and judicial system (combined support of \$129 million).

- ✦ The gap between total governmental activities expenses and related program revenues increased from \$153.2 million in 2004 to \$207.2 million in 2005. Much of the growth of this funding gap was caused by \$21 million of transportation program expense from several major roadway system annexations and a general decline in grant revenues.
- ✦ However, the county generated a \$23.8 million increase in net assets for governmental activities because general revenues were more than sufficient to cover the remaining funding gap between expense and program revenues.
- ✦ Business-type activities reported a \$12.4 million increase in net assets, which is slightly more than the 2004 increase of \$11.1 million. The major source of the increase was 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	
	2005	2004	2005	2004	2005	2004
Current Assets	\$ 296,199	\$ 286,100	\$ 31,237	\$ 35,613	\$ 327,436	\$ 321,713
Restricted Assets/Joint Ventures	870	599	68,224	46,002	69,094	46,601
Capital Assets	690,459	670,127	401,732	385,123	1,092,191	1,055,250
Total Assets	987,528	956,826	501,193	466,738	1,488,721	1,423,564
Current Liabilities	78,512	69,159	10,690	7,742	89,202	76,901
Noncurrent Liabilities	49,934	52,393	49,180	30,080	99,114	82,473
Total Liabilities	128,446	121,552	59,870	37,822	188,316	159,374
Total Net Assets	\$ 859,082	\$ 835,274	\$ 441,323	\$ 428,916	\$ 1,300,405	\$ 1,264,190

Financial Highlights

- ✦ Approximately \$859.1 million (66%) of total net assets are related to governmental activities, while \$441.3 million (34%) are related to business-type activities. These percentages are unchanged from 2004.
- ✦ As indicated earlier, net assets increased by \$36.2 million in 2005, the majority of which was generated by governmental activities. This is about half of the increase generated in 2004.
- ✦ Capital assets account for approximately 73% of total assets, and 84% of total net assets. The 2004 percentages were similar.
- ✦ Net assets can be further summarized as follows:

Summary of Net Assets (in thousands)

	Governmental Activities		Business-Type Activities		Total	
	2005	2004	2005	2004	2005	2004
Capital Assets (Net of Related Debt)	\$ 632,997	\$ 617,878	\$ 371,875	\$ 357,376	\$ 1,004,872	\$ 975,254
Restricted Net Assets	135,781	128,819	43,327	39,906	179,108	168,725
Unrestricted Net Assets	90,304	88,577	26,121	31,634	116,425	120,211
Total Net Assets	\$ 859,082	\$ 835,274	\$ 441,323	\$ 428,916	\$ 1,300,405	\$ 1,264,190

- ✦ Only 11% of governmental activities net assets are unrestricted, while only 6% of the business-type activities net assets are unrestricted.
- ✦ Unrestricted net assets decreased by \$3.8 million in 2005 due principally to spending for capital assets.

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 \$237.6 million in fiscal 2005, representing only a 1.5% 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)	
	2005	2004	Amount	Percent
Revenue:				
Property and Other Taxes	\$ 100,456	\$ 97,040	\$ 3,416	3.5 %
Sales Tax	49,589	44,722	4,867	10.9 %
Licenses and Permits	8,882	7,109	1,773	24.9 %
Intergovernmental	29,537	37,034	(7,497)	(20.2) %
Charges for Services	33,120	31,447	1,673	5.3 %
Fines and Forfeits	4,665	5,145	(480)	(9.3) %
Interest	7,629	6,971	658	9.4 %
Miscellaneous Revenue	2,061	1,966	95	4.8 %
Total Revenue	235,939	231,434	4,505	1.9 %
Other Financing Sources	1,655	2,609	(954)	(36.6) %
Total Funding Sources	\$ 237,594	\$ 234,043	\$ 3,551	1.5 %

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

- ✦ **Sales Taxes.** The almost 11% increase reflected very strong economic growth in both our cities and the surrounding unincorporated areas.
- ✦ **Licenses and Permits.** The 24.9% increase was due primarily to the continued strong growth in building activity, coupled with Council enacted fee increases.
- ✦ **Intergovernmental.** These revenues reflected a major decrease due to the discontinuance of a large police services contract.
- ✦ **Fines and Forfeits.** The large revenue decline was due to the impact of a recent court case which required new appeal processes prior to losing a license for failure to pay delinquent traffic infractions.
- ✦ **Interest Revenues.** The recent hike in short term interest rates resulted in a significant increase in interest revenues.
- ✦ **Other Financing Sources.** A reduction in timber and land sales caused this revenue decrease.

