

Traverse City Light and Power

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

Financial Statements

**For the Fiscal Year Ended
June 30, 2018**



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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INDEPENDENT AUDITORS' REPORT

December 17, 2018

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, 2018, 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, 2018, 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 31 through 36 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 17, 2018 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, 2018. 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.

Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the statement of net position statement because the resources of those funds are not available to support the Department's own programs. The accounting used for fiduciary funds is much like that used for enterprise funds.

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 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 \$72,763,793 at the close of the most recent fiscal year, June 30, 2018.

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 | |
|-----------------------------------|---------------------|---------------------|
| | 2018 | 2017 |
| Current and other assets | \$25,519,167 | \$28,054,525 |
| Capital assets | 64,892,176 | 59,630,827 |
| Total assets | 90,441,343 | 87,685,352 |
| Deferred outflows | 3,585,046 | 3,021,899 |
| Long-term liabilities outstanding | 13,751,375 | 13,126,689 |
| Other liabilities | 4,033,894 | 3,008,930 |
| Total liabilities | 17,785,269 | 16,135,619 |
| Deferred inflows | 1,929,881 | 774,212 |
| Net position | | |
| Invested in capital assets | 64,892,176 | 59,630,827 |
| Unrestricted | 9,389,063 | 14,166,593 |
| Total net position | \$74,281,239 | \$73,797,420 |

Traverse City Light and Power's Changes in Net Position

| Business-type Activities | June 30 | |
|---|---------------------|---------------------|
| | 2018 | 2017 |
| Operating revenue | \$35,190,195 | \$34,793,277 |
| Operating expenses | (31,979,692) | (33,258,191) |
| Nonoperating revenue (expense) | 887,880 | 321,564 |
| | | |
| Increase in net position | 4,098,383 | 1,856,650 |
| Net position – beginning of year, as restated | 70,182,856 | 71,940,770 |
| | | |
| Net position – end of year | \$74,281,239 | \$73,797,420 |

Net position was restated at July 1, 2017 to record other postemployment benefits in connection with the implementation of GASB 75.

Business-type activities

The overall financial position of the Department remained strong in 2017-2018. 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 \$1.3M, 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, Heritage Sustainable Energy, LLC, and Cherry Capital Airport for reimbursement of various capital projects in the approximate amount of \$640K. The change in fair market value of investments (\$244K) 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 2017-18, Electric Funds operating expenses was less than budget by approximately \$4.5M. This was primarily attributed to less kWh’s purchased along with purchase power cost having a lower price per kWh than what was forecasted. Overall fringe benefits came in lower than expected, specifically pension expense relating to higher deferred outflows 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 | |
|-----------------------------------|---------------------|---------------------|
| | 2018 | 2017 |
| Land and land improvements | \$1,079,419 | \$1,079,419 |
| Construction in progress | 2,746,924 | 2,098,071 |
| Buildings and improvements | 5,687,649 | 5,668,394 |
| Equipment and distribution system | 85,932,387 | 80,776,953 |
| Accumulated depreciation | (30,584,203) | (29,992,010) |
| Total | \$64,892,176 | \$59,630,827 |

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 are lower anticipated costs relating to purchase power because of the debt service paid in full relating to an entitlement commitment with MPPA. This will result in lower cost to customers passed on through the utility's variable power service cost recovery rate. Additionally, the utility is continuing with an 8-year amortization schedule on the utility's unfunded pension liability to increase the pension funding percentage.

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, 2018

| ASSETS | Light and Power Fund | Fiber Fund | Business-type Activities Total |
|---|----------------------------|------------------|--------------------------------------|
| Current assets | | | |
| Cash and cash equivalents | \$ 3,923,269 | \$ 239,441 | \$ 4,162,710 |
| Receivables | | | |
| Customer, less allowances of \$320,558 | | | |
| for uncollectible accounts (Light and Power Fund) | 3,506,319 | 24,714 | 3,531,033 |
| Accrued interest | 57,997 | - | 57,997 |
| Taxes | 4,923 | - | 4,923 |
| Other | 451,681 | - | 451,681 |
| Inventories | 1,575,211 | 11,411 | 1,586,622 |
| Prepaid expenses | 95,817 | - | 95,817 |
| Due from other funds | 553 | - | 553 |
| Total current assets | 9,615,770 | 275,566 | 9,891,336 |
| Non-current assets | | | |
| Investments | 14,203,540 | - | 14,203,540 |
| Accounts receivables | 1,417,647 | - | 1,417,647 |
| Long-term advances - due from primary government | 219 | - | 219 |
| Land and land improvements | 1,079,419 | - | 1,079,419 |
| Construction in progress | 2,746,924 | - | 2,746,924 |
| Capital assets being depreciated, net | 59,747,543 | 1,318,290 | 61,065,833 |
| Total non-current assets | 79,195,292 | 1,318,290 | 80,513,582 |
| Total assets | 88,811,062 | 1,593,856 | 90,404,918 |
| Deferred outflows | | | |
| Deferred outflows of resources - Pensions | 2,579,331 | - | 2,579,331 |
| Deferred outflows of resources - OPEB | 1,005,715 | - | 1,005,715 |
| Total deferred outflows of resources | 3,585,046 | - | 3,585,046 |

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, 2018

| LIABILITIES AND NET POSITION | Light and Power Fund | Fiber Fund | Business-type Activities Total |
|---|-------------------------|---------------------|--------------------------------------|
| Current liabilities | | | |
| Accounts payable | \$ 2,717,834 | \$ 33,856 | \$ 2,751,690 |
| Accrued expenses and other liabilities | 855,573 | 14,846 | 870,419 |
| Customer deposits | 95,289 | - | 95,289 |
| Compensated absences | 3,728 | - | 3,728 |
| Unearned revenue | - | 14,815 | 14,815 |
| Due to other funds | - | 553 | 553 |
| Due to primary government | 273,548 | 17,427 | 290,975 |
| Total current liabilities | 3,945,972 | 81,497 | 4,027,469 |
| Long-term liabilities | | | |
| Compensated absences | 196,318 | 2,444 | 198,762 |
| Net pension liability | 11,513,058 | - | 11,513,058 |
| Net other post employment benefit liability | 2,039,555 | - | 2,039,555 |
| Total liabilities | 17,694,903 | 83,941 | 17,778,844 |
| Deferred inflows | | | |
| Deferred inflows of resources - Pensions | 1,243,854 | - | 1,243,854 |
| Deferred inflows of resources - OPEB | 686,027 | - | 686,027 |
| Total deferred inflows of resources | 1,929,881 | - | 1,929,881 |
| Net position | | | |
| Invested in capital assets | 63,573,886 | 1,318,290 | 64,892,176 |
| Unrestricted | 9,197,438 | 191,625 | 9,389,063 |
| Total net position | \$ 72,771,324 | \$ 1,509,915 | \$ 74,281,239 |

