

Traverse City Light and Power

**(A Component Unit of the
City of Traverse City, Michigan)**

Financial Statements

**For the Fiscal Year Ended
June 30, 2017**



Vredeveld Haefner LLC
CPAs and Consultants

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

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Vredeveld Haefner LLC

CPAs and Consultants
10302 20th Avenue
Grand Rapids, MI 49534
Fax (616) 828-0307

Douglas J. Vredeveld, CPA
(616) 446-7474
Peter S. Haefner, CPA
(616) 460-9388

INDEPENDENT AUDITORS' REPORT

December 4, 2017

Honorable Chairman and Members
Traverse City Light and Power Board
Traverse City, Michigan

Report on the Financial Statements

We have audited the accompanying financial statements of Traverse City Light and Power, a Component Unit of the City of Traverse City, Michigan, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise Traverse City Light and Power's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 entity'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 entity'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.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Traverse City Light and Power as of June 30, 2017, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

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 3 through 5 and the information on pages 26 and 27 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 information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Traverse City Light and Power financial statements as a whole. The schedule of capital assets and depreciation and the schedule of revenues and expenses – budget and actual are presented for purposes of additional analysis and are not a required part of the financial statements.

The schedules have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated December 4, 2017 on our consideration of Traverse City Light and Power'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 Traverse City Light and Power's internal control over financial reporting and compliance.

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MANAGEMENT'S DISCUSSION AND ANALYSIS

TRAVERSE CITY LIGHT AND POWER

Management's Discussion and Analysis

As management of the *Traverse City Light and Power* (the "Department"), we offer readers of the Department's financial statements this narrative overview and analysis of the financial activities for the fiscal year ended June 30, 2017. We encourage readers to consider the information presented here in conjunction with additional information that is furnished in the financial statements and notes to the financial statements.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Department's financial statements. The Department's financial statements comprise three components:

1. Financial statements
2. Notes to the financial statements
3. Supplementary information

Financial Statements

A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Department, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The activity of the Department is accounted for in two proprietary funds (Enterprise Funds). The Light and Power Fund and the Fiber Fund, both of which are considered major for reporting purposes.

Enterprise funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing electrical and dark fiber services to customers. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

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

The *Statement of Revenues, Expenses and Changes in Net Position* presents information showing how the Department's net position changed during the most recent fiscal year. All changes in net position 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 only result in cash flows in past or future fiscal periods (for instance, depreciation expense associated with capital assets).

The Department is principally supported by charges for providing electrical and dark fiber services to customers in Traverse City and Townships within the franchise area. The financial statements include only the Department itself. The Department has no legally separate component units for which the Department is financially accountable.

The Department adopts an annual appropriated budget for its funds as required by City Charter. Budgetary comparison schedules have been provided herein to demonstrate compliance with that charter provision.

The Department does not maintain any governmental or fiduciary funds.

Notes to the financial statements. The notes provide additional information that is essential to gain a full understanding of the data provided in the Department’s financial statements.

Supplementary information. In addition to the financial statements and accompanying notes, this report also presents certain *supplementary information*, which includes this management discussion and analysis and schedules following the notes to the financial statements.

The Department’s Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of a government’s financial position. In the case of the Department, assets exceeded liabilities by \$73,797,420 at the close of the most recent fiscal year, June 30, 2017.

The largest portion of net position for the Department is its investment in capital assets (primarily land, construction in progress, buildings, distribution system and equipment). The Department uses these capital assets to provide services to customers. The remaining Department net position is unrestricted and available for Department activity.

Traverse City Light and Power’s Net Position

	June 30	
	2017	2016
Business-type Activities		
Current and other assets	\$28,054,525	\$27,994,499
Capital assets	59,630,827	57,720,452
Total assets	<u>87,685,352</u>	<u>85,714,951</u>
Deferred outflows	<u>3,021,899</u>	<u>3,200,929</u>
Long-term liabilities outstanding	13,126,689	14,316,633
Other liabilities	3,008,930	2,658,477
Total liabilities	<u>16,135,619</u>	<u>16,975,110</u>
Deferred inflows	<u>774,212</u>	<u>-</u>
Net position		
Invested in capital assets	59,630,827	57,720,452
Unrestricted	<u>14,166,593</u>	<u>14,220,318</u>
Total net position	<u>\$73,797,420</u>	<u>\$71,940,770</u>

Traverse City Light and Power’s Changes in Net Position

	June 30	
	2017	2016
Business-type Activities		
Operating revenue	\$34,793,277	\$35,808,549
Operating expenses	(33,258,191)	(34,543,891)
Nonoperating revenue (expense)	<u>321,564</u>	<u>435,971</u>
Increase in net position	1,856,650	1,700,629
Net position – beginning of year	<u>71,940,770</u>	<u>70,240,141</u>
Net position – end of year	<u>\$73,797,420</u>	<u>\$71,940,770</u>

Business-type activities

The overall financial position of the Department remained strong in 2016-2017. There are no outstanding debt obligations except for the commitments through the power supply contracts with Michigan Public Power Agency (“MPPA”) to reimburse MPPA for debt service costs relating to the Campbell, Belle River and Kalkaska generation plants.

Revenue

Overall, the Electric Fund’s revenues were lower than budget by approximately \$2.7M, specifically, operating revenues, because the power cost recovery rate and kwh sales came in lower than what was anticipated. Reimbursements are higher than budgeted because of funds received from City of Traverse City for reimbursement of lighting fixtures relating to the Garland Street Project. Along with other capital costs reimbursed by third parties for conduit installation and storm work assistance for other utilities located in the State of Michigan. The change in fair market value of investments (\$248K) resulted in a decrease this year as a result of the investment portfolio being comprised of bonds and bond prices decreasing due to the current interest rate rise environment.

Expenses

In fiscal year 2016-17, Electric Funds operating expenses was less than budget by approximately \$2.2M. This was primarily attributed to the purchase power cost having a lower price per kWh than what was forecasted and the pension expense coming in higher than expected relating to higher deferred outflows from prior year relating to deferred investment returns, change in experience and change in assumptions.

Capital asset and debt administration

Traverse City Light and Power Capital Assets (net of depreciation)

	June 30	
	2017	2016
Land and land improvements	\$1,079,419	\$1,079,419
Construction in progress	2,098,071	1,384,254
Buildings and improvements	5,668,394	5,383,556
Equipment and distribution system	80,776,953	77,843,218
Accumulated depreciation	(29,992,010)	(27,969,995)
Total	\$59,630,827	\$57,720,452

Additional information about capital assets is provided in Note 3 to the financial statements.

Debt of the Department consists of amounts outstanding for accrued compensated absences. Additional information can be found in Note 4 to the financial statements.

Economic Factors and Next Year’s Budgets and Rates

Overall the budget remains similar to past years. There is a slightly higher anticipated costs relating to purchase power resulting in an increase in sales caused by the flow through variable rate of power service cost recovery.

Requests for Information

This financial report is designed to provide a general overview of the Department's finances. Questions concerning any of the information provided in this report or requests for additional financial information, should be addressed to Karla Myers-Beman, Controller, Traverse City Light and Power, 1131 Hastings Street, Traverse City, MI 49686.