As illustrated in the graph below, the 1.5% increase in revenue was the lowest percentage growth in the last decade. Two factors are largely responsible for this low growth rate. First, the termination of the aforementioned police services contract by itself resulted in a decline of approximately 4.0%. Were it not for this first factor, the revenue increase in 2005 would have been approximately 5%. Second, property tax revenue growth from existing property is now limited to 1%.

It is likely that revenue increases for the rest of the decade will be below the levels from 1995-2001 due to the continued impact of this voter approved initiative limiting property tax revenue increases to 1%.

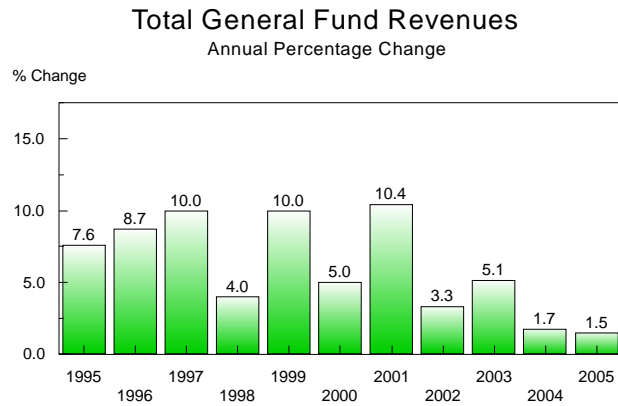


Figure 1

The chart below presents the percentage of 2005 revenue by category for the *General Fund*. The chart illustrates continued dependence on property and sales taxes (a combined 63.2%) as the major revenue sources. During much of the last ten years, the percentage of revenues from such taxes had declined slightly as service charges and intergovernmental revenue percentages have grown. Incorporation of new cities had shifted funding sources from taxes to intergovernmental revenues and service charges resulting from contracts with new cities. However the loss of a major service contract and the strong growth in the local economy have recently increased the relative percentages from these taxes.

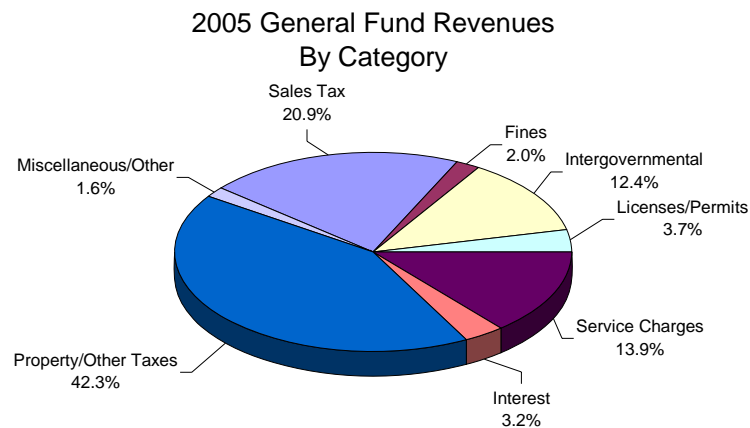


Figure 2

Expenditures. Fiscal 2005 *General Fund* expenditures and transfers out totaled \$237.7 million, representing an increase of \$3 million (1.3%) from 2004. 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)	
	2005	2004	Amount	Percent
General Government	\$ 37,680	\$ 35,142	\$ 2,538	7.2 %
Public Safety	109,673	113,844	(4,171)	(3.7) %
Physical Environment	16,219	14,347	1,872	13.0 %
Legal and Judicial	61,825	58,666	3,159	5.4 %
Mental and Physical Health	3,301	3,246	55	1.7 %
Culture and Recreation	7,356	7,941	(585)	(7.4) %
Economic Environment	1,631	1,535	96	6.3 %
Total Expenditures and Transfers Out	\$ 237,684	\$ 234,721	\$ 2,963	1.3 %