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, 2018

| | Light and Power Fund | Fiber Fund | Business-type Activities Total |
|--|----------------------------|---------------------|--------------------------------------|
| Operating revenues | | | |
| Charges for services | \$ 31,435,708 | \$ 347,847 | \$ 31,783,555 |
| MISO income | 3,090,792 | - | 3,090,792 |
| Other | 315,446 | 402 | 315,848 |
| Total operating revenues | 34,841,946 | 348,249 | 35,190,195 |
| Operating expenses | | | |
| Purchase power | 20,881,494 | - | 20,881,494 |
| Distribution | 3,701,031 | - | 3,701,031 |
| Transmission | 466,889 | - | 466,889 |
| Customer accounting | 477,359 | - | 477,359 |
| Public service | 448,879 | - | 448,879 |
| General administration | 1,192,961 | - | 1,192,961 |
| Fiber | - | 171,026 | 171,026 |
| WIFI | - | 27,646 | 27,646 |
| Other | 67,619 | 467 | 68,086 |
| City fee | 1,745,395 | 17,427 | 1,762,822 |
| Depreciation | 2,635,190 | 146,309 | 2,781,499 |
| Total operating expenses | 31,616,817 | 362,875 | 31,979,692 |
| Operating income (loss) | 3,225,129 | (14,626) | 3,210,503 |
| Nonoperating revenues (expenses) | | | |
| Rental income | 122,908 | - | 122,908 |
| Reimbursements | 893,101 | 75,465 | 968,566 |
| Interest income | 241,790 | 285 | 242,075 |
| Change in fair value of investments | (244,001) | - | (244,001) |
| Loss on sale of assets | (201,668) | - | (201,668) |
| Total nonoperating revenue | 812,130 | 75,750 | 887,880 |
| Income before transfers | 4,037,259 | 61,124 | 4,098,383 |
| Transfers | | | |
| Transfers in | 125,000 | - | 125,000 |
| Transfers out | - | (125,000) | (125,000) |
| Total transfers | 125,000 | (125,000) | - |
| Change in net position | 4,162,259 | (63,876) | 4,098,383 |
| Net position, beginning of year, as restated | 68,609,065 | 1,573,791 | 70,182,856 |
| Net position, end of year | \$ 72,771,324 | \$ 1,509,915 | \$ 74,281,239 |

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, 2018

| | Light and Power Fund | Fiber Fund | Business-type Activities Total |
|---|----------------------------|-------------------|--------------------------------------|
| Cash flows from operating activities | | | |
| Cash received from customers | \$ 34,529,048 | \$ 394,886 | \$ 34,923,934 |
| Cash payments to employees | (4,685,611) | (122,145) | (4,807,756) |
| Cash payments to suppliers for goods and services | (22,348,503) | (50,216) | (22,398,719) |
| Cash payments of City fee | (1,700,986) | (13,999) | (1,714,985) |
| Net cash provided by operating activities | 5,793,948 | 208,526 | 6,002,474 |
| Cash flows from noncapital financing activities | | | |
| Cash payments from primary government | 68 | - | 68 |
| Cash payments to/from other funds | 124,447 | (124,447) | - |
| Customer deposits paid | (2,158) | - | (2,158) |
| Rental income received | 122,908 | - | 122,908 |
| Reimbursements received | 893,101 | 75,465 | 968,566 |
| Net cash provided by (used in) noncapital financing activities | 1,138,366 | (48,982) | 1,089,384 |
| Cash flows from capital and related financing activities | | | |
| Proceeds from sale of capital assets | 9,072 | - | 9,072 |
| Purchase of capital assets | (8,222,972) | (30,616) | (8,253,588) |
| Net cash (used in) capital and related financing activities | (8,213,900) | (30,616) | (8,244,516) |
| Cash flows from investing activities | | | |
| Purchase of investments | (251,833) | - | (251,833) |
| Interest | (7,553) | 285 | (7,268) |
| Net cash provided by (used in) investing activities | (259,386) | 285 | (259,101) |
| Net (decrease) increase in cash and cash equivalents | (1,540,972) | 129,213 | (1,411,759) |
| Cash and cash equivalents, beginning of year | 5,464,241 | 110,228 | 5,574,469 |
| Cash and cash equivalents, end of year | \$ 3,923,269 | \$ 239,441 | \$ 4,162,710 |

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, 2018

| | Light and Power Fund | Fiber Fund | Business-type Activities Total |
|--|----------------------------|-------------------|--------------------------------------|
| Cash flows from operating activities | | | |
| Operating income (loss) | \$ 3,225,129 | \$ (14,626) | \$ 3,210,503 |
| Adjustments to reconcile operating income to net cash provided by operating activities | | | |
| Depreciation | 2,635,190 | 146,309 | 2,781,499 |
| Changes in operating assets and liabilities which provided (used) cash | | | |
| Receivables | (312,685) | 46,637 | (266,048) |
| Inventories | 19,367 | (5,455) | 13,912 |
| Prepaid expenses | (3,681) | - | (3,681) |
| Deferred outflow | 608,199 | - | 608,199 |
| Accounts payable | 689,387 | 26,666 | 716,053 |
| Due to other governments | 44,409 | 3,428 | 47,837 |
| Accrued expenses and other liabilities | 245,873 | 6,653 | 252,526 |
| Unearned revenue | - | - | - |
| Compensated absences | 41,631 | (1,086) | 40,545 |
| Net pension liability | (771,508) | - | (771,508) |
| Other postemployment benefit asset | (627,363) | - | (627,363) |
| Net cash provided by operating activities | \$ 5,793,948 | \$ 208,526 | \$ 6,002,474 |

Non cash transaction: The cash flow includes the change in fair market value of investments in the amount of \$ (244,001).

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 FIDUCIARY NET POSITION FIDUCIARY FUND JUNE 30, 2018

| | Other Postemployment Benefit Funds |
|---|---|
| Assets | |
| Investments, at fair value | |
| MERS total market fund | \$ 2,649,771 |
| Accounts receivable | 694,113 |
| | <hr/> |
| Total assets | 3,343,884 |
| | <hr/> |
| Net Position | |
| Held in trust for other postemployment benefits | \$ 3,343,884 |
| | <hr/> <hr/> |

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 CHANGES IN FIDUCIARY NET POSITION FIDUCIARY FUND FOR THE YEAR ENDED JUNE 30, 2018

| | Other Postemployment Benefit Funds |
|--|---|
| Additions | |
| Employer contributions | \$ 229,388 |
| Investment earnings | |
| Net investment in fair value of investments | 191,582 |
| Investment advisor fees | (6,221) |
| Net investment earnings | 185,361 |
| Total additions | 414,749 |
| Net position held in trust, beginning of year | 2,929,134 |
| Net position held in trust, end of year | \$ 3,343,884 |

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 2018, the city fee was \$1,762,822.

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 and OPEB investments as discussed in Note 8.

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.