FINANCIAL STATEMENTS

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TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

STATEMENT OF NET POSITION JUNE 30, 2017

ASSETS	<u>Light and Power Fund</u>	<u>Fiber Fund</u>	<u>Business-type Activities Total</u>
Current assets			
Cash and cash equivalents	\$ 5,464,241	\$ 110,228	\$ 5,574,469
Receivables			
Customer, less allowances of \$320,423 for uncollectible accounts (Light and Power Fund)	3,331,749	71,351	3,403,100
Accrued interest	52,656	-	52,656
Taxes	4,806	-	4,806
Other	304,007	-	304,007
Inventories	1,594,578	5,956	1,600,534
Prepaid expenses	92,136	-	92,136
Total current assets	<u>10,844,173</u>	<u>187,535</u>	<u>11,031,708</u>
Non-current assets			
Investments	13,951,707	-	13,951,707
Accounts receivables	1,427,323	-	1,427,323
Other postemployment benefit asset	1,643,502	-	1,643,502
Long-term advances - due from primary government	285	-	285
Land and land improvements	1,079,419	-	1,079,419
Construction in progress	2,098,071	-	2,098,071
Capital assets being depreciated, net	55,019,354	1,433,983	56,453,337
Total non-current assets	<u>75,219,661</u>	<u>1,433,983</u>	<u>76,653,644</u>
Total assets	<u>86,063,834</u>	<u>1,621,518</u>	<u>87,685,352</u>
Deferred outflows			
Deferred outflows of resources - Pensions	3,021,899	-	3,021,899

The accompanying notes are an integral part of these financial statements.

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

STATEMENT OF NET POSITION JUNE 30, 2017

LIABILITIES AND NET POSITION	<u>Light and Power Fund</u>	<u>Fiber Fund</u>	<u>Business-type Activities Total</u>
Current liabilities			
Accounts payable	\$ 2,028,447	\$ 7,190	\$ 2,035,637
Accrued expenses and other liabilities	609,700	8,193	617,893
Customer deposits	97,447	-	97,447
Unearned revenue	-	14,815	14,815
Due to primary government	229,139	13,999	243,138
Total current liabilities	2,964,733	44,197	3,008,930
Long-term liabilities			
Compensated absences	158,415	3,530	161,945
Net pension liability	12,964,744	-	12,964,744
Total liabilities	16,087,892	47,727	16,135,619
Deferred inflows			
Deferred inflows of resources - Pensions	774,212	-	774,212
Net position			
Invested in capital assets	58,196,844	1,433,983	59,630,827
Unrestricted	14,026,785	139,808	14,166,593
Total net position	\$ 72,223,629	\$ 1,573,791	\$ 73,797,420

The accompanying notes are an integral part of these financial statements.

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION FOR THE YEAR ENDED JUNE 30, 2017

	Light and Power Fund	Fiber Fund	Business-type Activities Total
Operating revenues			
Charges for services	\$ 31,165,119	\$ 279,746	\$ 31,444,865
MISO income	3,123,621	-	3,123,621
Other	224,791	-	224,791
Total operating revenues	34,513,531	279,746	34,793,277
Operating expenses			
Generation	22,132,569	-	22,132,569
Distribution	3,800,057	-	3,800,057
Transmission	444,502	-	444,502
Customer accounting	501,210	-	501,210
Public service	466,506	-	466,506
General administration	1,258,665	-	1,258,665
Fiber	-	150,932	150,932
WIFI	-	30,488	30,488
Other	73,530	435	73,965
City fee	1,729,139	13,999	1,743,138
Depreciation	2,511,527	144,630	2,656,157
Total operating expenses	32,917,705	340,484	33,258,189
Operating income (loss)	1,595,826	(60,738)	1,535,088
Nonoperating revenues (expenses)			
Rental income	104,746	-	104,746
Reimbursements	236,776	33,525	270,301
Interest income	204,013	231	204,244
Net decrease in fair value of investments	(247,867)	-	(247,867)
Loss on sale of assets	(5,965)	(3,897)	(9,862)
Total nonoperating revenue	291,703	29,859	321,562
Income before transfers	1,887,529	(30,879)	1,856,650
Transfers			
Transfers in	125,000	-	125,000
Transfers out	-	(125,000)	(125,000)
Total transfers	125,000	(125,000)	-
Change in net position	2,012,529	(155,879)	1,856,650
Net position, beginning of year	70,211,100	1,729,670	71,940,770
Net position, end of year	\$ 72,223,629	\$ 1,573,791	\$ 73,797,420

The accompanying notes are an integral part of these financial statements.

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2017

	Light and Power Fund	Fiber Fund	Business-type Activities Total
Cash flows from operating activities			
Cash received from customers	\$ 34,832,897	\$ 221,280	\$ 35,054,177
Cash payments to employees	(6,068,504)	(130,482)	(6,198,986)
Cash payments to suppliers for goods and services	(22,768,623)	(68,230)	(22,836,853)
Cash payments of City fee	(1,784,900)	(13,932)	(1,798,832)
Net cash provided by operating activities	4,210,870	8,636	4,219,506
Cash flows from noncapital financing activities			
Cash payments from primary government	404	-	404
Cash payments to/from other funds	125,000	(125,000)	-
Customer deposits received	(10,485)	-	(10,485)
Rental income received	104,746	-	104,746
Reimbursements received	236,776	33,525	270,301
Net cash provided by (used in) noncapital financing activities	456,441	(91,475)	364,966
Cash flows from capital and related financing activities			
Proceeds from sale of capital assets	11,087	-	11,087
Purchase of capital assets	(4,571,219)	(16,262)	(4,587,481)
Net cash (used in) capital and related financing activities	(4,560,132)	(16,262)	(4,576,394)
Cash flows from investing activities			
Sale of investments	(3,349,918)	-	(3,349,918)
Interest	185,481	231	185,712
Net cash provided by (used in) investing activities	(3,164,437)	231	(3,164,206)
Net (decrease) in cash and cash equivalents	(3,057,258)	(98,870)	(3,156,128)
Cash and cash equivalents, beginning of year	8,521,499	209,098	8,730,597
Cash and cash equivalents, end of year	\$ 5,464,241	\$ 110,228	\$ 5,574,469

The accompanying notes are an integral part of these financial statements.

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2017

	Light and Power Fund	Fiber Fund	Business-type Activities Total
Cash flows from operating activities			
Operating income (loss)	\$ 1,595,826	\$ (60,738)	\$ 1,535,088
Adjustments to reconcile operating income to net cash provided by operating activities			
Depreciation	2,511,527	144,630	2,656,157
Changes in operating assets and liabilities which provided (used) cash			
Receivables	319,366	(59,011)	260,355
Inventories	(17,918)	-	(17,918)
Prepaid expenses	(77,680)	-	(77,680)
Deferred outflow	169,065	9,965	179,030
Accounts payable	304,149	7,190	311,339
Due to other governments	(55,761)	67	(55,694)
Accrued expenses and other liabilities	101,265	3,483	104,748
Unearned revenue	-	545	545
Compensated absences	(40,745)	932	(39,813)
Net pension liability	(337,492)	(38,427)	(375,919)
Other postemployment benefit asset	(260,732)	-	(260,732)
Net cash provided by operating activities	\$ 4,210,870	\$ 8,636	\$ 4,219,506

Non cash transaction: The cash flow includes the change in fair market value of investments in the amount of \$ (247,867).

The accompanying notes are an integral part of these financial statements.

