

MD&A
Management's Discussion and Analysis

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MD&A

Management's Discussion & Analysis

As managers of the state of Washington, we offer this narrative overview and analysis of the financial activities for the fiscal year ended June 30, 2017. We present this information in conjunction with the information included in our letter of transmittal, which can be found preceding this narrative, and with the state's financial statements, which follow. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

Financial Highlights

- Total assets and deferred outflows of the state of Washington exceeded its liabilities and deferred inflows by \$23.99 billion (reported as net position). Of this amount, \$(12.11) billion was reported as "unrestricted net position." A negative balance indicates that no funds were available for discretionary purposes.
- The state of Washington's governmental funds reported a combined ending fund balance of \$16.89 billion, an increase of 7.0 percent compared with the prior year.
- The state's capital assets increased by \$1.63 billion, total bond debt increased by \$557.3 million, and the state's net investment in capital assets is \$21.80 billion.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the state of Washington's basic financial statements, which include three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. The focus is on both the state as a whole (government-wide) and the major individual funds. The dual perspectives allow the reader to address relevant questions, broaden the basis for comparison (year-to-year or government-to-government), and enhance the state's accountability.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are designed to provide readers with a broad overview of the state of Washington's finances, in a manner similar to a private sector business.

Statement of Net Position. The *Statement of Net Position* presents information on all of the state of Washington's assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference 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 state of Washington is improving or deteriorating.

Statement of Activities. The *Statement of Activities* presents information showing how the state'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 result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave). The Statement of Activities is focused on both the gross and net cost of various activities (including governmental, business-type, and component unit). This is intended to summarize and simplify the reader's analysis of the revenues and costs of various state activities and the degree to which activities are subsidized by general revenues.

Both of these government-wide financial statements distinguish functions of the state of Washington that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities).

The governmental activities of the state of Washington include education, human services, transportation, natural resources, adult corrections, and general government.

The business-type activities of the state of Washington include the workers' compensation and unemployment compensation programs, as well as Washington's lottery, the Guaranteed Education Tuition Program (GET), and various higher education student services such as housing and dining.

The government-wide financial statements can be found on pages 38-41 of this report.

FUND FINANCIAL STATEMENTS

A fund is a group of related accounts used to maintain control over resources that are segregated for specific activities or objectives. The state of Washington, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the state can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental Funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on fund balances at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for three major funds and an aggregate total for all nonmajor funds. The state's major governmental funds are the General Fund, Higher Education Special Revenue Fund, and the Higher Education Endowment Fund. Individual fund data for the state's nonmajor governmental funds are provided in the form of combining statements elsewhere in this report. The governmental fund financial statements can be found on pages 44-47 of this report.

Proprietary Funds. The state of Washington maintains two different types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. Internal service funds represent an accounting device used to accumulate and allocate costs internally among the state of Washington's various functions. The state of Washington uses internal service funds to account for general services such as motor pool, data processing services, risk management, and employee health insurance. Because internal service funds predominately benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary fund financial statements provide the same type of information as the government-wide financial

statements, but in greater detail. The proprietary fund financial statements provide separate information for the Workers' Compensation Fund, Unemployment Compensation Fund, the Higher Education Student Services Fund, and the Guaranteed Education Tuition Program Fund, which are considered to be major funds, as well as an aggregated total for all nonmajor enterprise funds.

The internal service funds are combined for presentation purposes. Individual fund data for the state's nonmajor proprietary funds are provided in the form of combining statements elsewhere in this report. The proprietary fund financial statements can be found on pages 48-57 of this report.

Fiduciary Funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the state of Washington's own programs. Washington's fiduciary funds include state administered pension plans. The accounting used for fiduciary funds is much like that used for proprietary funds. Individual fund data for the state's fiduciary funds are provided in the form of combining statements elsewhere in this report. The fiduciary fund financial statements can be found on pages 58-59 of this report.