The major changes from last year are explained below:

- ✦ **Public Safety.** This decrease was due to the cancellation of a city police services contract, and the resulting reduction in related staffing and operational expenses.
- ✦ **Physical Environment.** The large increase reflects allocations for additional staffing and professional services to deal with record levels of development plans and permits.
- ✦ **Culture and Recreation.** The large decrease simply reflects the transfer of the grounds maintenance function to an internal service fund operation.

The chart below graphically illustrates relative budget allocations to the various county functional activities. Combined expenditures for public safety, and legal and judicial functions make up 72.1% of total *General Fund* expenditures. This is slightly less than the 2004 percentage of 73.5% due to the aforementioned cancellation of a large city police services contract. The combined percentage for these two major functions would easily exceed 75% if the related general government support costs were all allocated to each department. Similarly, over 80% of the increase in total *General Fund* expenditures over the last ten years occurred in these two major functional areas. This trend of increased spending in these two functional areas is expected to continue into the next few years with increased demand for sheriff services, growing court caseloads, and full operation of the new jail facility.

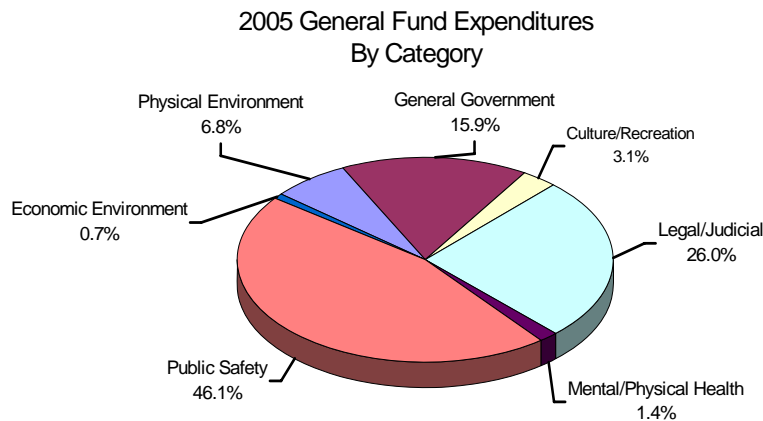
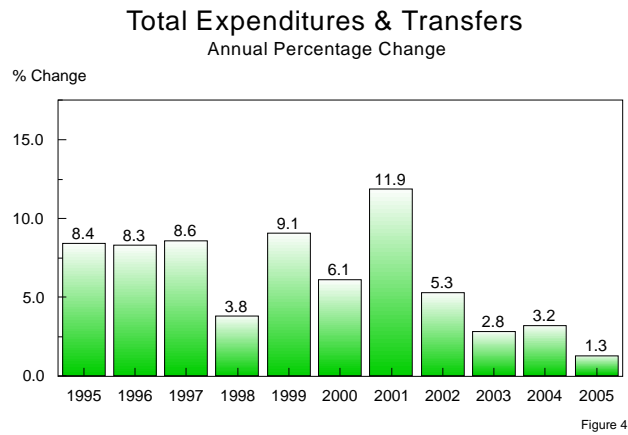


Figure 3

As previously indicated, total 2005 expenditures and transfers increased only 1.3% from 2004 activity. The 2005 percentage increase was the lowest in the last ten years, reflecting the revenue limitations discussed earlier (related to the loss of the city police contract). Corresponding percentage increases from prior years are presented below:

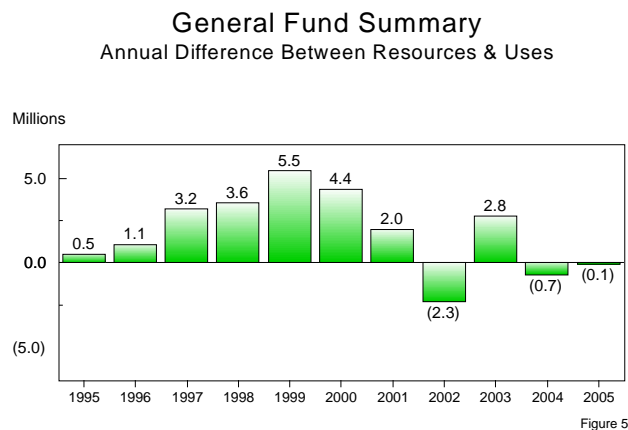


The 2005 "bottom-line" fiscal result for the *General Fund* was essentially "break-even", generating a "deficit" of only \$90,000 summarized as follows:

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

Revenues	\$ 235,939	
Expenditures	<u>226,165</u>	
Excess of Revenues Over Expenditures		\$ 9,774
Other Financing Sources (Uses), Net		<u>(9,864)</u>
Change in Fund Balance		<u><u>\$ (90)</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 2005 and the past ten years. The trend had been quite positive; with Resources exceeding Uses every year from 1995 through 2001. However, three of the last four years have produced negative results, although the "net" result was only a slight decline of \$300,000. And the "deficits" in 2002, 2004 and 2005 mostly resulted from 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 \$233.3 million. Reasons for budget increases of \$6.2 million during the year included the following:

- ✦ 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 specified by the County Council.
- ✦ Increases totaling \$4 million reflecting various grants, service contracts, and reimbursements of election cost, all 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>

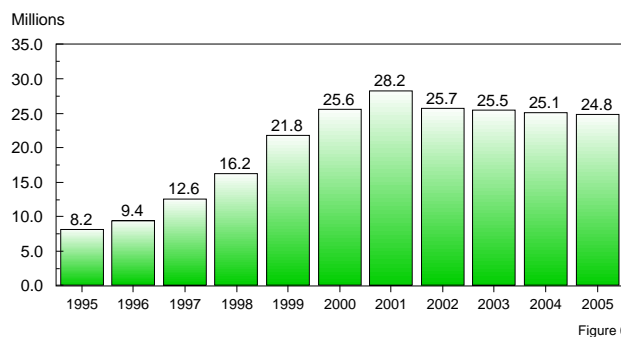
Actual expenditures totaled 99.2% of the final budgeted amounts, and consequently there were no significant variances between the final approved budget and actual expenditures.

General Fund Balance. The unreserved fund balance for the *General Fund* was approximately \$24.8 million at December 31, 2005, reflecting a slight decrease of approximately \$330,000 from 2004. This decrease resulted from the aforementioned operating “deficit” of \$90,000, and an increase in Loan Reserves of \$240,000.

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 \$30 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.

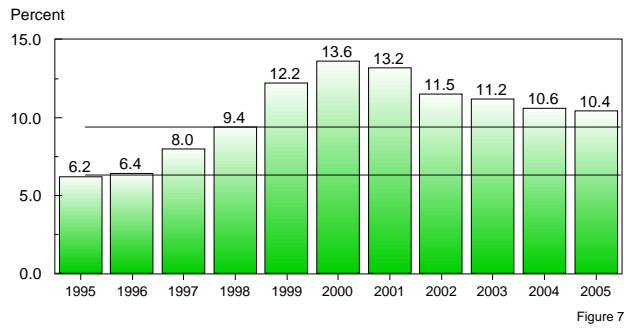
The graph below illustrates the trend in the unreserved fund balance over the past decade. The trend has been mostly positive through 2001, and “steady” thereafter. This level of fund balance has been sufficient to meet the needs referenced above.

Unreserved General Fund Balance



The figure on the following page 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 2005 the unreserved fund balance represented 10.4% of the 2005 budget. Approximately \$5.6 million of this fund balance has been budgeted to support the 2006 budget (primarily for one-time items). Should 2006 actual revenues and expenditures occur as budgeted; the unreserved percentage will be reduced to an estimated 7.7% at the end of 2006.

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



ROADS FUND

The *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 (\$17 million in fiscal 2005) to support major road construction and transportation building projects. All these activities totaled \$56 million in fiscal 2005. The major funding sources for these activities are property taxes (\$38.6 million), and gasoline tax revenues from the state (\$9.6 million).

