

Traverse City Light and Power

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

Financial Statements

**For the Fiscal Year Ended
June 30, 2016**



Vredeveld Haefner LLC

TRAVERSE CITY LIGHT AND POWER

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

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INDEPENDENT AUDITORS' REPORT

December 5, 2016

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, 2016, 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, a Component Unit of the City of Traverse City, Michigan, as of June 30, 2016, 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.

Specializing in services to governmental and nonprofit entities

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 27 and 28 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 5, 2016 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, 2016. 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 approximately \$71,941,000 at the close of the most recent fiscal year, June 30, 2016.

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

Business-type Activities	June 30	
	2016	2015
Current and other assets	\$27,994,499	\$30,693,508
Capital assets	57,720,452	52,251,537
Total assets	85,714,951	82,945,045
Deferred outflows	3,200,929	640,900
Long-term liabilities outstanding	14,316,633	10,612,247
Other liabilities	2,658,477	2,733,557
Total liabilities	16,975,110	13,345,804
Net position		
Invested in capital assets	57,720,452	52,251,537
Unrestricted	14,220,318	17,988,604
Total net position	\$71,940,770	\$70,240,141

Traverse City Light and Power’s Changes in Net Position

Business-type Activities	June 30	
	2016	2015
Operating revenue	\$35,808,549	\$37,399,341
Operating expenses	(34,543,891)	(33,043,681)
Nonoperating revenue (expense)	435,971	412,049
Increase (decrease) in net position	1,700,629	4,767,709
Net position – beginning of year	70,240,141	65,472,432
Net position – end of year	\$71,940,770	\$70,240,141

Business-type activities

The overall financial position of the Department remained strong in 2015-2016. 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 revenues were lower than budget by approximately \$475,000, specifically operating revenues, because the power cost recovery rate came in lower than what was budgeted. MISO income is higher than expected because of the anticipated decline in the capital rate of return did not occur in this fiscal year. FERC recently approved an order reducing the capital rate of return from 12.38% to 10.32% but it is unclear when the commencement date of the reduction will take place. Reimbursements are higher than budgeted because of funds received from State of Michigan for reimbursement of expenses relating to the August 2015 Wind Storm. Loss on sale of assets relates to the utility transferring the coal dock property to the City.

Expenses

In fiscal year 2015-16, operating expenses was less than budget by approximately \$1.0M. 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 negative investment returns for the year.

Capital asset and debt administration

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

	June 30	
	2016	2015
Land and land improvements	\$1,079,419	\$1,395,691
Construction in progress	1,384,254	5,043,136
Buildings and improvements	5,383,556	4,487,246
Equipment and distribution system	77,843,218	67,372,811
Accumulated depreciation	(27,969,995)	(26,047,347)
Total	\$57,720,452	\$52,251,537

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

There is no proposed rate increase for fiscal year 2016-17. The Department has seen an increase in capacity costs as a result of planned coal plants closing due to the age of the plants and the inability to meet EPA emission standards. Power supply costs will impact the Department’s future overall rate increases.

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

TRAVERSE CITY LIGHT AND POWER
(A Component Unit of the City of Traverse City, Michigan)

STATEMENT OF NET POSITION
JUNE 30, 2016

ASSETS	Light and Power Fund	Fiber Fund	Business-type Activities Total
Current assets			
Cash and cash equivalents	\$ 8,521,499	\$ 209,098	\$ 8,730,597
Receivables			
Customer, less allowances of \$319,084			
for uncollectible accounts (Light and Power Fund)	3,162,393	12,340	3,174,733
Accrued interest	34,124	-	34,124
Taxes	14,272	-	14,272
Other	779,495	-	779,495
Inventories	1,576,660	5,956	1,582,616
Prepaid expenses	14,456	-	14,456
Total current assets	14,102,899	227,394	14,330,293
Non-current assets			
Investments	10,849,656	-	10,849,656
Accounts receivables	1,431,091	-	1,431,091
Other postemployment benefit asset	1,382,770	-	1,382,770
Long-term advances - due from primary government	689	-	689
Land and land improvements	1,079,419	-	1,079,419
Construction in progress	1,384,254	-	1,384,254
Capital assets being depreciated, net	53,690,531	1,566,248	55,256,779
Total non-current assets	69,818,410	1,566,248	71,384,658
Total assets	83,921,309	1,793,642	85,714,951
Deferred outflows			
Deferred outflows of resources - Pensions	3,190,964	9,965	3,200,929