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Under provisions of the City of Traverse City (the “City”) Charter, the Light and Power Board (the “Board”) was created having jurisdiction and control of *Traverse City Light and Power* (the “Department”). The Board consists of seven members (two of which are City Commissioners) and one ex-officio member (the City Manager). The Department’s annual budget is approved by the City Commission. The Department is required to pay 5% of its gross revenue annually to the City’s General Fund as a city fee. For fiscal 2017, the city fee was \$1,743,138.

Reporting Entity

The Department is a discretely presented component unit of the City because the City appoints the Department’s Board of Directors, it has the ability to significantly influence the Department’s operations and it is financially accountable for the Department as defined under GASB Statement No. 14, *The Financial Reporting Entity*, as amended by GASB Statements 39 and 61. Accordingly, the Department is an integral part of that reporting entity.

As required by generally accepted accounting principles, the financial statements of the reporting entity include those of the Department. There are no component units to be included. The criteria for including a component unit includes significant operational or financial relationships with the Department.

Basis of Accounting

The Department uses the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, the Department considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Investments

Investments are stated at fair value. The change in fair value of the investments from the beginning of the year to the end of the year is reported in the “Nonoperating revenues” section of the Statements of Revenues, Expenses and Changes in Net Position”.

State statutes and City policy authorize the Department to invest in:

- a. Bonds, securities, other obligations and repurchase agreements of the United States or an agency or instrumentality of the United States.
- b. Certificates of deposit, savings accounts, deposit accounts, or depository receipts of a qualified financial institution.

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

NOTES TO FINANCIAL STATEMENTS

- c. Commercial paper rated at the time of purchase within the two highest classifications established by not less than two standard rating services and that matures not more than 270 days after the date of purchase.
- d. Bankers acceptances of United States banks.
- e. Obligations of the State of Michigan and its political subdivisions that at the time of purchase are rated as investment grade by at least one standard rating service.
- f. Mutual funds registered under the Investment Company Act of 1940 with the authority to purchase only investment vehicles that are legal for direct investment by a public corporation.
- g. External investment pools as authorized by Public Act 20, as amended.
- h. Long-term or perpetual trust funds consisting of money and royalties or money derived from oil and gas exploration on property or mineral rights owned by the Department has the same authority to invest the assets as is authorized by Public Act 314, as amended.

Receivables

All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible.

Inventories

Inventories consist of materials to be used in the electric system and are valued at cost (first-in, first-out) not in excess of market. Maintenance and office supplies (immaterial at year end) are charged to expenses upon purchase.

Prepaid Expenses

The Department made payments prior to year-end for services that will be performed in the next fiscal year. In these situations, the Department records an asset to reflect the investment in future services.

Capital assets

Capital assets are defined by the government as assets with an initial individual cost of more than \$2,500 and an estimated useful life in excess of two years.

Capital assets are stated at cost. Depreciation is computed using the straight-line method over the estimated lives of the related assets as follows:

	<u>Years</u>
Transmission and distribution plant	30-50
General plant	10-50

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

NOTES TO FINANCIAL STATEMENTS

Compensated Absences

Compensated absences consist of accumulated unpaid vacation, short-term leave and sick pay. Accumulated unpaid vacation and short-term leave are accrued when earned. Sick pay is frozen for employees but upon death or retirement 50% of accumulated sick leave shall be paid to a maximum of 120 days. Two choices for sick pay cash out are available to employees with more than 30 days of sick leave and 10 years of service. Employees can use sick leave as allowing under the Short-Term Leave Plan or cash out all amounts of sick leave in excess of 30 days up to 120 days at the rate of 50% of employee's current pay rate. Days in excess of 120 will be added to the 30 day bank. This choice must be made as a one-time selection at any time after the employee reaches 10 years of service.

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. The Department has items that qualify for reporting in this category related to the pension plan which is discussed in Note 6.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows or resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Department does not have any items that qualify for reporting in this category.

Pensions

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 the Municipal Employees Retirement System (MERS) of Michigan and additions to/deductions from MERS' fiduciary net position have been determined on the same basis as they are reported by MERS. For this purpose, benefit payments (including refunds or employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Operating Revenue versus Nonoperating Revenue

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 Department are charges to customers for sales and services and "MISO" revenue. Operating expenses for the Department include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

NOTES TO FINANCIAL STATEMENTS

Funds

The Department reports the following major proprietary funds:

The Light and Power Enterprise Fund is used to account for the operations of the Department's electric utility that provides electric service to customers on a user charge basis.

The Fiber Enterprise Fund is used to account for the operations of the Department's fiber optic utility that provides services to customers on a user charge basis and WIFI system located in the downtown area. The Fiber Fund was created in 2008 with an initial capital contribution from the Light and Power Enterprise Fund.

Restricted resources

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

2. CASH DEPOSITS AND INVESTMENTS

The Department's cash and cash equivalents, and investments at June 30, 2017 are composed of the following:

	<u>Cash and cash equivalents</u>	<u>Investments</u>	<u>Totals</u>
Deposits	\$ 5,574,469	\$ 712,325	\$ 6,286,794
Investments	-	13,239,382	13,239,382
Total	\$ 5,574,469	\$ 13,951,707	\$ 19,526,176

Deposits consist of various interest bearing cash accounts and certificates of deposit, held by the City of Traverse City Treasurer. The insured and uninsured bank balances for the Department's deposits are not available as these deposits are held in pools with other City funds.

The Department is authorized by Michigan Public Act 20 of 1943 to invest surplus monies in U.S. bonds and notes, certain commercial paper, mutual funds and investment pools that are composed of authorized investment vehicles.

The Department chooses to disclose its investments by specifically identifying each. As of June 30, 2017, the Department's Michigan CLASS investment and the U.S. Treasury notes are rated by Moody's.

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NOTES TO FINANCIAL STATEMENTS

The Department had the following investments:

<u>Investment</u>	<u>Maturity</u>	<u>Fair Value</u>	<u>Rating</u>
US Treasury Note	02/15/2020	\$ 421,764	AA+
US Treasury Note	06/30/2018	505,235	AA+
US Treasury Note-FHLB	03/23/2020	1,001,100	AA+
US Treasury Note-FHLB	05/17/2021	993,580	AA+
US Treasury Note-FHLB	08/24/2021	991,180	AA+
US Treasury Note-FHLB	12/14/2021	999,560	AA+
US Treasury Note-FHLB	02/28/2022	998,070	AA+
US Treasury Note-FHLB	03/29/2022	993,110	AA+
US Treasury Note-FHLB	06/22/2022	996,080	AA+
US Treasury Note-FHLB	08/24/2028	974,480	AA+
US Treasury Note-FHLB	07/25/2031	945,890	AA+
US Treasury Note-FHLB	08/15/2031	949,310	AA+
US Treasury Note-FHLB	10/12/2022	985,470	AA+
US Treasury Note-FHLB	02/26/2021	498,900	AA+
US Treasury Note-FHLB	04/27/2023	982,590	AA+
Michigan CLASS	NA	<u>3,063</u>	AAAm
		<u>\$ 13,239,382</u>	

Investment and deposit risk

Interest Rate Risk. State law limits the allowable investments and the maturities of some of the allowable investments as identified in Note 1. The Department's investment policy does not have specific limits in excess of state law on investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The maturity dates for each investment are identified above for investments held at year-end.

Credit Risk. State law limits investments to specific government securities, certificates of deposits and bank accounts with qualified financial institutions, commercial paper with specific maximum maturities and ratings when purchased, bankers acceptances of specific financial institutions, qualified mutual funds and qualified external investment pools as identified above. The Department's investment policy does not have specific limits in excess of state law on investment credit risk. The ratings for each investment are identified above for investments held at year end.