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, 2018 are composed of the following:

| | <u>Enterprise Funds</u> | <u>Fiduciary Fund</u> | <u>Total</u> |
|---------------------------|------------------------------------|----------------------------------|---------------------|
| Cash and cash equivalents | \$4,162,710 | \$ - | \$ 4,162,710 |
| Investments | 14,203,540 | 2,649,771 | 16,853,311 |
| | <u>\$18,366,250</u> | <u>\$2,649,771</u> | <u>\$21,016,021</u> |

The cash and investments making up the above balances are as follows:

| | |
|--------------------|---------------------|
| Deposits | \$ 4,626,317 |
| Investments | 13,739,933 |
| OPEB - investments | <u>2,649,771</u> |
| Total | <u>\$21,016,021</u> |

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.

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The Department chooses to disclose its investments by specifically identifying each. As of June 30, 2018, the Department's Michigan CLASS investment and the U.S. Treasury notes are rated by Standard and Poor's.

The Department also maintains a postemployment benefit trust fund where investments are maintained separately from the City's pooled cash and investments and are subject to the Michigan Public Employees Retirement System's Investment Act, Public Act 314, 1965, as amended, authorizes pension and postemployment benefit trusts to invest in stocks, government and corporate securities, mortgages, real estate, and various other investment instruments, subject to certain limitations. The investments are managed by the Michigan Employees Retirements System ("MERS") and are in the MERS Total Market Fund in the amount of \$2,649,771.

The Department had the following investments:

| <u>Investment</u> | <u>Maturity</u> | <u>Fair Value</u> | <u>Rating</u> |
|-----------------------|-----------------|-----------------------------|---------------|
| Commercial Paper | 10/12/2018 | \$496,585 | A-1/P-1 |
| Commercial Paper | 10/26/2018 | 248,050 | A-1/P-1 |
| US Treasury Note | 02/15/2020 | 407,064 | AA+ |
| US Treasury Note-FHLB | 02/26/2021 | 496,480 | AA+ |
| US Treasury Note-FHLB | 05/17/2021 | 986,800 | AA+ |
| US Treasury Note-FHLB | 08/24/2021 | 985,910 | AA+ |
| US Treasury Note-FHLB | 12/14/2021 | 995,690 | AA+ |
| US Treasury Note-FHLB | 02/28/2022 | 991,920 | AA+ |
| US Treasury Note-FHLB | 03/29/2022 | 976,620 | AA+ |
| US Treasury Note-FHLB | 06/22/2022 | 981,590 | AA+ |
| US Treasury Note-FHLB | 07/26/2022 | 991,320 | AA+ |
| US Treasury Note-FHLB | 08/24/2028 | 959,120 | AA+ |
| US Treasury Note-FHLB | 07/25/2031 | 909,040 | AA+ |
| US Treasury Note-FHLB | 08/15/2031 | 911,860 | AA+ |
| US Treasury Note-FHLB | 10/12/2022 | 955,160 | AA+ |
| US Treasury Note-FHLB | 10/12/2022 | 492,545 | AA+ |
| US Treasury Note-FHLB | 04/27/2023 | 951,070 | AA+ |
| Michigan CLASS | NA | <u>3,109</u> | AAAm |
| | | <u>\$ 13,739,933</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.

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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.

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 \$13,739,933 of investments at June 30, 2018, the Department has a custodial credit risk exposure of \$13,736,824 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.

- MERS Total Market Fund is valued using quoted market prices (Level 1 Inputs)
- US Treasury Notes are valued using prices quoted in active markets for those securities.
- The Department does not have any investments that report fair value based on significant unobservable inputs (Level 3 Inputs)

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NOTES TO FINANCIAL STATEMENTS

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 | \$ 3,109 | \$ - | - | - |

3. CAPITAL ASSETS

At June 30, 2018, capital assets consist of the following:

| | Beginning Balance | Additions &Transfers | Deletions & Transfers | Ending Balance |
|---|------------------------------|-------------------------------------|--------------------------------------|----------------------------|
| Capital assets not being depreciated | | | | |
| Land and land improvements | \$1,079,419 | \$ - | \$ - | \$1,079,419 |
| Construction in progress | <u>2,098,071</u> | <u>8,161,852</u> | <u>7,512,999</u> | <u>2,746,924</u> |
| Total capital assets not being depreciated | <u>3,177,490</u> | <u>8,161,852</u> | <u>7,512,999</u> | <u>3,826,343</u> |
| Capital assets being depreciated | | | | |
| Buildings and improvements | 5,668,394 | 32,219 | 12,964 | 5,687,649 |
| Equipment and distribution system | 78,434,011 | 7,554,864 | 2,400,046 | 83,588,829 |
| Fiber System | 1,841,222 | 30,473 | - | 1,871,695 |
| WiFi System | <u>501,720</u> | <u>143</u> | <u>-</u> | <u>501,863</u> |
| Total capital assets being depreciated | <u>86,445,347</u> | <u>7,617,699</u> | <u>2,413,010</u> | <u>91,650,036</u> |
| Less accumulated depreciation for | | | | |
| Buildings and improvements | 1,817,573 | 166,258 | - | 1,983,831 |
| Equipment and distribution system | 27,265,478 | 2,468,932 | 2,189,306 | 27,545,104 |
| Fiber System | 783,529 | 96,123 | - | 879,652 |
| WiFi System | <u>125,430</u> | <u>50,186</u> | <u>-</u> | <u>175,616</u> |
| Total accumulated depreciation | <u>29,992,010</u> | <u>2,781,499</u> | <u>2,189,306</u> | <u>30,584,203</u> |
| Total capital assets being depreciated, net | <u>56,453,337</u> | <u>4,836,200</u> | <u>223,704</u> | <u>61,065,833</u> |
| Total capital assets, net | <u>\$59,630,827</u> | <u>\$12,998,052</u> | <u>\$7,736,703</u> | <u>\$64,892,176</u> |

TRAVERSE CITY LIGHT AND POWER

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NOTES TO FINANCIAL STATEMENTS

4. LONG-TERM LIABILITIES

Long-term debt at June 30, 2018, 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>\$161,945</u> | <u>\$247,528</u> | <u>\$210,711</u> | <u>\$198,762</u> | <u>\$ 3,728</u> |

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 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.

For the year ended June 30, 2018, Traverse City Light and Power recognized expenses totaling \$17,628,451 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 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 |
|-----------------------------------|----------------------------|
| 2019 | \$7,478,632 |
| 2020 | 5,519,270 |
| 2021 | 5,684,848 |
| 2022 | 5,855,394 |
| 2023 | 6,031,055 |
| 2024-2027 | 14,035,960 |
| | <u>\$ 44,605,159</u> |

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

| Year Ended December 31 | Principal | Interest | Total |
|-----------------------------------|----------------------|---------------------|----------------------|
| 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 | 1,426,920 | 394,680 | 1,821,600 |
| 2024-2027 | 6,466,680 | 828,259 | 7,294,939 |
| | <u>\$ 17,188,944</u> | <u>\$ 3,671,411</u> | <u>\$ 20,860,355</u> |

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, 2018, the Department recognized expenses totaling \$2,810,991.

