

MUNICIPAL EMPLOYEES' BENEFIT TRUST

Financial Statements

For the Years Ended December 31, 2016 and 2015

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Independent Auditor's Report

**To the Cities' Municipal Employees' Benefit Trust Committee
Municipal Employees' Benefit Trust
Bellevue, Washington**

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the Municipal Employees' Benefit Trust (the Trust), which comprise the statements of net assets as of December 31, 2016 and 2015, and the related statements of changes in net assets for the years then ended, and the related notes to the financial statements.

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 audits. We conducted our audits 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 opinion.



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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets of the Trust as of December 31, 2016 and 2015, and the changes in its net assets for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

The accompanying financial statements are those of the Trust, which is established under the employee retirement benefit plans (the Plans) of certain entities in the State of Washington as described in Note 1. These financial statements do not purport to present the net assets available for benefits of the individual Plans and do not contain disclosures necessary for a fair presentation of the net assets available for benefits of the individual Plans in accordance with accounting principles generally accepted in the United States of America.

Clark Nuber P.S.

Certified Public Accountants
July 6, 2017

MUNICIPAL EMPLOYEES' BENEFIT TRUST

**Statements of Net Assets
December 31, 2016 and 2015**

	<u>2016</u>	<u>2015</u>
Assets:		
Investments at fair value-		
Mutual funds	\$ 441,095,412	\$ 357,361,257
Collective trust fund	123,602,515	113,184,913
Common and preferred stocks	139,008,671	184,732,384
Money market funds and cash	<u>3,644,442</u>	<u>24,805,947</u>
Total investments at fair value	707,351,040	680,084,501
Receivables-		
Accrued investment income	1,077,106	1,188,493
Notes receivable from participants	<u>8,974,205</u>	<u>9,271,566</u>
Total receivables	<u>10,051,311</u>	<u>10,460,059</u>
Total Assets	717,402,351	690,544,560
Liabilities:		
Accrued administrative fees	<u>474,906</u>	<u>617,113</u>
Total Liabilities	<u>474,906</u>	<u>617,113</u>
Net Assets	<u>\$ 716,927,445</u>	<u>\$ 689,927,447</u>

See accompanying notes.

MUNICIPAL EMPLOYEES' BENEFIT TRUST

**Statements of Changes in Net Assets
For the Years Ended December 31, 2016 and 2015**

	<u>2016</u>	<u>2015</u>
Additions:		
Contributions-		
Employer	\$ 18,231,462	\$ 18,038,380
Employee	21,182,311	20,793,463
Rollovers	<u>517,781</u>	<u>174,852</u>
Total contributions	39,931,554	39,006,695
Investment income (loss)-		
Interest and dividends	12,978,281	21,273,532
Net appreciation (depreciation) in fair value of investments	<u>33,579,514</u>	<u>(28,523,437)</u>
Net investment income (loss)	<u>46,557,795</u>	<u>(7,249,905)</u>
Total Additions	86,489,349	31,756,790
Deductions:		
Benefits paid to participants	55,264,705	42,298,701
Insurance premiums	1,952,862	1,927,380
Administrative expenses	<u>2,271,784</u>	<u>2,401,107</u>
Total Deductions	59,489,351	46,627,188
Net Increase (Decrease) in Net Assets	26,999,998	(14,870,398)
Net Assets:		
Beginning of year	<u>689,927,447</u>	<u>704,797,845</u>
End of Year	<u>\$ 716,927,445</u>	<u>\$ 689,927,447</u>

See accompanying notes.

MUNICIPAL EMPLOYEES' BENEFIT TRUST

Notes to Financial Statements For the Years Ended December 31, 2016 and 2015

Note 1 - Overview/Description of the Trust

The following description of the Municipal Employees' Benefit Trust (the Trust) is provided for general information purposes only. More complete information regarding the Trust's provisions may be found in the Trust document and individual entity plan documents.

General - The Trust was created to manage the assets of the employee retirement benefit plans (the Plans) of certain entities in the State of Washington, which currently includes the cities of Bellevue, Edmonds, Federal Way, Kirkland, Mill Creek, Redmond, Woodinville and the North East King County Regional Public Safety Communication Agency (NORCOM) (collectively, the Cities). Each entity has an individual plan document, which governs its participation, contributions and disbursements. Each of the Cities withdrew from, or elected not to participate in, coverage under the Federal Old Age, Survivors, Disability and Health Insurance Act (Social Security). In lieu of such coverage, the Cities created the Plans, whereby both the employee and employer make contributions to the Plans to provide retirement, survivor and disability benefits otherwise provided by Social Security. The Trust is comprised of two levels of Social Security replacement. Regular employees participate in MEBT I with benefits invested primarily in a pooled balanced fund. Those participants nearing retirement may choose to invest in a short term investment fund. Partially benefiting employees who are not eligible for PERS or LEOFF participate in MEBT II with benefits invested in a short term investment fund. The Trust and Plans are not subject to the provisions of the Employee Retirement Income Security Act of 1974.