Custodial Credit Risk – Deposits. Custodial credit risk is the risk that in the event of a bank failure, the Department's deposits may not be returned. State law does not require and the Department does not have a policy for deposit custodial credit risk. The insured and uninsured bank balances for the Department deposits are not available as these deposits are held in pools with other City funds.

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Custodial Credit Risk – Investments. For investments, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Department will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. State law does not require and the Department does not have a policy for investment custodial credit risk. Of the above \$13,238,382 of investments at June 30, 2017, the Department has a custodial credit risk exposure of \$13,235,319 because the related securities are uninsured, unregistered and held by the government's brokerage firm which is also the counterparty for these particular securities. For MBIA Class, the Department's custodial credit risk exposure cannot be determined because the Department does not own specifically identifiable securities.

Concentration of Credit Risk. State law limits allowable investments but does not limit concentration of credit risk as identified above. The Department's investment policy does not have specific limits in excess of state law on concentration of credit risk. None of the investments held by the Department, excluding government obligations explicitly guaranteed by the U.S. government and mutual fund investments, exceed 5% of the Department's investments.

Fair Value Measurements. The Department categorizes its fair value measurements of investments within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. Investments that are measured at the fair value using the net asset value per share (or its equivalent) as a practical expedient are not classified in the fair value hierarchy below.

The Department has the following recurring fair value measurements as of year end.

- US Treasury Notes are valued using prices quoted in active markets for those securities. (Level 1 inputs)
- The Department holds interests in an external investment pool (MBIA Class) whereby the fair value of the investments are measured on a recurring basis using net asset value per share. (Level 2 inputs)
- The Department does not has any investments that report fair value based on significant unobservable inputs (Level 3 inputs)

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NOTES TO FINANCIAL STATEMENTS

3. CAPITAL ASSETS

At June 30, 2017, capital assets consist of the following:

	<u>Beginning Balance</u>	<u>Additions & Transfers</u>	<u>Deletions & Transfers</u>	<u>Ending Balance</u>
Capital assets not being depreciated				
Land and land improvements	\$ 1,079,419	\$ -	\$ -	\$1,079,419
Construction in progress	<u>1,384,254</u>	<u>4,579,268</u>	<u>3,865,451</u>	<u>2,098,071</u>
Total capital assets not being depreciated	<u>2,463,673</u>	<u>4,579,268</u>	<u>3,865,451</u>	<u>3,177,490</u>
Capital assets being depreciated				
Buildings and improvements	5,383,556	284,838	-	5,668,394
Equipment and distribution system	75,509,586	3,572,564	648,139	78,434,011
Fiber System	1,831,912	16,262	6,952	1,841,222
WiFi System	<u>501,720</u>	<u>-</u>	<u>-</u>	<u>501,720</u>
Total capital assets being depreciated	<u>83,226,774</u>	<u>3,873,664</u>	<u>655,091</u>	<u>86,445,347</u>
Less accumulated depreciation for				
Buildings and improvements	1,651,746	165,827	-	1,817,573
Equipment and distribution system	25,550,865	2,345,700	631,087	27,265,478
Fiber System	692,126	94,458	3,055	783,529
WiFi System	<u>75,258</u>	<u>50,172</u>	<u>-</u>	<u>125,430</u>
Total accumulated depreciation	<u>27,969,995</u>	<u>2,656,157</u>	<u>634,142</u>	<u>29,992,010</u>
Total capital assets being depreciated, net	<u>55,256,779</u>	<u>1,217,507</u>	<u>20,949</u>	<u>56,453,337</u>
Total capital assets, net	<u>\$57,720,452</u>	<u>\$5,796,775</u>	<u>\$3,886,400</u>	<u>\$59,630,827</u>

4. LONG-TERM LIABILITIES

Long-term debt at June 30, 2017, consists of the following:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Accrued compensated absences	<u>\$201,758</u>	<u>\$201,747</u>	<u>\$241,560</u>	<u>\$161,945</u>	<u>\$ -</u>

TRAVERSE CITY LIGHT AND POWER

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NOTES TO FINANCIAL STATEMENTS

5. POWER SUPPLY PURCHASE

The Department, along with other Michigan municipal utilities, is a member of the MPPA. The agency was formed to acquire interest in certain electric generating plants and related transmission lines to service its members. MPPA has acquired a 4.8% undivided interest in the Consumers Energy Campbell 3 plant, an 18.6% undivided interest in the Detroit Edison Belle River project, and 100% undivided interest in the Kalkaska Combustion Turbine project.

In 1983, the Department entered into a 35-year power supply and project support contract with MPPA. Under the agreement, the Department will purchase 26.35% of the energy generated by MPPA's 4.8% interest in the Campbell 3 plant and 4.53% of the energy generated by MPPA's 18.6% interest in the Belle River plant. In 2002, the Department entered into a 25-year power supply and project support contract with MPPA. Under the agreement, the Department will purchase 75.9% of the energy generated by MPPA's 100% interest in the Kalkaska Combustion Turbine. In 2009, the Department entered into a power supply contract with MPPA. Under the agreement, the Department will purchase 8.13% of the energy generated in the MPPA's renewable energy contract with Grainger Electric of Michigan, LLC. In 2011, the Department entered into a power supply contract with MPPA. Under the agreement, the Department will purchase 8.13% of the energy generated in the MPPA's renewable energy contract with Northern American Natural Resources of Michigan. In 2014, the Department entered into an Energy Services Agreement with MPPA for the objective of accessing third party marketers in MISO for the purpose of reducing exposure to MISO markets during volatile seasons. This is accomplished through MPPA soliciting bids and subsequently entering into contracts on behalf of the Department for firm priced energy supply.

For the year ended June 30, 2017, Traverse City Light and Power recognized expenses totaling \$18,570,490 to purchase power under the terms of all contracts with MPPA. The price of the power was calculated on a basis, as specified in the contracts, to enable MPPA to recover its production, transmission and debt service costs.

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NOTES TO FINANCIAL STATEMENTS

Under the terms of the contracts, the Department must make minimum annual payments to cover their share of annual debt service requirements and fixed operation costs of the Campbell 3, Belle River, and Combustion Turbine projects (based on the percentage of power purchased). Future operating costs are estimated based on 2016 costs adjusted for inflation. The total estimated future operating costs, which do not include the annual debt payments, are as follows:

Year Ended December 31	Operating Costs
2018	\$ 7,461,621
2019	5,437,093
2020	5,600,206
2021	5,768,212
2022	5,941,259
2023-2027	17,338,178
	\$ 47,546,569

The estimated total annual debt payments (assuming no early calls or refinancing) are as follows:

Year Ended December 31	Principal	Interest	Total
2018	\$ 3,300,335	\$ 880,189	\$ 4,180,524
2019	2,197,513	739,091	2,936,604
2020	2,276,835	656,765	2,933,600
2021	2,366,383	571,050	2,937,433
2022	2,454,613	481,566	2,936,179
2023-2027	7,893,600	1,222,939	9,116,539
	\$ 20,489,279	\$ 4,551,600	\$ 25,040,879

In December 2009, the Department entered into a 20-year purchase power agreement with Heritage Stony Corners Wind Farm I, LLC to purchase up to 10 megawatts of electric energy and all associated renewable energy credits. For the year ended June 30, 2017, the Department recognized expenses totaling \$3,115,585.