In December 2014, the Department entered into a 20-year purchase power agreement with options to terminate on January 1, 2025 and January 1, 2030 upon ninety-day notice. The Agreement is with Heritage Sustainable Energy, LLC to purchase up to .6 MW of electric energy for the M-72 wind turbine. For the year ended June 30, 2018, the Department recognized expenses totaling \$30,143.

In August 2017, the Department amended the Heritage Sustainable Energy, LLC contract to purchase and additional 1MW of electric energy for the M-72 solar array. The contract has been an option to expand the solar array to include an additional approximate 1 to 3 MW of solar energy. The contract will terminate December 31, 2038. For the year ended June 30, 2018 the Department recognized expenses totaling \$99,416.

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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 – closed to new hires, linked to Division 11 | |
|--|----------------------------|
| | 2017 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 | |
|--|----------------------------|
| | 2017 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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| | |
|---|---------------------------|
| 11 - Non-union hired after 7/1/2017, linked to Division 01 | |
| | 2017 Valuation |
| Benefit Multiplier: | 1.5% Multiplier (80% 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 |

| | |
|---|---------------------------|
| 12 - Union hired after 7/1/2012, linked to Division 10 | |
| | 2017 Valuation |
| Benefit Multiplier: | 1.5% Multiplier (80% 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, 2017 valuation date, the following employees were covered by the benefit terms:

| | |
|--|-----------|
| Inactive employees or beneficiaries currently receiving benefits | 58 |
| Inactive employees entitled to but not yet receiving benefits | 4 |
| Active employees | <u>37</u> |
| | <u>99</u> |

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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 7.31 to 32.52% based on annual payroll for open divisions. One division that is closed to new employees has an annual employer contribution amount of \$65,832.

Net Pension Liability. The employer's Net Pension Liability was measured as of December 31, 2017, 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, 2017 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:

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| 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 2017. 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.

Changes in Net Pension Liability

| Calculating the Net Pension Liability | | | |
|---|----------------------------|---|---------------------------------|
| Changes in Net Pension Liability | Total Pension Liability | Increase (Decrease) Plan Fiduciary Net Position | |
| | (a) | (b) | Net Pension Liability (a) – (b) |
| Balances at 12/31/16 | | | |
| Changes for the Year | \$29,463,200 | \$16,498,456 | \$12,964,744 |
| Service Cost | 310,387 | - | 310,387 |
| Interest on Total Pension Liability | 2,292,239 | - | 2,292,239 |
| Difference between expected and actual experience | 363,115 | - | 363,115 |
| Employer Contributions | - | 2,253,396 | (2,253,396) |
| Net investment Income | - | 2,200,228 | (2,200,228) |
| Benefit payments, including employee refunds | (1,930,810) | (1,930,810) | - |
| Administrative expense | - | (34,750) | 34,750 |
| Other | 1,448 | - | 1,448 |
| Net Changes | <u>1,036,379</u> | <u>2,488,065</u> | <u>(1,451,686)</u> |
| Balances as of 12/31/17 | <u>\$30,499,579</u> | <u>\$18,986,521</u> | <u>\$11,513,058</u> |

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.

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| | 1% Decrease (7.00%) | Current Discount Rate (8.00%) | 1% Increase (9.00%) |
|---------------------------------------|------------------------|-------------------------------------|------------------------|
| Net Pension Liability at 12/31/17 | \$11,513,058 | \$11,513,058 | \$11,513,058 |
| Change in Net Pension Liability (NPL) | 3,387,924 | - | (2,863,200) |
| Calculated NPL for your Notes | \$14,900,982 | \$11,513,058 | \$8,649,858 |

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.

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

For the year ended June 30, 2018 the employer recognized pension expense of \$ 1,222,996. 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 | \$ 672,959 | \$ (948,856) |
| Change in Experience | 363,295 | (294,998) |
| Change in Assumptions | 361,014 | - |
| Contributions subsequent to the measurement date* | 1,182,063 | - |
| Total | \$ 2,579,331 | \$ (1,243,854) |

*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 2019.

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

| | |
|------------|-------------------|
| Year ended | |
| 2019 | \$ 509,271 |
| 2020 | (1,173) |
| 2021 | (180,917) |
| 2022 | (173,767) |
| | <u>\$ 153,414</u> |

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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 \$175,697 and employees contributed \$216,809.

8. POSTEMPLOYMENT BENEFITS

Plan Description. The Department maintains a single-employer defined benefit healthcare plan (the "Plan"). In addition to the retirement benefits described in Note 6, the Plan provides health insurance benefits to certain retirees and their beneficiaries, which are advance funded on a discretionary basis. The Plan is included as an other post-employment benefits trust fund in the Department's financial statements; a stand-alone financial report of the Plan has not been issued.

Benefits provided. The plan provides health insurance premiums paid at 100% for the retiree only. If a retiree receives a reduced benefit pension as calculated by MERS the Board will reduce the retiree health payment by the same percentage. Effective July 1, 2017 for all new hires who become eligible for a pension benefit, the Board will pay the retiree's health insurance premium until the retiree is Medicare eligible. If a retiree receives a reduced benefit pension as calculated by MERS the Board will reduce the retiree health payment by the same percentage.

Membership of the Plan consisted of the following at the date of the latest actuarial valuation (June 30, 2018):

| | |
|---|------------------|
| Active plan members | 34 |
| Retirees and beneficiaries receiving benefits | <u>38</u> |
| Total | <u><u>72</u></u> |

Contributions. The Plan was established and is being funded under the authority of the Traverse City Light and Power Board. Employees are not required to contribute to the plan.

The Plan's funding policy is that the employer will contribute any required amounts as determined by an annual actuarial valuation. There are no long-term contracts for contributions to the Plan. The plan has no legally required reserves.

TRAVERSE CITY LIGHT AND POWER

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

NOTES TO FINANCIAL STATEMENTS

Net OPEB Liability. The total OPEB liability in the June 30, 2018 annual actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation: 2.50%

Salary Increases: 5.00%

Investment rate of return: 7.5%

Healthcare cost trend rates: 4.5 to 7.0% per year

Mortality rates used RP-2014 Combined Annuitant Mortality Table for males and females.

The actuarial assumptions used in the valuation were based on the results of the most recent actuarial experience study.

The long-term expected rate of return on OPEB 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 produce the long-term expected rate of return by weighting the expected future real rates of return by 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 |
|------------------------|-------------------|--|
| US Stocks | 34.5% | 7.0% |
| International Stocks | 5.0% | 8.0% |
| Emerging Market Stocks | 5.0% | 12.0% |
| U.S. Bonds | 20.0% | 6.0% |
| Global Bonds | 15.0% | 7.0% |
| Global Real Estate | 7.0% | 8.0% |
| Commodities | 5.0% | 8.0% |
| Private Equity | 7.0% | 12.0% |
| Cash | <u>1.5%</u> | .5% |
| Total | 100.0% | |

The City, as the investment fiduciary, has chosen for the Plan an asset mix intended to meet or exceed a long-term rate of return of 7.5%.