Component Units. Component units that are legally separate from the state and primarily serve or benefit those outside the state are discretely presented. They are either financially accountable to the state, or have relationships with the state such that exclusion would cause the state's financial statements to be misleading or incomplete. The state discretely reports three major component units: the Valley Medical Center, the Washington State Public Stadium Authority and the Health Benefit Exchange, as well as four nonmajor component units. Refer to Note 1 on pages 69-70 for more detailed information. Individual fund data for the state's nonmajor component units are provided in the form of combining statements elsewhere in this report. The component unit financial statements can be found on pages 60-65 of this report.

NOTES TO THE FINANCIAL STATEMENTS

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 68-176 of this report.

OTHER INFORMATION

This report also presents required supplementary information on budgetary comparisons, pension plans and other postemployment benefits information, and infrastructure assets reported using the modified approach.

Required supplementary information can be found on pages 179-209 of this report.

The combining statements referred to earlier are presented immediately following the required supplementary information. Combining financial statements and individual fund schedules can be found on pages 213-277 of this report.

STATE OF WASHINGTON						
Statement of Net Position						
<i>(in millions of dollars)</i>						
	Governmental		Business-Type		Total	
	Activities		Activities			
	2017	2016	2017	2016 *	2017	2016
ASSETS						
Current and other assets	\$ 26,295	\$ 25,362	\$ 26,535	\$ 25,435	\$ 52,830	\$ 50,797
Capital assets	40,512	38,962	3,108	3,030	43,620	41,992
Total assets	66,807	64,324	29,643	28,465	96,450	92,789
DEFERRED OUTFLOWS OF RESOURCES	1,320	771	197	132	1,517	903
LIABILITIES						
Current and other liabilities	5,976	5,643	1,090	968	7,066	6,611
Long-term liabilities outstanding	34,527	32,797	32,143	31,014	66,670	63,811
Total liabilities	40,503	38,440	33,233	31,982	73,736	70,422
DEFERRED INFLOWS OF RESOURCES	235	886	9	59	244	945
NET POSITION						
Net investment in capital assets	21,048	19,942	751	781	21,799	20,723
Restricted	9,718	8,518	4,581	4,485	14,299	13,003
Unrestricted	(3,377)	(2,691)	(8,734)	(8,710)	(12,111)	(11,401)
Total net position	\$ 27,389	\$ 25,769	\$ (3,402)	\$ (3,444)	\$ 23,987	\$ 22,325

*Prior year balances restated for comparability

Government-wide Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. For the state of Washington, total assets and deferred outflows of resources exceed liabilities and deferred inflows of resources by \$23.99 billion at June 30, 2017, as compared to \$22.33 billion as reported at June 30, 2016.

The largest portion of the state's net position (90.9 percent for fiscal year 2017 as compared to 92.8 percent for fiscal year 2016) reflects its net investment in capital assets (e.g., land, buildings, equipment, and intangible assets) less any related debt used to acquire those assets that is still outstanding. The state of Washington uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending.

Although the state of Washington's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

A portion of the state of Washington's net position (59.6 percent for fiscal year 2017 as compared to 58.2 percent for fiscal year 2016) represents resources that are subject to external restrictions on how they may be used. The remaining balance of \$(12.11) billion represents unrestricted net position. The state's overall negative balance in unrestricted net position is largely due to deficits in business-type activities.

In governmental activities, net position increased from \$25.77 billion in fiscal year 2016 to \$27.39 billion in fiscal year 2017. The increase reflects increases in grants and tax revenues that outpaced the increases in expenses.

In business-type activities, the deficit is caused by the workers' compensation program that provides time-loss, medical, disability, and pension payments to qualifying individuals who sustain work-related injuries or develop occupational diseases as a result of their required work activities.

The main benefit plans of the workers' compensation program are funded on rates that will keep the plans solvent in accordance with recognized actuarial principles.

The supplemental pension cost-of-living adjustments (COLAs) granted for time-loss and disability payments, however, are funded on a pay-as-you-go basis. By statute, the state is only allowed to collect enough revenue to fund the current COLA payments.