In December 2014, the Department entered into a 20-year purchase power agreement with options to terminate on the 10th and 15th anniversary dates. The Agreement is with Heritage Sustainable Energy, LLC to purchase up to .6 MW of electric energy. For the year ended June 30, 2017, the Department recognized expenses totaling \$27,551.

TRAVERSE CITY LIGHT AND POWER

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NOTES TO FINANCIAL STATEMENTS

6. RETIREMENT PLAN

General Information about the Pension Plan

Plan Description. The employer’s defined benefit pension plan provides certain retirement, disability and death benefits to plan members and beneficiaries. The employer participates in MERS of Michigan. MERS is an agent multiple-employer, statewide public employee pension plan established by the Michigan Legislature under Public Act 135 of 1945 and administered by a nine member Retirement Board. MERS issues a publicly available financial report that includes financial statements and required supplementary information. This report may be obtained accessing the MERS website at www.mersofmich.com.

Benefits Provided

01 - Non Union – Open Division	
	2016 Valuation
Benefit Multiplier:	2.25% Multiplier (80% max)
Normal Retirement Age:	60
Vesting:	10 years
Early Retirement (Unreduced):	55/25
Early Retirement (Reduced):	50/25
	55/15
Final Average Compensation:	5 years
COLA for Current/Future Retirees:	2.50% (Non-Compound)
Member Contributions:	0%
Act 88:	No

10 - Union closed to new hires, linked to Division 12	
	2016 Valuation
Benefit Multiplier:	2.25% Multiplier (80% max)
Normal Retirement Age:	60
Vesting:	6 years
Early Retirement (Unreduced):	50/25
Early Retirement (Reduced):	55/15
Final Average Compensation:	5 years
COLA for Current/Future Retirees:	2.50% (Non-Compound)
Member Contributions:	0%
Act 88:	No

TRAVERSE CITY LIGHT AND POWER

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NOTES TO FINANCIAL STATEMENTS

12 - Union hired after 7/1/2012, linked to Division 10	
	2016 Valuation
Benefit Multiplier:	1.5% Multiplier (no max)
Normal Retirement Age:	60
Vesting:	6 years
Early Retirement (Unreduced):	55/25
Early Retirement (Reduced):	55/15 50/25
Final Average Compensation:	5 years
COLA for Future Retirees:	2.50% (Non-Compound)
Member Contributions:	0%
Act 88:	No

- Benefits provided include plans with multipliers ranging from 1.5 to 2.25.
- Vesting periods range from 6 to 10 years.
- Normal retirement age is 60 with early retirement at 55 and 50 with 25 years of service.
- Final average compensation is calculated based on 5 years.
- There are no member contributions.

Employees covered by benefits terms. At the December 31, 2016 valuation date, the following employees were covered by the benefit terms:

Inactive employees or beneficiaries currently receiving benefits	57
Inactive employees entitled to but not yet receiving benefits	4
Active employees	<u>36</u>
	<u>97</u>

Contributions. The employer is required to contribute amounts at least equal to the actuarially determined rate, as established by the MERS Retirement Board. The actuarially determined rate is the estimated amount necessary to finance the cost of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The employer may establish contribution rates to be paid by its covered employees.

Employer minimum contributions range from 7.39 to 29.14% based on annual payroll for open divisions. One division that is closed to new employees has an annual employer contribution amount of \$57,972.

Net Pension Liability. The employer's Net Pension Liability was measured as of December 31, 2016, and the total pension liability used to calculate the Net Pension Liability was determined by an annual actuarial valuation as of that date.

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NOTES TO FINANCIAL STATEMENTS

Actuarial assumptions. The total pension liability in the December 31, 2016 annual actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation: 2.5%

Salary Increases: 3.75% in the long-term

Investment rate of return: 7.75%, net of administrative and investment expenses, including inflation.

Although no specific price inflation assumptions are needed for the valuation, the 2.5% long-term wage inflation assumption would be consistent with a price inflation of 3-4%.

Mortality rates used were based on RP-2014 Group Annuity Mortality Table of a 50% Male and a 50% Female blend. For disabled retirees, the rates were based on RP-2014 Disable Retiree Mortality Table of a 50% Male and a 50% Female blend.

The actuarial assumptions used in valuation were based on the results of the most recent actuarial experience study in 2015 that covered the period from December 31, 2008 through December 31, 2013.

The long-term expected rate of return on pension plan investments was determined using a model method in which the best-estimate ranges of expected future real rates of return (expected returns, net of investment and administrative expenses and inflation) are developed for each major asset class. These ranges are combined to provide the long-term expected rate of return by weighting the expected future real rates of return of the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Global Equity	57.5%	5.02%
Global Fixed Income	20.0%	2.18%
Real Assets	12.5%	4.23%
Diversifying Strategies	10.0%	6.56%

Discount rate. The discount rate used to measure the total pension liability is 8% for 2016. The projection of cash flows used to determine the discount rate assumes that employer and employee contributions will be made at the rates agreed upon for employees and the actuarially determined rates for employers. Based on these assumptions, the pension plan's fiduciary net position was projected to be available to pay all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

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NOTES TO FINANCIAL STATEMENTS

Changes in Net Pension Liability

Calculating the Net Pension Liability			
Changes in Net Pension Liability	Total Pension Liability (a)	Increase (Decrease) Plan Fiduciary Net Position (b)	
Balances at 12/31/15			Net Pension Liability (a) – (b)
Changes for the Year	\$29,214,897	\$15,100,022	\$14,114,875
Service Cost	300,475	-	300,475
Interest on Total Pension Liability	2,276,465	-	2,276,465
Difference between expected and actual experience	(509,997)	-	(509,997)
Employer Contributions	-	1,564,302	(1,564,302)
Net investment Income	-	1,686,136	(1,686,136)
Benefit payments, including employee refunds	(1,818,642)	(1,818,642)	-
Administrative expense	-	(33,364)	33,364
Net Changes	248,301	1,398,432	(1,150,131)
Balances as of 12/31/16	\$29,463,198	\$16,498,454	\$12,964,744

Sensitivity of the Net Position Liability to changes in the discount rate. The following presents the Net Pension Liability of the employer, calculated using the discount rate of 8.00%, as well as what the employer's Net Pension Liability would be using a discount rate that is 1 percentage point lower (7.00%) or 1% higher (9.00%) than the current rate.

	1% Decrease (7.00%)	Current Discount Rate (8.00%)	1% Increase (9.00%)
Net Pension Liability at 12/31/16	\$12,964,744	\$12,964,744	\$12,964,744
Change in Net Pension Liability (NPL)	3,297,830	-	(2,784,828)
Calculated NPL for your Notes	\$16,262,574	\$12,964,744	\$10,179,916

Note: The current discount rate shown for GASB 68 purposes is higher than the MERS assumed rate of return. This is because for GASB purposes, the discount rate must be gross of administrative expenses, whereas for funding purposes, it is net of administrative expenses.

TRAVERSE CITY LIGHT AND POWER

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NOTES TO FINANCIAL STATEMENTS

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended June 30, 2017 the employer recognized pension expense of \$1,188,382. The employer reported deferred outflows and inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Excess (Deficit) Investment Returns	\$ 1,038,675	\$ (391,714)
Change in Experience	181,918	(382,498)
Change in Assumptions	722,027	-
Contributions subsequent to the measurement date*	1,079,279	-
Total	\$ 3,021,899	\$ (774,212)

*The amount reported as deferred outflows of resources resulting from contributions subsequent to the measurement date will be recognized as a reduction in the Net Pension Liability for the year ending 2017.

Amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended	
2018	\$ 592,260
2019	592,260
2020	81,816
2021	(97,928)
	<u>\$ 1,168,408</u>

7. DEFERRED COMPENSATION

The Department participated in the City's Deferred Compensation Plan created in accordance with the Internal Revenue Code Section 457. The City has ICMA Retirement Corporation and Mass Mutual as administrators for the Plan. Participants may contribute zero to six percent of covered payroll based on the employee's employment or labor union contract. The employer provides for the administrative group a 100% match up to 6% of the employee's gross pay and for the union group contributes 6% if the employee contributes 1.5% to the program. Plan provision and contribution requirements can only be amended by authorization of the Traverse City Light and Power Board. In the current fiscal year, the Department contributed \$156,268 and employees contributed \$218,043.

TRAVERSE CITY LIGHT AND POWER

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NOTES TO FINANCIAL STATEMENTS

8. POSTEMPLOYMENT BENEFITS

In addition to the pension benefits described above, the Department provides postretirement health insurance benefits in accordance with its personnel policies and union agreements. The benefit includes payment of the retirees' premiums until they reach the age of Medicare eligibility. The Department paid \$260,732 for 36 participants in fiscal year 2016-2017.

The Department participates in the City's MERS retiree health funding vehicle that covers substantially all employees. Annual contributions to the Plan are based on actuarial studies performed bi-annually. The Department's required contribution to the Plan for the fiscal year ended June 30, 2017, was \$ 235,720. The postemployment benefit asset for the current year is \$1,643,502. The required disclosures related to the Plan are provided in the City's financial statements.

9. CONTINGENCIES

In the normal course of business, the Department becomes a party in various legal actions and claims, some of which are uninsured. The outcome of these actions and claims is not expected to have a material effect on the financial position of the Department.

A wrongful death suit was filed against the utility in August 2016 and is pending in Grand Traverse County Circuit Court. This case is covered under the Departments insurance policy. Subsequent to year end, the Judge on the case rendered an opinion dismissing the Department from this case.

10. RISK OF LOSS

The Department is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; errors and omission; injuries to employees; and natural disasters. The Department is covered for these losses through the City via the Michigan Municipal Liability and Property Pool, Michigan Municipal Workers Compensation Self Insurance Fund and commercial health insurance. The Department has had no settled claims resulting from these risks that exceeded their coverage in any of the past three years.

11. SUBSEQUENT EVENTS

On July 11, 2017, the Board authorized the execution of an amended and restated purchase power agreement with Heritage Sustainable Energy, LLC adding to purchase the power from a 1MW solar array at the cost of \$.1125 per kwh, comprising of energy cost, capacity credit, and renewable energy credits for a term of 20 years.

On July 11, 2017, the Board authorized the execution of a procurement agreement with Delta Star in the amount of \$1,251,768 for two 12/16/20 MVA transformers to be installed at the Barlow Substation.

TRAVERSE CITY LIGHT AND POWER

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NOTES TO FINANCIAL STATEMENTS

12. DESIGNATIONS OF NET POSITION

The following are designations of net position established by the Board and City Charter:

	<u>June 30, 2017</u>
Emergencies	\$ 100,056
Minimum Cash Reserve	<u>9,667,324</u>
Total	<u>\$ 9,767,380</u>

13. COMMITMENTS

The utility has agreements with the MPPA committing it to purchase of up to 2MW of renewable energy from Granger Electric of Michigan, LLC, .65MW of renewable energy from North American Natural Resources, Inc., and 3.6MW of all energy, capacity, and environmental attributes under the agreement for a development in the thumb area of Michigan. Additionally, through the MPPA Energy Service Committee, the utility has base energy bilateral contracts for the calendar year 2018 through 2021 in the amount of \$5,641,525 and peak energy bilateral contracts for the calendar year 2018 through 2020 in the amount of \$3,013,632 and capacity transaction bilateral contracts for the calendar year 2018 through 2027 in the amount of \$4,364,160.

On May 9, 2017, the Board authorized the execution of a contract for advanced metering infrastructures system from Eaton in the amount of \$3,573,292.

SUPPLEMENTARY INFORMATION

TRAVERSE CITY LIGHT AND POWER

REQUIRED SUPPLEMENTARY INFORMATION
MERS DEFINED BENEFIT PENSION PLAN
SCHEDULE OF CHANGES IN NET PENSION LIABILITY AND RELATED RATIOS
FOR THE YEAR ENDED JUNE 30, 2017

	December 31,		
	2014	2015	2016
Total pension liability			
Service cost	\$ 313,020	\$ 295,317	\$ 300,475
Interest	2,083,781	2,142,935	2,276,465
Differences between expected and actuarial experience	-	363,835	(509,997)
Changes in assumptions	-	1,444,054	-
Benefit payments, including refunds	(1,626,244)	(1,715,604)	(1,818,642)
Other changes	-	(759)	-
Net change in total pension liability	770,557	2,529,778	248,301
Total pension liability, beginning of year	25,914,564	26,685,121	29,214,899
Total pension liability, end of year	26,685,121	29,214,899	29,463,200
Plan fiduciary net position			
Contribution - employer	773,230	858,331	1,564,302
Net investment income	1,000,478	(234,339)	1,686,136
Administrative expenses	(36,578)	(34,767)	(33,363)
Benefit payments, including refunds	(1,626,244)	(1,715,604)	(1,818,642)
Net change in plan fiduciary net position	110,886	(1,126,379)	1,398,433
Plan fiduciary net position, beginning of year	16,115,516	16,226,403	15,100,023
Plan fiduciary net position, end of year	16,226,402	15,100,024	16,498,456
Department's net pension liability	\$ 10,458,719	\$ 14,114,875	\$ 12,964,744
Plan fiduciary net position as a percent of total pension liability	60.81%	51.69%	56.00%
Covered employee payroll	\$ 2,862,491	\$ 2,736,729	\$ 2,728,607
Department's net pension liability as a percent of covered employee payroll	365.37%	515.76%	475.14%

TRAVERSE CITY LIGHT AND POWER

**REQUIRED SUPPLEMENTARY INFORMATION
DEFINED BENEFIT PENSION PLAN
MERS SCHEDULE OF EMPLOYER CONTRIBUTIONS
FOR THE YEAR ENDED JUNE 30, 2017**

	<u>2015</u>	<u>2016</u>	<u>2017</u>
Actual determined contribution	\$ 770,572	\$ 891,939	\$ 944,388
Contribution in relation to the actuarially determined contribution	<u>(770,572)</u>	<u>(891,939)</u>	<u>(2,202,960)</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (1,258,572)</u>
 Covered employee payroll	 \$ 2,880,960	 \$ 2,866,124	 \$ 2,862,491
 Contribution as a percentage of covered employee payroll	 26.75%	 31.12%	 32.99%

Notes to schedule

Actuarial cost method	Entry Age
Amortization method	Level percentage of payroll, open
Remaining amortization period	25 years
Asset valuation method	5 year smoothed (10 year smoothing 2014)
Inflation	2.5% (3.5% 2014)
Salary increases	3.75 to 14.5% (4.50% in 2014)
Investment rate of return	7.75% (8.25% 2014)
Retirement age	Varies depending on plan adoption
Mortality	RP-2014 mortality tables of a 50% Male and 50% Female blend (50% female/50% male 1994 group annuity mortality table 2014)