Concentrations. 100% of the Plan's investments are invested in the MERS total market portfolio.

TRAVERSE CITY LIGHT AND POWER

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

NOTES TO FINANCIAL STATEMENTS

Discount rate. The discount rate used to measure the total OPEB liability is 7.5%. The projection of cash flows used to determine the discount rate assumed that City contributions will be made at rates equal to the actuarially determined contribution rates. Based on those assumptions, the OPEB plan's fiduciary net position was projected to be available to make all projected OPEB payments for current active and inactive employees. Therefore, the long-term expected rate of return on OPEB plan investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

Changes in the Net OPEB Liability

| Calculating the Net Pension Liability | | | |
|--|-----------------------------------|--|----------------------------------|
| | | Increase (Decrease) | |
| | Total OPEB Liability (a) | Plan Fiduciary Net Position (b) | Net OPEB Liability (a)-(b) |
| Balances at 6/30/2017 | | | |
| Changes for the Year | \$5,596,053 | \$2,929,134 | \$2,666,919 |
| Service cost | 2,852 | - | 2,852 |
| Interest | 406,878 | - | 406,878 |
| Differences between expected and actual experience | (269,497) | (24,842) | (244,655) |
| Change in assumptions | 28,187 | - | 28,187 |
| Contributions: employer | - | 229,388 | (229,388) |
| Net investment Income | - | 191,582 | (191,582) |
| Benefit payments, including refunds | (342,038) | - | (342,038) |
| Administrative expense | - | (6,220) | 6,220 |
| Other changes | (38,996) | 24,842 | (63,838) |
| Net changes | (212,614) | 414,750 | (627,364) |
| Balance as of 6/30/2018 | \$5,383,439 | \$3,343,884 | \$2,039,555 |

Sensitivity of the Net OPEB Liability to changes in the discount rate.

The following presents the net OPEB liability of the employer, calculated using the discount rate of 7.5%, as well as what the employer's net OPEB liability would be using a discount rate that is 1 percentage point lower or higher than the current rate.

| | 1% Decrease | Current Discount rate | 1% Increase |
|---|-------------|--------------------------|-------------|
| Net OPEB liability | \$1,520,136 | \$2,039,555 | \$2,663,596 |
| Plan fiduciary position as a percentage of the total OPEB liability | (25.47%) | | 30.60% |

TRAVERSE CITY LIGHT AND POWER

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

NOTES TO FINANCIAL STATEMENTS

Sensitivity of the Net OPEB Liability to changes in the healthcare cost trend rates.

The following presents the net OPEB liability of the employer, calculated using the healthcare cost trend rate of 4.5%, as well as what the employer's net OPEB liability would be using a healthcare cost trend rate that is 1 percentage point lower or higher than the current rate.

| | 1% Decrease | Current healthcare cost trend rate | 1% Increase |
|--|-------------|---|-------------|
| Net OPEB liability | \$2,678,854 | \$2,039,555 | \$1,500,267 |
| Plan fiduciary position as a percentage of total OPEB liability | 31.35% | | (26.44%) |

OPEB Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB Plan

For the year ended June 30, 2018 the employer recognized OPEB expense of \$530,432. The employer reported deferred outflows and inflows of resources related to pensions from the following sources:

| | Deferred Outflows of Resources | Deferred Inflows of Resources |
|------------------------------------|--------------------------------------|-------------------------------------|
| Differences in experience | \$ - | \$ 270,539 |
| Changes in assumptions | 985,843 | 176,234 |
| Excess(deficit) investment returns | 19,872 | 218,217 |
| Other changes | - | 21,037 |
| Total | \$ 1,005,715 | \$ 686,027 |

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

| | |
|-------|------------------|
| 2019 | \$ 120,702 |
| 2020 | 227,657 |
| 2021 | (33,639) |
| 2022 | 4,968 |
| Total | <u>\$319,688</u> |

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.

TRAVERSE CITY LIGHT AND POWER

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

NOTES TO FINANCIAL STATEMENTS

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 September 25, 2018, the Board authorized the execution of a project transaction authorization for 22 MW of solar energy with Michigan Public Power Agency for a term of 25 years with an expected commencement in 2021 for and estimated total contract cost of \$48,000,000.

12. DESIGNATIONS OF NET POSITION

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

| | <u>June 30, 2018</u> |
|----------------------|----------------------|
| Emergencies | \$ 100,056 |
| Minimum Cash Reserve | <u>8,900,000</u> |
| Total | <u>\$ 9,000,056</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 \$5,881,238 and peak energy bilateral contracts for the calendar year 2018 through 2020 in the amount of \$3,289,013 and capacity transaction bilateral contracts for the calendar year 2018 through 2027 in the amount of \$3,366,680.

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. As of June 30, 2018, the balance left on the contract is \$2,756,643.

14. PRIOR PERIOD ADJUSTMENT

Beginning net position was decreased by \$3,614,565 to record the other postemployment benefits liability in accordance with the implementation of Governmental Accounting Standards Board (GASB) Statement No. 75.

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, 2018**

| | December 31, | | | |
|---|----------------------|----------------------|----------------------|----------------------|
| | 2014 | 2015 | 2016 | 2017 |
| Total pension liability | | | | |
| Service cost | \$ 313,020 | \$ 295,317 | \$ 300,475 | \$ 310,387 |
| Interest | 2,083,781 | 2,142,935 | 2,276,465 | 2,292,239 |
| Differences between expected and actuarial experience | - | 363,835 | (509,997) | 363,115 |
| Changes in assumptions | - | 1,444,054 | - | - |
| Benefit payments, including refunds | (1,626,244) | (1,715,604) | (1,818,642) | (1,930,810) |
| Other changes | - | (759) | - | 1,448 |
| Net change in total pension liability | 770,557 | 2,529,778 | 248,301 | 1,036,379 |
| Total pension liability, beginning of year | 25,914,564 | 26,685,121 | 29,214,899 | 29,463,200 |
| Total pension liability, end of year | 26,685,121 | 29,214,899 | 29,463,200 | 30,499,579 |
| Plan fiduciary net position | | | | |
| Contribution - employer | 773,230 | 858,331 | 1,564,302 | 2,253,396 |
| Net investment income | 1,000,478 | (234,339) | 1,686,136 | 2,200,228 |
| Administrative expenses | (36,578) | (34,767) | (33,363) | (34,750) |
| Benefit payments, including refunds | (1,626,244) | (1,715,604) | (1,818,642) | (1,930,809) |
| Net change in plan fiduciary net position | 110,886 | (1,126,379) | 1,398,433 | 2,488,065 |
| Plan fiduciary net position, beginning of year | 16,115,516 | 16,226,402 | 15,100,023 | 16,498,456 |
| Plan fiduciary net position, end of year | 16,226,402 | 15,100,023 | 16,498,456 | 18,986,521 |
| Department's net pension liability | \$ 10,458,719 | \$ 14,114,876 | \$ 12,964,744 | \$ 11,513,058 |
| Plan fiduciary net position as a percent of total pension liability | 60.81% | 51.69% | 56.00% | 62.25% |
| Covered employee payroll | \$ 2,862,491 | \$ 2,736,729 | \$ 2,728,607 | \$ 2,883,420 |
| Department's net pension liability as a percent of covered employee payroll | 365.37% | 515.76% | 475.14% | 399.28% |