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, 2016

LIABILITIES AND NET POSITION	<u>Light and Power Fund</u>	<u>Fiber Fund</u>	<u>Business-type Activities Total</u>
Current liabilities			
Accounts payable	\$ 1,724,298	\$ 3,614	\$ 1,727,912
Accrued expenses and other liabilities	508,435	1,096	509,531
Customer deposits	107,932	-	107,932
Unearned revenue	-	14,270	14,270
Due to primary government	284,900	13,932	298,832
Total current liabilities	2,625,565	32,912	2,658,477
Long-term liabilities			
Compensated absences	199,160	2,598	201,758
Net pension liability	14,076,448	38,427	14,114,875
Total liabilities	16,901,173	73,937	16,975,110
Net position			
Invested in capital assets	56,154,204	1,566,248	57,720,452
Unrestricted	14,056,896	163,422	14,220,318
Total net position	\$ 70,211,100	\$ 1,729,670	\$ 71,940,770

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, 2016

	Light and Power Fund	Fiber Fund	Business-type Activities Total
Operating revenues			
Charges for services	\$ 31,666,113	\$ 278,376	\$ 31,944,489
MISO income	3,483,052	-	3,483,052
Other	380,879	129	381,008
Total operating revenues	35,530,044	278,505	35,808,549
Operating expenses			
Generation	23,070,005	-	23,070,005
Distribution	4,424,951	-	4,424,951
Transmission	421,135	-	421,135
Customer accounting	577,278	-	577,278
Public service	671,545	-	671,545
General administration	986,037	-	986,037
Fiber	-	105,858	105,858
WIFI	-	28,678	28,678
Other	62,001	-	62,001
City fee	1,784,900	13,932	1,798,832
Depreciation	2,254,188	143,383	2,397,571
Total operating expenses	34,252,040	291,851	34,543,891
Operating income (loss)	1,278,004	(13,346)	1,264,658
Nonoperating revenues (expenses)			
Rental income	93,247	-	93,247
Reimbursements	296,244	54,127	350,371
Interest income	288,991	125	289,116
Change in fair value of investments	59,202	-	59,202
Loss on sale of assets	(355,965)	-	(355,965)
Total nonoperating revenue	381,719	54,252	435,971
Income before transfers	1,659,723	40,906	1,700,629
Transfers			
Transfers in	175,000	-	175,000
Transfers out	-	(175,000)	(175,000)
Total transfers	175,000	(175,000)	-
Change in net position	1,834,723	(134,094)	1,700,629
Net position, beginning of year	68,376,377	1,863,764	70,240,141
Net position, end of year	\$ 70,211,100	\$ 1,729,670	\$ 71,940,770

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, 2016

	Light and Power Fund	Fiber Fund	Business-type Activities Total
Cash flows from operating activities			
Cash received from customers	\$ 34,462,306	\$ 546,463	\$ 35,008,769
Cash payments to employees	(3,426,762)	(74,164)	(3,500,926)
Cash payments to suppliers for goods and services	(25,689,043)	(81,519)	(25,770,562)
Cash payments of City fee	(1,863,259)	(12,788)	(1,876,047)
Net cash provided by operating activities	3,483,242	377,992	3,861,234
Cash flows from noncapital financing activities			
Cash payments from primary government	2,311	-	2,311
Cash payments to/from other funds	194,441	(194,441)	-
Customer deposits received	9,546	-	9,546
Rental income received	93,247	-	93,247
Reimbursements received	296,244	54,127	350,371
Net cash provided by (used in) noncapital financing activities	595,789	(140,314)	455,475
Cash flows from capital and related financing activities			
Proceeds from sale of capital assets	907	-	907
Proceeds from sale of assets held for sale	980,900	-	980,900
Purchase of capital assets	(8,372,838)	(28,705)	(8,401,543)
Net cash (used in) capital and related financing activities	(7,391,031)	(28,705)	(7,419,736)
Cash flows from investing activities			
Sale of investments	2,311,544	-	2,311,544
Interest	423,952	125	424,077
Net cash provided by investing activities	2,735,496	125	2,735,621
Net increase (decrease) in cash and cash equivalents	(576,504)	209,098	(367,406)
Cash and cash equivalents, beginning of year	9,098,003	-	9,098,003
Cash and cash equivalents, end of year	\$ 8,521,499	\$ 209,098	\$ 8,730,597