Eligibility - In each entity, all regular (40 hours per week) and part-time (20 hours per week) employees are immediately eligible upon the date of employment. With the exception of Edmonds, Federal Way, Woodinville and NORCOM, all temporary (hourly) employees are also eligible when hired. Bellevue, Kirkland and Redmond PERS hourly/partially benefited employees are not eligible.

Contributions - The Plans generally provide that the employers make contributions equal to those that would be required had the Cities not withdrawn from or elected not to participate in Social Security. Employer contributions to the Plans, which are made according to each entity's Plan, are used to pay administrative expenses, operating costs and other employee benefits, including disability coverage for employees and survivor benefits to beneficiaries.

The Plans also require that the employees contribute 100% of the amount that would be required for Social Security, except for Bellevue, Kirkland and Redmond MEBT I employees, whose contributions to the Plans are optional. Depending on the individual entity's Plan, employees may make their contributions on a before or after tax basis. Additionally, depending on the individual entity's Plan, these employees may elect to make additional voluntary contributions to the Plans on a before or after tax basis, subject to certain conditions and restrictions, as defined in the Plans' documents and subject to certain requirements set forth by the Internal Revenue Code (IRC).

Participant Accounts - Each participant's account is credited with the participant's contribution and an allocation of (a) the respective entity's contribution, net of expenses and insurance premiums, (b) forfeitures of terminated participants' nonvested accounts and (c) Trust earnings or losses, participant fees or other listed items. Trust earnings or losses are reflected in each participant's account based on the daily change in the Trust's unit value. The benefit to which a participant is entitled is limited to the participant's vested account balance.

The Plans' Administration and Trustee - The Trust is administered by the Cities' Municipal Employees' Benefit Trust Committee (the Committee), which is appointed by the Bellevue City Manager. The Plans' investments are held under a trust agreement with Broadridge Matrix Trust Company (Broadridge Matrix). An Investment Advisory Committee (IAC), which consists of a member from each of the Cities, provides advice to the Committee on the Trust's investment activities.

MUNICIPAL EMPLOYEES' BENEFIT TRUST

Notes to Financial Statements For the Years Ended December 31, 2016 and 2015

Note 1 - Continued

All members are voting members of the IAC if their entity has five or more years of membership in the Trust. A minimum of five IAC members need to be present to vote on a recommendation to be considered by the Trust.

Vesting - Employee contributions to the Trust are fully vested at all times. Employer contributions are vested as follows for each entity:

Bellevue - Employer contributions vest at 10% at the end of twelve months of participation and then at 0.83% for each additional month of participation. Employees become fully vested after ten years of participation.

Edmonds, Kirkland and Mill Creek - Employer contributions vest at 10% at the end of twelve months of participation and then at 1.25% for each additional month of participation. Employees become fully vested after seven years of participation.

Federal Way - Employer contributions vest at 20% per year and become fully vested after five years of service.

Redmond and NORCOM - Employer contributions vest at 20% after twelve months and at 1.66% for each additional month. Employees become fully vested after five years of service.

Woodinville - Employer contributions are 100% vested at all times.

Forfeitures - Forfeitures become part of an unallocated account within each Plan, which is allocated to the Plans' respective participants on a periodic basis based on a prescribed formula related to employer contributions. Total forfeitures allocated in 2016 and 2015 were approximately \$580,000 and \$613,000, respectively.

Temporary/Hourly/Partially Benefited Employees - The Plans (except for the Plans of Edmonds, Federal Way, Woodinville and NORCOM) allow participation by temporary/hourly/partially benefited employees of the Cities. The part of the Plan for the temporary/hourly/partially benefited employees is commonly referred to as MEBT II. Edmonds, Federal Way, Woodinville and NORCOM temporary/hourly employees are covered by Social Security. These participants do not share in the distribution of the Plans' earnings or in the risk of any of the Plans' investment losses.

Benefit Payments - The Plans provide that participants may make withdrawals of basic and extra after tax contributions, subject to certain conditions and limitations outlined in the Plans' documents. In addition, the Plans provide that in the event of hardship (as defined in the Plans' documents), participants may make withdrawals from their before or after tax contributions, subject to certain limitations and restrictions. Upon termination of service, death, disability or retirement, participants or their beneficiaries may elect to receive their vested account balances in a lump-sum distribution, in monthly, quarterly, or annual installments, or in annuity payments as determined by provisions of the Plans.