TRAVERSE CITY LIGHT AND POWER

**REQUIRED SUPPLEMENTARY INFORMATION
DEFINED BENEFIT PENSION PLAN
MERS SCHEDULE OF EMPLOYER CONTRIBUTIONS
FOR THE YEAR ENDED JUNE 30, 2018**

| | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> |
|--|--|--------------|-----------------------|-----------------------|
| Actual determined contribution | \$ 770,572 | \$ 891,939 | \$ 944,388 | \$ 1,110,648 |
| Contribution in relation to the actuarially determined contribution | (770,572) | (891,939) | (2,202,960) | (2,356,392) |
| Contribution deficiency (excess) | <u>\$ -</u> | <u>\$ -</u> | <u>\$ (1,258,572)</u> | <u>\$ (1,245,744)</u> |
| Covered employee payroll | \$ 2,880,960 | \$ 2,866,124 | \$ 2,862,491 | \$ 2,947,185 |
| Contribution as a percentage of covered employee payroll | 26.75% | 31.12% | 32.99% | 37.69% |
| 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

REQUIRED SUPPLEMENTARY INFORMATION

OTHER POST EMPLOYMENT BENEFIT TRUST FUND

SCHEDULE OF CHANGES IN NET OPEB LIABILITY AND RELATED RATIOS

FOR THE YEAR ENDED JUNE 30, 2018

| | |
|--|---------------------------------|
| Total OPEB liability | 2018 |
| Service cost | \$ 2,852 |
| Interest | 406,878 |
| Differences between expected and actuarial experience | (269,497) |
| Changes in assumptions | 28,187 |
| Benefit payments, including refunds | (342,038) |
| Other changes | (38,996) |
| | <hr/> |
| Net change in total OPEB liability | (212,614) |
| Total OPEB liability, beginning of year | <hr/> 5,596,053 |
| Total OPEB liability, end of year | <hr/> 5,383,439 <hr/> |
| Plan fiduciary net position | |
| Contribution - employer | 229,388 |
| Net investment income | 191,582 |
| Administrative expenses | (6,220) |
| | <hr/> |
| Net change in plan fiduciary net position | 414,750 |
| Plan fiduciary net position, beginning of year | <hr/> 2,929,134 |
| Plan fiduciary net position, end of year | <hr/> 3,343,884 <hr/> |
| Department's net OPEB liability | <hr/> \$ 2,039,555 <hr/> |
| Plan fiduciary net position as a percent of total OPEB liability | 62.11% |
| Covered employee payroll | \$ 2,947,185 |
| Department's net OPEB liability as a percent of covered employee payroll | 69.20% |

Note: TCL&P Plan was included within the City's Plan for fiscal year end June 30, 2017.

TRAVERSE CITY LIGHT AND POWER

REQUIRED SUPPLEMENTARY INFORMATION

OTHER POST EMPLOYMENT BENEFIT TRUST FUND

**SCHEDULE OF NET OPEB LIABILITY, FIDUCIARY NET POSITION AND RELATED RATIOS
FOR THE YEAR ENDED JUNE 30, 2018**

| | 2017 | 2018 |
|---|------------------|------------------|
| Total OPEB liability | \$ 5,596,053 | \$ 5,383,439 |
| OPEB fiduciary net position | <u>2,929,135</u> | <u>3,343,884</u> |
| Net OPEB liability | 2,666,918 | 2,039,555 |
| OPEB fiduciary net position as a % of total OPEB liability | 52.34% | 62.11% |
| Covered employee payroll | \$ 2,862,491 | 2,947,185 |
| NET OPEB liability as a percentage of covered employee payroll | 93.17% | 69.20% |

TRAVERSE CITY LIGHT AND POWER

REQUIRED SUPPLEMENTARY INFORMATION OTHER POSTEMPLOYMENT BENEFIT TRUST FUND SCHEDULE OF CONTRIBUTIONS FOR THE YEAR ENDED JUNE 30, 2018

| | 2017 | 2018 |
|--|--|--------------|
| Actual determined contribution | \$ 229,556 | \$ 175,757 |
| Contribution in relation to the actuarially determined contribution | 229,556 | 229,388 |
| Contribution deficiency (excess) | \$ - | \$ (53,631) |
| Covered employee payroll | \$ 2,862,491 | \$ 2,947,185 |
| Contribution as a percentage of covered employee payroll | 8.02% | 5.96% |
| Notes to Schedule | | |
| Actuarial cost method | Entry Age Normal | |
| Amortization method | Straight line | |
| Remaining amortization period | 2.11 years | |
| Asset valuation method | Market Value | |
| Inflation | 2.50% | |
| Salary increases | 5.00% | |
| Investment rate of return | 7.50% | |
| Retirement age | Varies depending on retirement plan | |
| Mortality | RP-2014 Combined Annuitant Mortality Table for males and females | |
| Health Care Trend rates | 4.0 - 7.0% | |

TRAVERSE CITY LIGHT AND POWER
REQUIRED SUPPLEMENTARY INFORMATION
OTHER POSTEMPLOYMENT BENEFIT TRUST FUND
SCHEDULE OF INVESTMENT RETURNS
FOR THE YEAR ENDED JUNE 30, 2018

| | <u>2017</u> | <u>2018</u> |
|--|-------------|-------------|
| Annual money-weighted rate of return, net of investment expense | 20.50% | 5.90% |

TRAVERSE CITY LIGHT AND POWER

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

SCHEDULE OF CAPITAL ASSETS AND DEPRECIATION (UNAUDITED) LIGHT AND POWER FUND FOR THE YEAR ENDED JUNE 30, 2018

| | Capital Assets - Cost | | | Balance at June 30, 2018 |
|--|-----------------------------|-------------------------|-------------------------|-----------------------------|
| | Balance at June 30, 2017 | 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 | 5,521,977 | 19,255 | 12,964 | 5,528,268 |
| Office structures | 97,149 | - | - | 97,149 |
| Other buildings | 49,268 | 12,964 | - | 62,232 |
| Total buildings and improvements | 5,668,394 | 32,219 | 12,964 | 5,687,649 |
| 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 | 77,022,236 | 7,188,393 | 2,400,046 | 81,810,583 |
| General | 1,366,525 | 366,471 | - | 1,732,996 |
| Total equipment and distribution system | 78,434,011 | 7,554,864 | 2,400,046 | 83,588,829 |
| Construction in progress | 2,098,071 | 8,131,732 | 7,482,879 | 2,746,924 |
| Total | \$ 87,279,895 | \$ 15,718,815 | \$ 9,895,889 | \$ 93,102,821 |