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, 2016

	Light and Power Fund	Fiber Fund	Business-type Activities Total
Cash flows from operating activities			
Operating income (loss)	\$ 1,278,004	\$ (13,346)	\$ 1,264,658
Adjustments to reconcile operating income to net cash provided by operating activities			
Depreciation	2,254,188	143,383	2,397,571
Changes in operating assets and liabilities which provided (used) cash			
Receivables	(1,072,082)	267,958	(804,124)
Inventories	153,836	-	153,836
Prepaid expenses	3,352	-	3,352
Deferred outflow	(2,551,650)	(8,379)	(2,560,029)
Accounts payable	(228,018)	(26,665)	(254,683)
Due to other governments	(78,359)	1,144	(77,215)
Accrued expenses and other liabilities	289,788	645	290,433
Unearned revenue	(20,570)	-	(20,570)
Compensated absences	43,490	1,590	45,080
Net pension liability	3,644,494	11,662	3,656,156
Other postemployment benefit asset	(233,231)	-	(233,231)
Net cash provided by operating activities	\$ 3,483,242	\$ 377,992	\$ 3,861,234

Non cash transaction: The cash flow includes the change in fair market value of investments in the amount of \$(18,196).

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 2016, the city fee was \$1,798,832.

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 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, 2016 are composed of the following:

	<u>Cash and cash equivalents</u>	<u>Investments</u>	<u>Totals</u>
Deposits	\$ 8,730,597	\$ 2,461,168	\$ 11,191,765
Investments	-	8,388,488	8,388,488
Total	\$ 8,730,597	\$ 10,849,656	\$ 19,580,253

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, 2016, the Department's Michigan CLASS investment and the U.S. Treasury notes are rated by Moody's. The Department had the following investments:

TRAVERSE CITY LIGHT AND POWER

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

NOTES TO FINANCIAL STATEMENTS

<u>Investment</u>	<u>Maturity</u>	<u>Fair Value</u>	<u>Rating</u>
US Treasury Note	02/26/2021	\$ 500,105	AA+
US Treasury Note	12/31/2016	912,681	AA+
US Treasury Note	06/30/2018	517,560	AA+
US Treasury Note	02/15/2020	440,156	AA+
US Treasury Note	03/23/2020	1,000,980	AA+
US Treasury Note	10/29/2020	1,000,290	AA+
US Treasury Note	01/29/2021	1,000,190	AA+
US Treasury Note	05/17/2021	1,002,990	AA+
US Treasury Note	10/29/2027	1,000,120	AA+
US Treasury Note	04/27/2023	1,004,240	AA+
MPPA Investments Pool	Various	6,139	Unrated
Michigan CLASS	NA	3,037	AAAm
		<u>\$ 8,388,488</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.

TRAVERSE CITY LIGHT AND POWER

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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 \$8,388,488 of investments at June 30, 2016, the Department has a custodial credit risk exposure of \$8,379,312 because the related securities are uninsured, unregistered and held by the government’s brokerage firm which is also the counterparty for these particular securities. Of the above investment pools 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.
- MPPA Investment Pool investments are valued using a pricing model utilizing observable fair value measures of pool investments and other observable inputs to determining the fair value of the securities making up the investments pool.
- The Department does not have any investments that report fair value based on significant unobservable inputs (Level 3 Inputs)

Investments in Entities that Calculate Net Asset Value per Share

The Department holds interests in an external investment pool whereby the fair value of the investments are measured on a recurring basis using net asset value per share.