Notes Receivable From Participants - Bellevue, Federal Way, Kirkland and Redmond allow participants to obtain loans of up to 50% of their vested account balances, not to exceed \$50,000. The interest rate charged on loans is equal to the prime rate for the city of Federal Way and the prime rate plus 1.0% for the cities of Bellevue, Kirkland and Redmond. For 2016 and 2015, the interest rate on outstanding participant loans ranged from 3.25% to 8.25%.

Insurance Premiums - Most of the Cities have purchased survivor and disability insurance coverage for plan participants. The insurance carrier, The Standard Insurance Company, provides surviving beneficiaries with coverage in the event of death, and disabled participants with coverage in the event of a disabling condition, as described in such policy.

MUNICIPAL EMPLOYEES' BENEFIT TRUST

Notes to Financial Statements For the Years Ended December 31, 2016 and 2015

Note 1 - Continued

The premiums for these policies, with the exception of life insurance premiums at Edmonds and Woodinville, are deducted from the Cities overall contributions to the Plans, with the remainder deposited into the Trust. The cities of Edmonds, Woodinville and NORCOM replaced survivor insurance with term life insurance, which is wholly or partially paid by the employees on an after-tax basis.

Plan Termination - Although the Cities have no intent to do so, they have the right to reduce, suspend or completely discontinue contributions to the Plans. Upon such action by any participating entity, participant accounts related to that entity would become fully vested.

Investment Policy - The Committee has established an Investment Policy Statement that the Trustee, Broadridge Matrix, must follow. The approved target asset allocation of the Trust is as follows at December 31:

	<u>2016</u>	<u>2015</u>
Equities - domestic	40.5%	40.5%
Equities - international	13.5%	13.5%
Fixed income	36.0%	36.0%
Liquid alternatives	10.0%	10.0%
Cash and cash equivalents (kept to a workable minimum for cash flow)		

For any month-end allocation varying more than 20% from the target percentages, the Chair of the Committee may instruct the trustee to sell assets from the asset class in question, sufficient to bring that asset class back to within a 10% deviation from its target, and allocate to the other asset classes to bring those asset classes back towards their targets. A rebalance is not required if the allocation returns within the target percentages prior to rebalancing.

Note 2 - Significant Accounting Policies

Basis of Accounting - The accompanying financial statements are maintained on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). Revenues are recognized when earned and expenses are recognized when incurred.

Use of Estimates - The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Payment of Benefits - Benefit payments are recorded when paid. There was approximately \$163,000 and \$565,000 allocated to the accounts of persons who have elected to withdraw from the plan but have not yet been paid at December 31, 2016 and 2015, respectively.

Investment Valuation and Income Recognition - The Trust's investments are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. See Note 3 for discussion of fair value measurements.

MUNICIPAL EMPLOYEES' BENEFIT TRUST

Notes to Financial Statements For the Years Ended December 31, 2016 and 2015

Note 2 - Continued

Purchases and sales are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Net appreciation or depreciation in the fair value of investments represents the change in fair value from the beginning to the end of the Trust's fiscal year or from the date of purchase to the end of the Trust's fiscal year, if purchased during the current year, plus realized gains and losses.

Notes Receivable From Participants - Notes receivable from participants are measured at their unpaid principal balance. Accrued but unpaid interest, if any, would not have a material impact on the Plan's financial statements. If a participant ceases to make loan repayments and the plan administrator deems the participant loan to be in default, the participant loan balance is reduced and a benefit payment is recorded.

Risks and Uncertainties - Investments are exposed to various risks such as interest rate, market and credit risk. Due to the level of risk associated with certain investments and the level of uncertainty related to changes in the value of investments, it is reasonably possible that changes in risks in the near term would materially affect participants' account balances and the amounts reported in the statements of net assets and the statements of changes in net assets.

Subsequent Events - The Cities have evaluated subsequent events through July 6, 2017, the date on which the financial statements were available to be issued.

Note 3 - Fair Value Measurements

U.S. GAAP provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

The three levels of the fair value hierarchy are described as follows:

Level 1 - Unadjusted quoted prices available in active markets for identical assets or liabilities;

Level 2 - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; or

Level 3 - Unobservable inputs that are significant to the fair value measurement.

A financial instrument's level within the fair value hierarchy is based upon the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2016 and 2015.

Mutual Funds - Valued at the daily closing price as reported by the fund. Mutual funds held by the Plan are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily Net Asset Value (NAV) and to transact at that price. The mutual funds held by the Plan are deemed to be actively traded.