| Balance at June 30, 2017 | Accumulated Depreciation | | Balance at June 30, 2018 | Capital Assets - Net |
|-----------------------------|--------------------------|---------------------|-----------------------------|-----------------------------|
| | Current Depreciation | Deletions | | Balance at June 30, 2018 |
| \$ - | \$ - | \$ - | \$ - | \$ 1,073,535 |
| - | - | - | - | 5,884 |
| - | - | - | - | 1,079,419 |
| 1,787,009 | 163,165 | - | 1,950,174 | 3,578,094 |
| 13,732 | 1,226 | - | 14,958 | 82,191 |
| 16,832 | 1,867 | - | 18,699 | 43,533 |
| 1,817,573 | 166,258 | - | 1,983,831 | 3,703,818 |
| 24,008 | 2 | - | 24,010 | - |
| 390 | - | - | 390 | - |
| 2,189 | 625 | - | 2,814 | 18,036 |
| 26,554,441 | 2,334,928 | 2,189,306 | 26,700,063 | 55,110,520 |
| 684,450 | 133,377 | - | 817,827 | 915,169 |
| 27,265,478 | 2,468,932 | 2,189,306 | 27,545,104 | 56,043,725 |
| - | - | - | - | 2,746,924 |
| \$ 29,083,051 | \$ 2,635,190 | \$ 2,189,306 | \$ 29,528,935 | \$ 63,573,886 |

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, 2018

| | Capital Assets - Cost | | | Balance at June 30, 2018 |
|--|-----------------------------|-------------------------|-------------------------|-----------------------------|
| | Balance at June 30, 2017 | Additions/ Transfers | Deletions/ Transfers | |
| Equipment and distribution system | | | | |
| Overhead | \$ 1,076,106 | \$ 28,578 | \$ - | \$ 1,104,684 |
| Underground | 298,380 | - | - | 298,380 |
| Termination boxes | 365,883 | 1,399 | - | 367,282 |
| Wireless equipment | 51,725 | - | - | 51,725 |
| WIFI system | 501,720 | 143 | - | 501,863 |
| Other property | 49,128 | 496 | - | 49,624 |
| Total equipment and distribution system | 2,342,942 | 30,616 | - | 2,373,558 |
| Construction in progress | - | 30,120 | 30,120 | - |
| Total | \$ 2,342,942 | \$ 60,736 | \$ 30,120 | \$ 2,373,558 |

| | | | | Capital Assets - Net |
|-----------------------------|-------------------------|-------------|-----------------------------|-----------------------------|
| Accumulated Depreciation | | | | |
| Balance at June 30, 2017 | Current Depreciation | Deletions | Balance at June 30, 2018 | Balance at June 30, 2018 |
| \$ 454,382 | \$ 55,582 | \$ - | \$ 509,964 | \$ 594,720 |
| 109,196 | 14,513 | - | 123,709 | 174,671 |
| 158,255 | 18,364 | - | 176,619 | 190,663 |
| 23,274 | 2,586 | - | 25,860 | 25,865 |
| 125,430 | 50,186 | - | 175,616 | 326,247 |
| 38,422 | 5,078 | - | 43,500 | 6,124 |
| 908,959 | 146,309 | - | 1,055,268 | 1,318,290 |
| - | - | - | - | - |
| \$ 908,959 | \$ 146,309 | \$ - | \$ 1,055,268 | \$ 1,318,290 |

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, 2018

| | <u>Amended Budget</u> | <u>Actual</u> | <u>Positive (Negative) Variance</u> |
|--|---------------------------|--------------------------|---|
| Operating revenues - sales | | | |
| Residential | \$ 6,400,000 | \$ 6,139,210 | \$ (260,790) |
| Commercial | 15,560,000 | 15,377,008 | (182,992) |
| Industrial | 10,050,000 | 9,274,947 | (775,053) |
| Public authority | 300,000 | 289,087 | (10,913) |
| Street lighting | 225,000 | 230,933 | 5,933 |
| Green energy | - | 1,375 | 1,375 |
| Yard lights | 155,000 | 123,148 | (31,852) |
| Total operating revenues - sales | <u>32,690,000</u> | <u>31,435,708</u> | <u>(1,254,292)</u> |
| Other operating revenues | | | |
| Forfeited discounts | 60,000 | 62,418 | 2,418 |
| Merchandise and jobbing | 70,000 | 139,731 | 69,731 |
| Sale of scrap | 35,000 | 65,256 | 30,256 |
| Recovery of bad debts | 200 | - | (200) |
| MISO income | 3,170,000 | 3,090,792 | (79,208) |
| Miscellaneous | 40,000 | 48,041 | 8,041 |
| Total other operating revenues | <u>3,375,200</u> | <u>3,406,238</u> | <u>31,038</u> |
| Nonoperating revenues | | | |
| Rental income | 46,500 | 45,356 | (1,144) |
| Pole rental income | 68,000 | 77,552 | 9,552 |
| Reimbursements | 91,300 | 893,101 | 801,801 |
| Interest income | 350,000 | 241,790 | (108,210) |
| Change in fair market value of investments | - | (244,001) | (244,001) |
| Gain/(Loss) on sale of assets | - | (201,668) | (201,668) |
| Total nonoperating revenues | <u>555,800</u> | <u>812,130</u> | <u>256,330</u> |
| Total revenues | <u>36,621,000</u> | <u>35,654,076</u> | <u>(966,924)</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, 2018

| | Amended Budget | Actual | Positive (Negative) Variance |
|--------------------------------------|-------------------|-------------------|------------------------------------|
| Purchase power expense | | | |
| Salaries and wages | \$ 62,000 | \$ 18,631 | \$ 43,369 |
| Payroll taxes and fringes | 142,700 | 164,832 | (22,132) |
| Purchased power | 23,770,500 | 20,569,001 | 3,201,499 |
| Trap and transfer | 250 | - | 250 |
| Union street fish ladder | 250 | 8 | 242 |
| Professional and contractual | 96,000 | 110,145 | (14,145) |
| Professional development | 500 | 1,496 | (996) |
| Operation supplies | 5,200 | 3,840 | 1,360 |
| Communications | 250 | 549 | (299) |
| Safety | 3,500 | 2,933 | 567 |
| Transportation | 7,000 | 6,260 | 740 |
| Equipment rental | 11,400 | 3,799 | 7,601 |
| | | | |
| Total purchase power expenses | 24,099,550 | 20,881,494 | 3,218,056 |