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

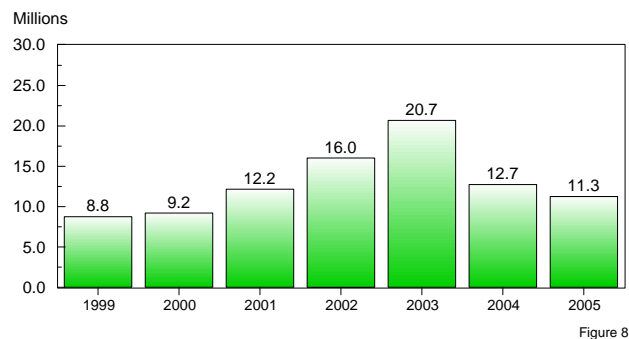
Five Year Summary of Roads Fund Revenues and Expenditures (in thousands)

	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>
Revenues/Sources	\$ 47,346	\$ 48,920	\$ 51,931	\$ 52,947	\$ 54,657
Expenditures/Uses	44,291	45,204	48,053	60,952	56,040
Revenues/Sources Over (Under) Expenditures/Uses	<u>\$ 3,055</u>	<u>\$ 3,716</u>	<u>\$ 3,878</u>	<u>\$ (8,005)</u>	<u>\$ (1,383)</u>

Fiscal 2005 recorded the second straight deficit for this fund, although the deficit was considerably less than that experienced in 2004. Most of this deficit was simply due to large 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* for the last seven years 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

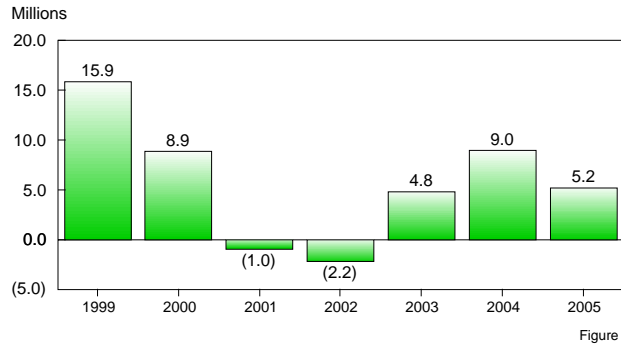


HUMAN SERVICES FUND

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 and the use of a portion of those reserves in 2005.

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 51,300. 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.

A comparison of the components of sewer utility net assets for fiscal 2005 and 2004 follows:

Summary of Sewer Utilities Net Assets
(in thousands)

	Amount		Increase (Decrease)	
	2005	2004	Amount	Percent
Current and Other Assets	\$ 58,397	\$ 59,906	\$ (1,509)	(2.5) %
Capital Assets	367,510	357,746	9,764	2.7 %
Total Assets	425,907	417,652	8,255	2.0 %
Long-Term Liabilities	19,323	21,275	(1,952)	(9.2) %
Other Liabilities	5,760	7,370	(1,610)	(21.8) %
Total Liabilities	25,083	28,645	(3,562)	(12.4) %
Net Assets				
Invested in Capital Assets - Net of Related Debt	347,071	333,648	13,423	4.0 %
Restricted	37,799	34,712	3,087	8.9 %
Unrestricted	15,954	20,647	(4,693)	(22.7) %
Total Net Assets	\$ 400,824	\$ 389,007	\$ 11,817	3.0 %

A comparison of changes in sewer utility net assets for fiscal 2005 and 2004 follows:

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

	Amount		Increase (Decrease)	
	2005	2004	Amount	Percent
Operating Revenues	\$ 26,948	\$ 25,022	\$ 1,926	7.7 %
Nonoperating Revenues	1,950	1,400	550	39.3 %
Total Revenues	<u>28,898</u>	<u>26,422</u>	<u>2,476</u>	9.4 %
Operating Expenses	18,414	16,913	1,501	8.9 %
Depreciation	11,120	10,722	398	3.7 %
Nonoperating Expenses	857	1,270	(413)	(32.5) %
Total Expenses	<u>30,391</u>	<u>28,905</u>	<u>1,486</u>	5.1 %
Loss before transfers, contributions and extraordinary item	(1,493)	(2,483)	990	(39.9) %
Transfers	(247)	(245)	(2)	0.8 %
Capital Contributions	<u>13,557</u>	<u>10,590</u>	<u>2,967</u>	28.0 %
Change in Net Assets	11,817	7,862	3,955	50.3 %
Beginning Net Assets	<u>389,007</u>	<u>381,145</u>	<u>7,862</u>	2.1 %
Ending Net Assets	<u>\$ 400,824</u>	<u>\$ 389,007</u>	<u>\$ 11,817</u>	3.0 %