TRAVERSE CITY LIGHT AND POWER

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SCHEDULE OF CAPITAL ASSETS AND DEPRECIATION (UNAUDITED) LIGHT AND POWER FUND FOR THE YEAR ENDED JUNE 30, 2017

	Capital Assets - Cost			Balance at June 30, 2017
	Balance at June 30, 2016	Additions/ Transfers	Deletions/ Transfers	
Land and land improvements				
Land	\$ 1,073,535	\$ -	\$ -	\$ 1,073,535
Land improvements	5,884	-	-	5,884
Total land and land improvements	1,079,419	-	-	1,079,419
Buildings and improvements				
Distribution plant	5,237,139	284,838	-	5,521,977
Office structures	97,149	-	-	97,149
Other buildings	49,268	-	-	49,268
Total buildings and improvements	5,383,556	284,838	-	5,668,394
Equipment and distribution system				
Union St. Dam	24,010	-	-	24,010
Keystone plant	390	-	-	390
Wind generation unit	20,850	-	-	20,850
Transmission and distribution	74,350,911	3,319,464	648,139	77,022,236
General	1,113,425	253,100	-	1,366,525
Total equipment and distribution system	75,509,586	3,572,564	648,139	78,434,011
Construction in progress	1,384,254	4,561,316	3,847,499	2,098,071
Total	\$ 83,356,815	\$ 8,418,718	\$ 4,495,638	\$ 87,279,895

Balance at June 30, 2016	Accumulated Depreciation		Balance at June 30, 2017	Capital Assets - Net
	Current Depreciation	Deletions		Balance at June 30, 2017
\$ -	\$ -	\$ -	\$ -	\$ 1,073,535
-	-	-	-	5,884
-	-	-	-	1,079,419
1,624,323	162,686	-	1,787,009	3,734,968
12,506	1,226	-	13,732	83,417
14,917	1,915	-	16,832	32,436
1,651,746	165,827	-	1,817,573	3,850,821
23,434	574	-	24,008	2
390	-	-	390	-
1,564	625	-	2,189	18,661
24,956,729	2,228,799	631,087	26,554,441	50,467,795
568,748	115,702	-	684,450	682,075
25,550,865	2,345,700	631,087	27,265,478	51,168,533
-	-	-	-	2,098,071
\$ 27,202,611	\$ 2,511,527	\$ 631,087	\$ 29,083,051	\$ 58,196,844

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

SCHEDULE OF CAPITAL ASSETS AND DEPRECIATION (UNAUDITED) FIBER FUND FOR THE YEAR ENDED JUNE 30, 2017

	Capital Assets - Cost			Balance at June 30, 2017
	Balance at June 30, 2016	Additions/ Transfers	Deletions/ Transfers	
Equipment and distribution system				
Overhead	\$ 1,083,058	\$ -	\$ 6,952	\$ 1,076,106
Underground	282,118	16,262	-	298,380
Termination boxes	365,883	-	-	365,883
Wireless equipment	51,725	-	-	51,725
WIFI system	501,720	-	-	501,720
Other property	49,128	-	-	49,128
Total equipment and distribution system	2,333,632	16,262	6,952	2,342,942
Construction in progress	-	17,952	17,952	-
Total	\$ 2,333,632	\$ 34,214	\$ 24,904	\$ 2,342,942

Balance at June 30, 2016	Accumulated Depreciation		Balance at June 30, 2017	Capital Assets
	Current Depreciation	Deletions		- Net
				Balance at June 30, 2017
\$ 403,284	\$ 54,153	\$ 3,055	\$ 454,382	\$ 621,724
94,683	14,513	-	109,196	189,184
139,961	18,294	-	158,255	207,628
20,688	2,586	-	23,274	28,451
75,258	50,172	-	125,430	376,290
33,510	4,912	-	38,422	10,706
767,384	144,630	3,055	908,959	1,433,983
-	-	-	-	-
\$ 767,384	\$ 144,630	\$ 3,055	\$ 908,959	\$ 1,433,983

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

SCHEDULE OF REVENUES AND EXPENSES - BUDGET AND ACTUAL (UNAUDITED) LIGHT AND POWER FUND FOR THE YEAR ENDED JUNE 30, 2017

	<u>Amended Budget</u>	<u>Actual</u>	<u>Positive (Negative) Variance</u>
Operating revenues - sales			
Residential	\$ 6,375,000	\$ 6,121,779	\$ (253,221)
Commercial	16,150,000	14,832,506	(1,317,494)
Industrial	10,770,000	9,594,935	(1,175,065)
Public authority	315,000	299,780	(15,220)
Street lighting	195,000	209,592	14,592
Yard lights	82,000	106,527	24,527
Total operating revenues - sales	<u>33,887,000</u>	<u>31,165,119</u>	<u>(2,721,881)</u>
Other operating revenues			
Forfeited discounts	70,000	50,712	(19,288)
Merchandise and jobbing	64,200	91,528	27,328
Sale of scrap	35,000	26,911	(8,089)
Recovery of bad debts	200	151	(49)
MISO income	3,000,000	3,123,621	123,621
Miscellaneous	35,500	55,489	19,989
Total other operating revenues	<u>3,204,900</u>	<u>3,348,412</u>	<u>143,512</u>
Nonoperating revenues			
Rental income	40,700	38,880	(1,820)
Pole rental income	36,500	65,866	29,366
Reimbursements	72,000	236,776	164,776
Interest income	170,000	204,013	34,013
Net decrease in fair value of investments	-	(247,867)	(247,867)
Gain/(Loss) on sale of assets	50,000	(5,965)	(55,965)
Total nonoperating revenues	<u>369,200</u>	<u>291,703</u>	<u>(77,497)</u>
Total revenues	<u>37,461,100</u>	<u>34,805,234</u>	<u>(2,655,866)</u>

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

SCHEDULE OF REVENUES AND EXPENSES - BUDGET AND ACTUAL (UNAUDITED) LIGHT AND POWER FUND FOR THE YEAR ENDED JUNE 30, 2017

	<u>Amended Budget</u>	<u>Actual</u>	<u>Positive (Negative) Variance</u>
Generation expense			
Salaries and wages	\$ 152,100	\$ 101,437	\$ 50,663
Payroll taxes and fringes	148,800	195,024	(46,224)
Kalkaska combustion turbine	-	5,613	(5,613)
Purchased power	23,628,000	21,713,626	1,914,374
Trap and transfer	250	-	250
Union street fish ladder	250	-	250
Professional and contractual	110,000	100,384	9,616
Professional development	2,000	175	1,825
Operation supplies	5,200	3,425	1,775
Communications	250	171	79
Safety	3,500	2,415	1,085
Transportation	9,800	6,449	3,351
Equipment rental	17,500	3,820	13,680
Miscellaneous	-	30	(30)
	<u>24,077,650</u>	<u>22,132,569</u>	<u>1,945,081</u>
Total generation expenses			