	Fair Value	Unfunded Commitments	Redemption Frequency, if Eligible	Redemption Notice Period
Michigan Class	\$ 3,037	\$ -	-	-

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NOTES TO FINANCIAL STATEMENTS

3. CAPITAL ASSETS

At June 30, 2016, 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	\$ 1,395,691	\$ 7,970	\$ 324,242	\$ 1,079,419
Construction in progress	<u>5,043,136</u>	<u>6,901,079</u>	<u>10,559,961</u>	<u>1,384,254</u>
Total capital assets not being depreciated	<u>6,438,827</u>	<u>6,909,049</u>	<u>10,884,203</u>	<u>2,463,673</u>
Capital assets being depreciated				
Buildings and improvements	4,487,246	896,310	-	5,383,556
Equipment and distribution system	65,067,884	11,127,440	685,738	75,509,586
Fiber System	1,803,207	28,705	-	1,831,912
WiFi System	<u>501,720</u>	<u>-</u>	<u>-</u>	<u>501,720</u>
Total capital assets being depreciated	<u>71,860,057</u>	<u>12,052,455</u>	<u>685,738</u>	<u>83,226,774</u>
Less accumulated depreciation for				
buildings and improvements	1,503,543	148,203	-	1,651,746
Equipment and distribution system	23,919,803	2,156,767	525,705	25,550,865
Fiber System	598,915	93,211	-	692,126
WiFi System	<u>25,086</u>	<u>50,172</u>	<u>-</u>	<u>75,258</u>
Total accumulated depreciation	<u>26,047,347</u>	<u>2,448,353</u>	<u>525,705</u>	<u>27,969,995</u>
Total capital assets being depreciated, net	<u>45,812,710</u>	<u>9,604,102</u>	<u>160,033</u>	<u>55,256,779</u>
Total capital assets, net	<u>\$52,251,537</u>	<u>\$16,513,151</u>	<u>\$ 11,044,236</u>	<u>\$57,720,452</u>

4. LONG-TERM LIABILITIES

Long-term debt at June 30, 2016, 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>\$156,678</u>	<u>\$ 255,792</u>	<u>\$210,712</u>	<u>\$201,758</u>	<u>\$ -</u>

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NOTES TO FINANCIAL STATEMENTS

5. POWER SUPPLY PURCHASE

In September 2010, the Department entered into two 5-year agreements with the Lansing Board of Water & Light (“LBWL”) to commence January 1, 2011. The purchase power agreement allows for the purchase of a minimum of 10 megawatts of electric energy up to a maximum of 45 megawatts to replace its deficient energy needs from the expired agreement with Michigan Public Power Agency (“MPPA”) power pool. The energy service agency agreement provides for LBWL to act as the Department’s agent with Midcontinent Independent System Operator (“MISO”). LBWL will enter into third party contracts to purchase energy and sell surplus energy into the MISO daily and hourly markets. For the year ended June 30, 2016, the Department recognized expenses totaling \$3,012,175. The contracts were terminated as of December 31, 2015.

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 market 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 during more volatile months.

For the year ended June 30, 2016, Traverse City Light and Power recognized expenses totaling \$16,647,070 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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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 2015 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
2017	\$ 7,932,029
2018	8,169,990
2019	6,062,606
2020	6,244,484
2021	6,431,849
2022-2026	20,533,196
2027	3,741,742
	\$59,115,896

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

Year Ended December 31	Principal	Interest	Total
2017	\$ 3,160,421	\$ 1,020,444	\$ 4,180,865
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
2022-2026	8,610,103	1,617,600	10,227,703
2027	1,738,110	86,906	1,825,016
	\$ 23,649,700	\$ 5,572,045	\$ 29,221,745

The MPPA and its member utilities were over-charged on their power sales contract agreements by Detroit Edison. Because of this, MPPA and the member utilities have established a trust fund (“The Municipal Competitive Trust”). Specific policies have been established by each member regarding the use of these funds. The Department’s share of this trust fund was \$6,139 as of June 30, 2016.

In December 2009, the Department entered into a 20-year purchase power agreement with Heritage Stoney 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, 2016, the Department recognized expenses totaling \$2,940,041.

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, 2016, the Department recognized expenses totaling \$35,056.