Financial Highlights:

- ✦ Total assets at year end were \$425.9 million and exceeded liabilities of \$25.1 million, yielding total net assets of \$400.8 million. Total net assets increased by \$11.8 million or 3% from last year. Of the total net assets, \$16 million was unrestricted and available to support short-term operations or to fund capital improvement projects.
- ✦ The Utility invested \$9.2 million in the acquisition of property, plant and equipment during the year.
- ✦ The Utility transferred several completed projects with a cost of \$3.3 million from construction work in progress during the year. The largest of these was the \$2.4 million Northend SCADA (Supervisory Control and Data Acquisition) System project which provides additional remote instrumentation and system control of the Utility's pump stations and collection system.
- ✦ In June 2005, the County issued \$5.4 million in limited tax general obligation refunding bonds which advance refunded \$6.2 million of Sewer Revenue and Refunding Bonds. This advance refunding was undertaken to reduce total debt service payments over the life of the bonds by \$1.3 million, and resulted in an economic gain of \$382,181.
- ✦ Bonds outstanding at year-end total \$20.3 million. Of this amount, \$7.1 million is due within the next four years.
- ✦ Operating revenues increased by \$1.9 million or 7.7% to \$26.9 million. The increase for the year reflects the impact of the 3.1% sewer rate increase implemented in January 2005 and normal growth in the Utility's customer base.
- ✦ Operating expenses (excluding depreciation) increased by \$1.5 million or 8.9% to \$18.4 million. A combination of salary and benefit increases plus higher costs for replacement, repairs and maintenance of aging utility plant and equipment account for this change.
- ✦ Capital contributions increased by \$3 million or 28% to \$13.6 million, compared to \$10.6 million for 2004. This increase was principally due to strong development activity in the county in 2005, evidenced by a 5.7% increase in customer accounts.

NONMAJOR SPECIAL REVENUE FUNDS (COMBINED)

The *Nonmajor Special Revenue Funds* (including 36 funds) had a positive fiscal year in 2005 as follows:

Combined Revenues	\$ 81,317,934
Combined Expenditures	<u>67,463,709</u>
Excess Revenues over Expenditures	13,854,225
Combined Other Sources (Uses)	<u>(4,130,213)</u>
Net Change in Fund Balance	<u><u>\$ 9,724,012</u></u>

The largest increases in fund balances occurred in the *Real Estate Excise Tax River Improvement Fund* (\$1.8 million – delay of a major project) and the *Second Real Estate Tax Roads Fund* (\$2.9 million - projects in design phase).

The combined fund balances for the last four fiscal years are as show below. The major portion of these balances (\$28.9 million) has been allocated in the 2006 budget, most for one-time capital projects.

Non-Major Special Revenue Funds Balance

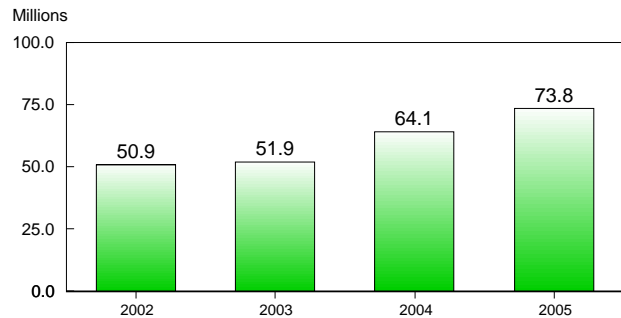


Figure 10

CAPITAL ASSETS

The county investment in capital assets for governmental and business-type activities totals \$1.092 billion at December 31, 2005. 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 \$36.9 million in fiscal 2005 as follows:

Summary of Capital Asset Activity (in thousands)

Asset Category	Governmental Activities		Business-Type Activities	
	2005 Changes	Ending Asset Values	2005 Changes	Ending Asset Values
Land and Land Rights	\$ (1,101)	\$ 84,218	\$ –	\$ 47,447
Buildings and Systems	54,276	166,614	68	88,892
Improvements Other Than Buildings	10,537	13,933	63	12,761
Machinery and Equipment	17,726	77,932	3,492	45,420
Infrastructure	15,979	329,878	5,319	341,799
Construction In Progress	(66,843)	141,460	19,462	25,096
Avigation Rights	–	–	–	562
Accumulated Depreciation	<u>(10,241)</u>	<u>(123,575)</u>	<u>(11,794)</u>	<u>(160,246)</u>
Total Capital Assets, Net	<u><u>\$ 20,333</u></u>	<u><u>\$ 690,459</u></u>	<u><u>\$ 16,610</u></u>	<u><u>\$ 401,732</u></u>

Highlights:

- ✦ Governmental Activities decrease in construction in progress is the result of completing and transferring \$122 million in completed projects, while adding \$55.2 million to new or ongoing construction in progress projects.
- ✦ Of the \$122 million completed and transferred out, \$97.6 million was transferred to other asset classifications in the county (New Jail \$60.2 million, Road Projects \$15.3 million, All Other Projects \$22.1 million), \$3.4 million was expensed for various minor improvements and repairs, and \$21 million of road construction projects was donated to or annexed by other local governments.
- ✦ Completed construction projects accounted for a majority of the increase for governmental activities for buildings and improvements.
- ✦ Most of the change in construction in progress for the business-type activities is due to construction of an eighteen-hole golf course.
- ✦ The gross increase in governmental activities capital assets (\$30.5 million) was greatly in excess of related capital asset depreciation (\$10.2 million), as was the gross increase in business-type activities capital assets (\$28.4 million) compared to related capital asset depreciation (\$11.8 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, 2005 follow:

	Ratio of Debt To Assessed Valuation	Debt Per Capita
Net Direct Tax Supported Bonded Debt*	0.0011	\$ 74.44

* 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 2004 are 0.70 and \$400, 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)

	01-01-05	Debt Issued	Debt Retired	12-31-05
General Obligation Bonds	\$ 50,573	\$ 68,514	\$ 35,455	\$ 83,632
Sewer Revenue Bonds	24,100	-	9,265	14,835
Total Bond Debt	<u>\$ 74,673</u>	<u>\$ 68,514</u>	<u>\$ 44,720</u>	<u>\$ 98,467</u>

In March 2005 the county entered into a construction loan agreement with the Washington State Public Works Board to provide financing for 85% of the cost of improving the intersection of Canyon Road East and 176th Street East. The maximum amount of the loan is \$2.942 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 \$1.324 million on the loan.

During 2005 the county issued two limited tax general obligation bonds. In June \$38.38 million of bonds with an average coupon of 4.20% were issued to refinance \$39.175 million of outstanding bonds with an average coupon of 5.57% and to reduce the total debt service on the refunded bonds by \$4.4 million. In September the county issued \$20.77 million of bonds with an average coupon of 4.30% to construct the Chambers Bay Golf Course. See note 6 for more information.

The county drew \$6.958 million on the limited tax general obligation revolving credit grant and bond anticipation note, 2004 (LOC). The LOC in the amount of \$9.4 million was reclassified to long-term debt at year-end, and was refinanced in February 2006 with a twenty year general obligation bond.

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 2.69 for 2004 and 5.26 for 2005. This increase in coverage was mainly the result of the early call for redemption of \$4 million of revenue bonds in 2004.

In the next five years, the county will retire 32% of the general obligation bond debt (\$26.8 million), and 31% of the sewer revenue bond debt (\$4.6 million). In the next ten years, the retirement amounts are 52%, or \$43.5 million, and 62%, or \$9.2 million, respectively.

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.