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, 2018

| | Amended Budget | Actual | Positive (Negative) Variance |
|---|-------------------|------------------|------------------------------------|
| Distribution expense | | | |
| Salaries and wages | \$ 1,213,000 | \$ 1,128,352 | \$ 84,648 |
| Payroll taxes and fringes | 1,616,000 | 1,285,965 | 330,035 |
| Substation | 120,000 | 318,631 | (198,631) |
| Overhead lines | 205,000 | 186,119 | 18,881 |
| Underground lines | 30,000 | 32,711 | (2,711) |
| Storm work | 50,000 | 115 | 49,885 |
| Electric meters | 6,000 | 25,625 | (19,625) |
| Street lighting | 230,000 | 222,256 | 7,744 |
| Traffic signals | 5,000 | (28,017) | 33,017 |
| Plant and structures | 82,000 | 89,573 | (7,573) |
| Load and dispatching contractual services | 31,500 | 32,265 | (765) |
| Professional services | 94,000 | 59,034 | 34,966 |
| Professional development | 65,000 | 58,728 | 6,272 |
| Operation supplies | 301,400 | 186,530 | 114,870 |
| Utilities | 112,500 | 112,615 | (115) |
| Safety | 38,000 | 29,265 | 8,735 |
| Transportation | 28,000 | 34,696 | (6,696) |
| Equipment rental | 16,600 | (24,558) | 41,158 |
| Inventory adjustment | 10,000 | (56,110) | 66,110 |
| Miscellaneous | 7,500 | 7,236 | 264 |
| Total distribution expense | 4,261,500 | 3,701,031 | 560,469 |
| Transmission expense | | | |
| Salaries and wages | 297,600 | 222,698 | 74,902 |
| Substation | 50,000 | 82,257 | (32,257) |
| Overhead lines | 23,000 | 17,219 | 5,781 |
| MISO | 36,000 | 35,971 | 29 |
| Load and dispatching | 13,500 | 12,735 | 765 |
| Equipment rental | 3,000 | 645 | 2,355 |
| Inventory adjustment | - | 37,617 | (37,617) |
| Miscellaneous | 102,000 | 57,747 | 44,253 |
| Total transmission expense | 525,100 | 466,889 | 58,211 |

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, 2018

| | Amended Budget | Actual | Positive (Negative) Variance |
|--|---------------------------|----------------|---|
| Customer accounting expense | | | |
| Salaries and wages | \$ 154,000 | \$ 140,303 | \$ 13,697 |
| Meter reading | 108,500 | 94,667 | 13,833 |
| Payroll taxes and fringes | 165,800 | 147,525 | 18,275 |
| Office supplies | 4,200 | 4,366 | (166) |
| Postage | 33,000 | 22,626 | 10,374 |
| Stationary and printing | 4,000 | 334 | 3,666 |
| Professional and contractual | 13,000 | 11,078 | 1,922 |
| Uncollectible accounts | 10,000 | 2,540 | 7,460 |
| Collection expense | 5,000 | 1,870 | 3,130 |
| Data processing | 25,000 | 18,321 | 6,679 |
| Professional development | 5,000 | 3,212 | 1,788 |
| Transportation | 4,500 | 2,391 | 2,109 |
| Equipment rental | 14,000 | 20,604 | (6,604) |
| Miscellaneous | 15,550 | 7,522 | 8,028 |
| Total customer accounting expense | 561,550 | 477,359 | 84,191 |
| Public service expense | | | |
| Salaries and wages | 13,300 | 42,682 | (29,382) |
| Payroll taxes and fringes | 9,700 | 9,204 | 496 |
| Office supplies | - | 1,078 | (1,078) |
| Public service information | 570,000 | 395,915 | 174,085 |
| Total public service expense | 593,000 | 448,879 | 144,121 |

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, 2018

| | Amended Budget | Actual | Postive (Negative) Variance |
|---|-------------------|---------------------|-----------------------------------|
| General administration expense | | | |
| Salaries | \$ 515,700 | \$ 526,751 | \$ (11,051) |
| Payroll taxes and fringes | 474,100 | 417,784 | 56,316 |
| Professional development | 25,000 | 11,602 | 13,398 |
| Professional and contractual | 67,400 | 96,076 | (28,676) |
| Office supplies | 21,000 | 15,365 | 5,635 |
| Fees and per diems | 85,000 | 62,348 | 22,652 |
| Special services | 7,000 | 3,188 | 3,812 |
| Legal fees | 65,000 | 40,266 | 24,734 |
| Utilities | 4,400 | 9,630 | (5,230) |
| Printing and publishing | 5,000 | 3,862 | 1,138 |
| Transportation | 1,500 | 854 | 646 |
| Miscellaneous | 5,000 | 5,235 | (235) |
| Total general administration expense | 1,276,100 | 1,192,961 | 83,139 |
| Other expenses | | | |
| Insurance - general | 70,720 | 67,619 | 3,101 |
| City fee | 1,820,000 | 1,745,395 | 74,605 |
| Depreciation | 2,605,000 | 2,635,190 | (30,190) |
| Total other expenses | 4,495,720 | 4,448,204 | 47,516 |
| Total operating expenses | 35,812,520 | 31,616,817 | (4,195,703) |
| Transfers | | | |
| Transfer in | 125,000 | 125,000 | - |
| Change in net position | \$ 933,480 | \$ 4,162,259 | \$ 3,228,779 |

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, 2018

| | Amended Budget | Actual | Positive (Negative) Variance |
|-------------------------------------|---------------------|--------------------|------------------------------------|
| Operating revenues - sales | | | |
| Charges for services | \$ 319,000 | \$ 347,847 | \$ 28,847 |
| Merchandising and jobbing | - | 402 | 402 |
| Total operating revenues | 319,000 | 348,249 | 29,249 |
| Non-operating revenues | | | |
| Reimbursements | 53,400 | 75,465 | 22,065 |
| Interest income | 500 | 285 | (215) |
| Total non-operating revenues | 53,900 | 75,750 | 21,850 |
| Total revenues | 372,900 | 423,999 | 51,099 |
| Fiber expenses | | | |
| Salaries and wages | 80,800 | 56,867 | 23,933 |
| Payroll taxes and fringes | 94,600 | 70,845 | 23,755 |
| Operation supplies | 1,000 | 1,421 | (421) |
| Software and hardware | 5,400 | 3,150 | 2,250 |
| Professional and contractual | 1,500 | 2,639 | (1,139) |
| Professional development | 2,500 | 932 | 1,568 |
| Transportation | 13,000 | 10,986 | 2,014 |
| Pole attachment fees | - | 11,016 | (11,016) |
| Repair and Maintenance | 20,000 | 12,871 | 7,129 |
| Miscellaneous | - | 299 | (299) |
| Total fiber expenses | 218,800 | 171,026 | 47,774 |
| WIFI expenses | | | |
| Operation and maintenance | 29,800 | 27,646 | 2,154 |
| Other expenses | | | |
| Insurance and bonds | 1,000 | 467 | 533 |
| City fee | 15,975 | 17,427 | (1,452) |
| Depreciation | 145,000 | 146,309 | (1,309) |
| Total other expenses | 161,975 | 164,203 | (2,228) |
| Total operating expenses | 410,575 | 362,875 | 47,700 |
| Transfers | | | |
| Transfers out | 125,000 | 125,000 | - |
| Change in net position | \$ (162,675) | \$ (63,876) | \$ 3,399 |

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 17, 2018

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, 2018, 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 17, 2018.

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.

Vredendael Haefner LLC