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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	
	2015 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	
	2015 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

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NOTES TO FINANCIAL STATEMENTS

12 - Union hired after 7/1/2012, linked to Division 10	
	2015 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 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, 2015 valuation date, the following employees were covered by the benefit terms:

Inactive employees or beneficiaries currently receiving benefits	55
Inactive employees entitled to but not yet receiving benefits	6
Active employees	<u>34</u>
	<u>95</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 contributions range from 7.31 to 35.88% based on annual payroll for open divisions. One division that is closed to new employees has an annual employer contribution amount of \$73,328.

Net Pension Liability. The employer's Net Pension Liability was measured as of December 31, 2015, and the total pension liability used to calculate the Net Pension Liability was determined by an annual actuarial valuation as of that date.

Actuarial assumptions. The total pension liability in the December 31, 2015 annual actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

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NOTES TO FINANCIAL STATEMENTS

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 2015. 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)	Net Pension Liability (a) – (b)
Balances at 12/31/14			
Changes for the Year	\$26,685,121	\$16,226,402	\$10,458,719
Service Cost	295,317	-	295,317
Interest on Total Pension Liability	2,142,936	-	2,142,936
Difference between expected and actual experience	363,835	-	363,835
Change in Assumptions	1,444,054	-	1,444,054
Employer Contributions	-	858,331	(858,331)
Net investment Income	-	(234,339)	234,339
Benefit payments, including employee refunds	(1,715,605)	(1,715,605)	-
Administrative expense	-	(34,767)	34,767
Other Changes	(761)	-	(761)
Net Changes	2,529,776	(1,126,380)	3,656,156
Balances as of 12/31/15	\$29,214,897	\$15,100,022	\$14,114,875

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%)
<u>Net Pension Liability at 12/31/15</u>	\$ 14,114,875	\$ 14,114,875	\$14,114,875
Change in Net Pension Liability (NPL)	3,370,807	-	(2,838,760)
Calculated NPL for your Notes	\$17,485,682	\$14,114,875	\$11,276,115

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.

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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, 2016 the employer recognized pension expense of \$1,988,826. 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	\$ 1,404,390	\$ -
Change in Experience	\$ 272,876	\$ -
Change in Assumptions	\$ 1,083,036	\$ -
Contributions subsequent to the measurement date*	\$ 440,627	\$ -
Total	\$ 3,200,929	\$ -

*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 2016.

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

Year ended	
2017	\$ 817,688
2018	817,688
2019	817,688
2020	<u>307,238</u>
	\$ 2,760,302

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 employees' 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 \$155,230 and employees contributed \$210,026.

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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 \$181,622 for 36 participants in fiscal year 2015-2016.

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, 2016, was \$235,760. The postemployment benefit asset for the current year is \$1,382,770. 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.

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. DESIGNATIONS OF NET POSITION

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

	<u>June 30, 2016</u>
Emergencies	\$ 100,056
Minimum Cash Reserve	<u>9,700,000</u>
Total	<u>\$ 9,800,056</u>

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NOTES TO FINANCIAL STATEMENTS

12. GASB PRONOUNCEMENTS

In June 2015, the GASB issued two new standards addressing accounting and financial reporting by state and local governments for postemployment benefits other than pensions (OPEB). GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, addresses reporting by OPEB plans whereas GASB No.75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, addresses accounting and reporting by employer governments that provide OPEB benefits to their employees. Along with the currently required statement of fiduciary net position and statement of changes in fiduciary net position, OPEB plans will now be required to include in the financial statements more extensive footnote disclosures and required supplemental information related to the measurement of the OPEB liabilities for which assets have been accumulated. In addition, the City will, after adoption of GASB Statement No. 75, recognize on the face of the financial statements its net OPEB liability. The City is currently evaluating the impact these standards will have on the financial statements when adopted. GASB Statement No. 74 is effective for fiscal years beginning after June 15, 2016 whereas GASB Statement No. 75 is effective one year later.

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 2017 through 2020 in the amount of \$6,811,464 and peak energy bilateral contracts for the calendar year 2017 through 2020 in the amount of \$2,514,237 and capacity transaction bilateral contracts for the calendar year 2017 through 2024 in the amount of \$3,982,080.