MUNICIPAL EMPLOYEES' BENEFIT TRUST

**Notes to Financial Statements
For the Years Ended December 31, 2016 and 2015**

Note 3 - Continued

Collective Trust Fund - Valued at the NAV of units of a bank collective trust. The NAV, as provided by the fund's trustee, is used as a practical expedient to estimate fair value. The NAV is based on the fair value of the underlying investments held by the fund less its liabilities. This practical expedient is not used when it is determined to be probable that the fund will sell the investment for an amount different than the reported NAV. Participant transactions (purchases and sales) may occur daily.

Common and Preferred Stocks - Valued at the closing price reported on the active market on which the individual securities are traded.

Money Market Funds and Cash - Money market funds are valued similar to mutual funds as described above. Cash is valued at cost, which approximates fair value.

The following tables set forth by level, within the fair value hierarchy, the Trust's assets at fair value as of December 31:

	Fair Value Measurements as of December 31, 2016			
	Level 1	Level 2	Level 3	Total
Mutual funds	\$ 441,095,412	\$ -	\$ -	\$ 441,095,412
Common and preferred stocks	139,008,671			139,008,671
Money market funds and cash	3,644,442			3,644,442
Total Assets in the Fair Value Hierarchy	\$ 583,748,525	\$ -	\$ -	583,748,525
Investments measured at NAV ^(a)				123,602,515
Total Investments at Fair Value				\$ 707,351,040

	Fair Value Measurements as of December 31, 2015			
	Level 1	Level 2	Level 3	Total
Mutual funds	\$ 357,361,257	\$ -	\$ -	\$ 357,361,257
Common and preferred stocks	184,732,384			184,732,384
Money market funds and cash	24,805,947			24,805,947
Total Assets in the Fair Value Hierarchy	\$ 566,899,588	\$ -	\$ -	566,899,588
Investments measured at NAV ^(a)				113,184,913
Total Investments at Fair Value				\$ 680,084,501

(a) In accordance with Subtopic 820-10, investments that were measured at fair value using the NAV per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the line items presented in the statements of net assets.

MUNICIPAL EMPLOYEES' BENEFIT TRUST

**Notes to Financial Statements
For the Years Ended December 31, 2016 and 2015**

Note 3 - Continued

The following sets forth additional disclosures of the Trust's investments, whose fair value is estimated using NAV per share (or its equivalent), as of December 31:

	<u>2016 Fair Value</u>	<u>2015 Fair Value</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Collective trust fund- State Street S&P 500 Flagship Fund ^(b)	\$123,602,515	\$113,184,913	Daily	None

(b) The investment objective of the fund is to approximate as closely as practicable, before expenses, the performance of the S&P 500 Index over the long term. There were no unfunded commitments at December 31, 2016 and 2015.

Note 4 - Relative Share of the Trust Assets

The relative share of the Trust's assets for each entity is as follows at December 31:

	<u>2016</u>	<u>2015</u>
Bellevue	48.3%	49.1%
Redmond	19.4%	19.2%
Kirkland	15.0%	14.6%
Edmonds	7.2%	7.3%
Federal Way	7.1%	6.8%
NORCOM	1.2%	1.1%
Mill Creek	1.1%	1.2%
Woodinville	0.7%	0.7%
	<u>100.0%</u>	<u>100.0%</u>

Note 5 - Administrative Expenses

The administrative expenses charged directly to the Trust consist of the following for the years ended December 31:

	<u>2016</u>	<u>2015</u>
Trustee and recordkeeper	\$ 412,372	\$ 451,848
Legal and accounting	96,876	114,458
Asset management and other	1,762,536	1,834,801
	<u>\$ 2,271,784</u>	<u>\$ 2,401,107</u>

MUNICIPAL EMPLOYEES' BENEFIT TRUST

**Notes to Financial Statements
For the Years Ended December 31, 2016 and 2015**

Note 5 - Continued

Administrative expenses as a percentage of average net assets are as follows for the years ended December 31:

	<u>2016</u>	<u>2015</u>
Trustee and recordkeeper	0.06%	0.07%
Legal and accounting	0.01%	0.02%
Asset management and other	<u>0.25%</u>	<u>0.27%</u>
	<u>0.32%</u>	<u>0.35%</u>

Note 6 - Federal Income Taxes

Each entity has received a determination letter from the Internal Revenue Service (IRS) stating that its Plan qualifies for exemption from taxation. The Plans have been amended since receiving the latest determination letter; however, the Plan's administrators believe the Plans are designed in compliance with the applicable requirements of the IRC and are being operated as designed. Therefore, no provision for income taxes has been made in the accompanying financial statements.

The Plans are subject to audits by the IRS for certain tax periods based on applicable laws and regulations; however, there are currently no audits for any tax periods in progress.