Continued

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

SCHEDULE OF REVENUES AND EXPENSES - BUDGET AND ACTUAL (UNAUDITED) LIGHT AND POWER FUND FOR THE YEAR ENDED JUNE 30, 2017

	Amended Budget	Actual	Positive (Negative) Variance
Distribution expense			
Salaries and wages	\$ 1,247,000	\$ 1,098,243	\$ 148,757
Payroll taxes and fringes	1,200,650	1,543,663	(343,013)
Substation	119,900	103,743	16,157
Overhead lines	181,000	222,665	(41,665)
Underground lines	40,000	54,830	(14,830)
Storm work	100,000	-	100,000
Electric meters	8,000	2,933	5,067
Street lighting	204,000	212,558	(8,558)
Traffic signals	10,000	4,952	5,048
Plant and structures	96,700	81,830	14,870
Load and dispatching contractual services	30,600	25,991	4,609
Professional services	93,500	84,768	8,732
Professional development	60,000	47,176	12,824
Operation supplies	256,000	192,348	63,652
Utilities	127,000	76,805	50,195
Safety	38,000	29,578	8,422
Transportation	29,000	23,742	5,258
Equipment rental	28,900	(12,567)	41,467
Inventory adjustment	-	(782)	782
Miscellaneous	16,000	7,581	8,419
Total distribution expense	3,886,250	3,800,057	86,193
Transmission expense			
Salaries and wages	283,000	221,728	61,272
Substation	16,000	45,927	(29,927)
Overhead lines	21,000	33,623	(12,623)
MISO	36,000	38,466	(2,466)
Load and dispatching	-	10,259	(10,259)
Equipment rental	1,000	2,242	(1,242)
Inventory adjustment	-	36,968	(36,968)
Miscellaneous	80,000	55,289	24,711
Total transmission expense	437,000	444,502	(7,502)

Continued

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

SCHEDULE OF REVENUES AND EXPENSES - BUDGET AND ACTUAL (UNAUDITED) LIGHT AND POWER FUND FOR THE YEAR ENDED JUNE 30, 2017

	<u>Amended Budget</u>	<u>Actual</u>	<u>Positive (Negative) Variance</u>
Customer accounting expense			
Salaries and wages	\$ 172,800	\$ 149,412	\$ 23,388
Meter reading	91,400	99,238	(7,838)
Payroll taxes and fringes	138,700	158,120	(19,420)
Office supplies	4,150	1,737	2,413
Postage	33,000	16,575	16,425
Stationary and printing	4,000	62	3,938
Professional and contractual	14,000	18,509	(4,509)
Uncollectible accounts	38,000	7,690	30,310
Collection expense	6,000	3,669	2,331
Data processing	25,000	15,890	9,110
Professional development	2,500	1,494	1,006
Transportation	8,500	2,127	6,373
Equipment rental	12,600	19,422	(6,822)
Miscellaneous	8,700	7,265	1,435
Total customer accounting expense	<u>559,350</u>	<u>501,210</u>	<u>58,140</u>
Public service expense			
Salaries and wages	15,100	12,470	2,630
Payroll taxes and fringes	11,100	9,887	1,213
Public service information	459,800	444,149	15,651
Total public service expense	<u>486,000</u>	<u>466,506</u>	<u>19,494</u>

Continued

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

SCHEDULE OF REVENUES AND EXPENSES - BUDGET AND ACTUAL (UNAUDITED) LIGHT AND POWER FUND FOR THE YEAR ENDED JUNE 30, 2017

	<u>Amended Budget</u>	<u>Actual</u>	<u>Positive (Negative) Variance</u>
General administration expense			
Salaries	\$ 521,000	\$ 517,101	\$ 3,899
Payroll taxes and fringes	361,300	462,157	(100,857)
Professional development	25,000	21,890	3,110
Professional and contractual	83,300	73,293	10,007
Office supplies	27,700	35,407	(7,707)
Fees and per diems	81,300	67,260	14,040
Special services	9,000	7,195	1,805
Legal fees	63,200	57,112	6,088
Utilities	3,500	6,452	(2,952)
Printing and publishing	6,000	4,733	1,267
Transportation	1,500	326	1,174
Miscellaneous	5,000	5,739	(739)
Total general administration expense	<u>1,187,800</u>	<u>1,258,665</u>	<u>(70,865)</u>
Other expenses			
Insurance - general	65,500	73,530	(8,030)
City fee	1,870,000	1,729,139	140,861
Depreciation	2,525,000	2,511,527	13,473
Total other expenses	<u>4,460,500</u>	<u>4,314,196</u>	<u>146,304</u>
Total operating expenses	<u>35,094,550</u>	<u>32,917,705</u>	<u>(2,176,845)</u>
Transfers			
Transfer in	175,000	125,000	50,000
Change in net position	<u><u>\$ 2,541,550</u></u>	<u><u>\$ 2,012,529</u></u>	<u><u>\$ (529,021)</u></u>

TRAVERSE CITY LIGHT AND POWER

(A Component Unit of the City of Traverse City, Michigan)

SCHEDULE OF REVENUES AND EXPENSES - BUDGET AND ACTUAL (UNAUDITED) FIBER FUND FOR THE YEAR ENDED JUNE 30, 2017

	Amended Budget	Actual	Positive (Negative) Variance
Operating revenues - sales			
Charges for services	\$ 326,316	\$ 279,746	\$ (46,570)
Non-operating revenues			
Reimbursements	38,400	33,525	(4,875)
Interest income	500	231	(269)
Total non-operating revenues	38,900	33,756	(5,144)
Total revenues	365,216	313,502	(51,714)
Fiber expenses			
Salaries and wages	72,072	56,984	15,088
Payroll taxes and fringes	57,632	49,451	8,181
Operation supplies	1,000	1,273	(273)
Software and hardware	4,000	5,850	(1,850)
Professional and contractual	56,900	26,306	30,594
Professional development	2,500	-	2,500
Transportation	13,000	8,026	4,974
Repair and Maintenance	5,000	2,999	2,001
Miscellaneous	-	43	(43)
Total fiber expenses	212,104	150,932	61,172
WIFI expenses			
Operation and maintenance	32,000	30,488	1,512
Other expenses			
Insurance and bonds	1,400	435	965
City fee	16,400	13,999	2,401
Depreciation	145,000	144,630	370
Total other expenses	162,800	159,064	3,736
Total operating expenses	406,904	340,484	66,420
Nonoperating expense			
Loss on disposal of fixed assets	-	3,897	(3,897)
Transfers			
Transfers out	175,000	125,000	50,000
Change in net position	\$ (216,688)	\$ (155,879)	\$ (164,237)

INTERNAL CONTROL AND COMPLIANCE



Vredeveld Haefner LLC

CPAs and Consultants
10302 20th Avenue
Grand Rapids, MI 49534
Fax (616) 828-0307

Douglas J. Vredeveld, CPA
(616) 446-7474
Peter S. Haefner, CPA
(616) 460-9388

INDEPENDENT AUDITORS' 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

December 4, 2017

Honorable Chairman and Members
Traverse City Light and Power Board
Traverse City, Michigan

We have audited, in accordance with the 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 Traverse City Light and Power, a Component Unit of the City of Traverse City, Michigan, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise Traverse City Light and Power's basic financial statements, and have issued our report thereon dated December 4, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Traverse City Light and Power'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 Traverse City Light and Power's internal control. Accordingly, we do not express an opinion on the effectiveness of Traverse City Light and Power'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 Traverse City Light and Power'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 Traverse City Light and Power's financial statements are free from material misstatement, we performed tests of its 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 Traverse City Light and Power's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Traverse City Light and Power's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Orederold Haefner LLC