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, 2016

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

TRAVERSE CITY LIGHT AND POWER

**REQUIRED SUPPLEMENTARY INFORMATION
DEFINED BENEFIT PENSION PLAN
MERS SCHEDULE OF EMPLOYER CONTRIBUTIONS
FOR THE YEAR ENDED JUNE 30, 2016**

	2015	2016
Actual determined contribution	\$ 770,572	\$ 891,939
Contribution in relation to the actuarially determined contribution	(770,572)	(891,939)
Contribution deficiency (excess)	\$ -	\$ -
 Covered employee payroll	 \$ 2,880,960	 \$ 2,866,124
 Contribution as a percentage of covered employee payroll	 26.75%	 31.12%

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)

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SCHEDULE OF CAPITAL ASSETS AND DEPRECIATION (UNAUDITED) LIGHT AND POWER FUND FOR THE YEAR ENDED JUNE 30, 2016

	Capital Assets - Cost			Balance at June 30, 2016
	Balance at June 30, 2015	Additions/ Transfers	Deletions/ Transfers	
Land and land improvements				
Land	\$ 1,065,565	\$ 7,970	\$ -	\$ 1,073,535
Land - coal dock	248,023	-	248,023	-
Land improvements	82,103	-	76,219	5,884
Total land and land improvements	1,395,691	7,970	324,242	1,079,419
Buildings and improvements				
Distribution plant	4,340,829	896,310	-	5,237,139
Office structures	97,149	-	-	97,149
Other buildings	49,268	-	-	49,268
Total buildings and improvements	4,487,246	896,310	-	5,383,556
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	63,993,916	11,042,733	685,738	74,350,911
General	1,028,718	84,707	-	1,113,425
Total equipment and distribution system	65,067,884	11,127,440	685,738	75,509,586
Construction in progress	5,043,136	6,901,079	10,559,961	1,384,254
Total	\$ 75,993,957	\$ 18,932,799	\$ 11,569,941	\$ 83,356,815

Balance at June 30, 2015	Accumulated Depreciation		Balance at June 30, 2016	Capital Assets - Net
	Current Depreciation	Deletions		Balance at June 30, 2016
\$ -	\$ -	\$ -	\$ -	\$ 1,073,535
-	-	-	-	-
-	-	-	-	5,884
-	-	-	-	1,079,419
1,479,116	145,207	-	1,624,323	3,612,816
11,280	1,226	-	12,506	84,643
13,147	1,770	-	14,917	34,351
1,503,543	148,203	-	1,651,746	3,731,810
22,745	689	-	23,434	576
385	5	-	390	-
939	625	-	1,564	19,286
23,446,712	2,035,722	525,705	24,956,729	49,394,182
449,022	119,726	-	568,748	544,677
23,919,803	2,156,767	525,705	25,550,865	49,958,721
-	-	-	-	1,384,254
\$ 25,423,346	\$ 2,304,970	\$ 525,705	\$ 27,202,611	\$ 56,154,204

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, 2016**

	Capital Assets - Cost			Balance at June 30, 2016
	Balance at June 30, 2015	Additions/ Transfers	Deletions/ Transfers	
Equipment and distribution system				
Overhead	\$ 1,083,058	\$ -	\$ -	\$ 1,083,058
Underground	258,363	23,755	-	282,118
Termination boxes	365,883	-	-	365,883
Wireless equipment	51,725	-	-	51,725
WIFI system	501,720	-	-	501,720
Other property	44,178	4,950	-	49,128
Total equipment and distribution system	2,304,927	28,705	-	2,333,632
Construction in progress	-	13,241	13,241	-
Total	\$ 2,304,927	\$ 41,946	\$ 13,241	\$ 2,333,632

Balance at June 30, 2015	Accumulated Depreciation		Balance at June 30, 2016	Capital Assets
	Current Depreciation	Deletions		- Net Balance at June 30, 2016
\$ 349,131	\$ 54,153	\$ -	\$ 403,284	\$ 679,774
81,170	13,513	-	94,683	187,435
121,667	18,294	-	139,961	225,922
18,102	2,586	-	20,688	31,037
25,086	50,172	-	75,258	426,462
28,845	4,665	-	33,510	15,618
624,001	143,383	-	767,384	1,566,248
-	-	-	-	-
\$ 624,001	\$ 143,383	\$ -	\$ 767,384	\$ 1,566,248

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, 2016

	<u>Amended Budget</u>	<u>Actual</u>	<u>Positive (Negative) Variance</u>
Operating revenues - sales			
Residential	\$ 6,338,000	\$ 6,090,231	\$ (247,769)
Commercial	15,766,500	15,348,675	(417,825)
Industrial	10,040,000	9,615,567	(424,433)
Public authority	286,000	309,162	23,162
Street lighting	195,000	203,949	8,949
Yard lights	82,000	98,529	16,529
Total operating revenues - sales	<u>32,707,500</u>	<u>31,666,113</u>	<u>(1,041,387)</u>
Other operating revenues			
Forfeited discounts	60,000	60,777	777
Merchandise and jobbing	187,000	231,826	44,826
Sale of scrap	35,000	41,792	6,792
Recovery of bad debts	200	26	(174)
MISO income	2,900,000	3,483,052	583,052
Miscellaneous	39,000	46,458	7,458
Total other operating revenues	<u>3,221,200</u>	<u>3,863,931</u>	<u>642,731</u>
Nonoperating revenues			
Rental income	44,350	44,387	37
Pole rental income	34,600	48,860	14,260
Reimbursements	102,800	296,244	193,444
Interest income	250,000	288,991	38,991
Change in fair market value of investments	-	59,202	59,202
Gain/(Loss) on sale of assets	25,000	(355,965)	(380,965)
Total nonoperating revenues	<u>456,750</u>	<u>381,719</u>	<u>(75,031)</u>
Total revenues	<u>36,385,450</u>	<u>35,911,763</u>	<u>(473,687)</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, 2016

	<u>Amended Budget</u>	<u>Actual</u>	<u>Positive (Negative) Variance</u>
Generation expense			
Salaries and wages	\$ 125,400	\$ 123,124	\$ 2,276
Payroll taxes and fringes	85,600	192,648	(107,048)
Kalkaska combustion turbine	-	1,153	(1,153)
Purchased power	24,461,800	22,655,581	1,806,219
Coal dock	2,500	2,842	(342)
Trap and transfer	250	-	250
Union street fish ladder	250	-	250
Professional and contractual	68,000	85,029	(17,029)
Professional development	2,000	-	2,000
Operation supplies	4,200	3,456	744
Communications	1,500	170	1,330
Safety	3,500	2,994	506
Transportation	11,500	6,316	5,184
Equipment rental	12,400	(3,308)	15,708
Total generation expenses	<u>24,778,900</u>	<u>23,070,005</u>	<u>1,708,895</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, 2016

	Amended Budget	Actual	Positive (Negative) Variance
Distribution expense			
Salaries and wages	\$ 1,550,600	\$ 1,226,717	\$ 323,883
Payroll taxes and fringes	1,100,400	1,611,956	(511,556)
Substation	123,900	70,618	53,282
Overhead lines	175,800	170,363	5,437
Underground lines	28,000	97,922	(69,922)
Storm work	50,000	448,383	(398,383)
Electric meters	12,000	2,624	9,376
Street lighting	244,000	217,587	26,413
Traffic signals	17,000	1,767	15,233
Plant and structures	85,000	94,302	(9,302)
Load and dispatching contractual services	-	25,000	(25,000)
Professional services	95,800	139,050	(43,250)
Professional development	66,000	28,861	37,139
Operation supplies	239,150	172,630	66,520
Utilities	77,000	78,231	(1,231)
Safety	45,000	27,538	17,462
Transportation	35,000	23,796	11,204
Equipment rental	21,000	(23,539)	44,539
Inventory adjustment	-	3,674	(3,674)
Miscellaneous	10,500	7,471	3,029
Total distribution expense	3,976,150	4,424,951	(448,801)
Transmission expense			
Salaries and wages	223,300	233,222	(9,922)
Substation	25,000	14,496	10,504
Overhead lines	10,000	76,567	(66,567)
MISO	27,500	32,494	(4,994)
Equipment rental	-	223	(223)
Miscellaneous	73,500	64,133	9,367
Total transmission expense	359,300	421,135	(61,835)

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, 2016

	<u>Amended Budget</u>	<u>Actual</u>	<u>Positive (Negative) Variance</u>
Customer accounting expense			
Salaries and wages	\$ 174,400	\$ 172,616	\$ 1,784
Meter reading	103,300	97,624	5,676
Payroll taxes and fringes	126,800	193,576	(66,776)
Office supplies	4,000	3,610	390
Postage	35,000	28,185	6,815
Stationary and printing	4,000	684	3,316
Professional and contractual	12,000	23,893	(11,893)
Uncollectible accounts	10,000	1,739	8,261
Collection expense	2,000	4,118	(2,118)
Data processing	22,000	20,197	1,803
Professional development	6,500	1,124	5,376
Transportation	4,200	2,344	1,856
Equipment rental	7,400	19,666	(12,266)
Miscellaneous	9,900	7,902	1,998
Total customer accounting expense	<u>521,500</u>	<u>577,278</u>	<u>(55,778)</u>
Public service expense			
Salaries and wages	53,000	22,481	30,519
Payroll taxes and fringes	29,900	34,637	(4,737)
Public service information	596,500	614,427	(17,927)
Total public service expense	<u>679,400</u>	<u>671,545</u>	<u>7,855</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, 2016

	<u>Amended Budget</u>	<u>Actual</u>	<u>Positive (Negative) Variance</u>
General administration expense			
Salaries	\$ 367,300	\$ 386,497	\$ (19,197)
Payroll taxes and fringes	201,300	322,167	(120,867)
Professional development	27,000	15,985	11,015
Professional and contractual	106,300	82,759	23,541
Office supplies	31,200	24,552	6,648
Fees and per diems	82,000	71,485	10,515
Special services	9,700	7,073	2,627
Legal fees	60,000	57,950	2,050
Utilities	3,500	3,909	(409)
Printing and publishing	6,000	4,682	1,318
Transportation	2,500	619	1,881
Miscellaneous	5,000	8,359	(3,359)
Total general administration expense	901,800	986,037	(84,237)
Other expenses			
Insurance - general	63,000	62,001	999
City fee	1,801,000	1,784,900	16,100
Depreciation	2,150,000	2,254,188	(104,188)
Total other expenses	4,014,000	4,101,089	(87,089)
Total operating expenses	35,231,050	34,252,040	(979,010)
Transfers			
Transfer in	-	175,000	(175,000)
Change in net position	\$ 1,154,400	\$ 1,834,723	\$ 680,323

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, 2016

	Amended Budget	Actual	Positive (Negative) Variance
Operating revenues - sales			
Charges for services	\$ 288,200	\$ 278,376	\$ (9,824)
Other operating revenues			
Merchandising and jobbing	-	129	129
Non-operating revenues			
Reimbursements	30,400	54,127	23,727
Interest income	500	125	(375)
Total non-operating revenues	30,900	54,252	23,352
Total revenues	319,100	332,757	13,657
Fiber expenses			
Salaries and wages	31,000	44,601	(13,601)
Payroll taxes and fringes	21,000	35,081	(14,081)
Operation supplies	12,000	1,829	10,171
Professional development	2,100	-	2,100
Miscellaneous	10,900	24,347	(13,447)
Total fiber expenses	77,000	105,858	(28,858)
WIFI Expenses			
Operation and maintenance	37,400	28,678	8,722
Other expenses			
Insurance and bonds	1,200	-	1,200
City fee	14,435	13,932	503
Depreciation	138,400	143,383	(4,983)
Total other expenses	154,035	157,315	(3,280)
Total operating expenses	268,435	291,851	(23,416)
Transfers			
Transfers out	-	175,000	(175,000)
Change in net position	\$ 50,665	\$ (134,094)	\$ (184,759)

INTERNAL CONTROL AND COMPLIANCE



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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 5, 2016

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, 2016, 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 5, 2016.

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.

Orstedald Haefner LLC