As previously mentioned, the state's activities are divided between governmental and business-type. The majority of support for governmental activities comes from taxes and intergovernmental grants, while business-type activities are supported primarily through user charges.

STATE OF WASHINGTON						
Changes in Net Position						
<i>(in millions of dollars)</i>						
	Governmental		Business-Type		Total	
	Activities		Activities			
	2017	2016	2017	2016	2017	2016
REVENUES						
Program revenues:						
Charges for services	\$ 6,643	\$ 6,039	\$ 7,524	\$ 6,915	\$ 14,167	\$ 12,954
Operating grants and contributions	15,832	15,357	65	70	15,897	15,427
Capital grants and contributions	1,012	1,113	5	-	1,017	1,113
General revenues:						
Taxes	21,883	20,692	21	21	21,904	20,713
Interest and investment earnings (loss)	614	168	880	999	1,494	1,167
Total revenues	<u>45,984</u>	<u>43,369</u>	<u>8,495</u>	<u>8,005</u>	<u>54,479</u>	<u>51,374</u>
EXPENSES						
General government	(1,945)	(1,658)	-	-	(1,945)	(1,658)
Education - K-12	(11,042)	(10,153)	-	-	(11,042)	(10,153)
Education - Higher education	(7,633)	(7,532)	-	-	(7,633)	(7,532)
Human services	(18,216)	(17,209)	-	-	(18,216)	(17,209)
Adult corrections	(1,062)	(983)	-	-	(1,062)	(983)
Natural resources and recreation	(1,266)	(1,264)	-	-	(1,266)	(1,264)
Transportation	(2,118)	(2,363)	-	-	(2,118)	(2,363)
Interest on long-term debt	(1,027)	(991)	-	-	(1,027)	(991)
Workers' compensation	-	-	(3,269)	(3,238)	(3,269)	(3,238)
Unemployment compensation	-	-	(1,027)	(1,020)	(1,027)	(1,020)
Higher education student services	-	-	(3,022)	(2,494)	(3,022)	(2,494)
Washington's lottery	-	-	(520)	(535)	(520)	(535)
Guaranteed education tuition program	-	-	(306)	152	(306)	152
Other business-type activities	-	-	(190)	(161)	(190)	(161)
Total expenses	<u>(44,309)</u>	<u>(42,153)</u>	<u>(8,334)</u>	<u>(7,296)</u>	<u>(52,643)</u>	<u>(49,449)</u>
Excess (deficiency) of revenues over expenses before contributions to endowments and transfers	1,675	1,216	161	709	1,836	1,925
Contributions to endowments	100	67	-	-	100	67
Transfers	119	152	(119)	(152)	-	-
Special item	-	-	-	(319)	-	(319)
Increase (decrease) in net position	1,894	1,435	42	238	1,936	1,673
Net position - July 1, as restated	<u>25,495</u>	<u>24,334</u>	<u>(3,444)</u>	<u>(3,732)</u>	<u>22,051</u>	<u>20,602</u>
Net position - June 30	<u>\$ 27,389</u>	<u>\$ 25,769</u>	<u>\$ (3,402)</u>	<u>\$ (3,494)</u>	<u>\$ 23,987</u>	<u>\$ 22,275</u>

Governmental Activities. Governmental activities resulted in an increase in the state of Washington's net position of \$1.89 billion. A number of factors were in play including increases in tax revenues and spending on K-12 education and human services.

- Tax revenues increased by \$1.19 billion in fiscal year 2017 as compared to fiscal year 2016 reflecting positive growth in the economy. Sales and use tax reported an increase of \$622.4 million. Sales and use tax are the main tax revenue for governmental activities. Real estate excise tax revenue increased by \$257.9 million. Real estate excise taxes are levied on the sale of real estate. These tax revenue increases reflect the rebounding economy, recovering housing markets, and improving employment picture in Washington.
- Operating grants and contributions grew by \$474.7 million in fiscal year 2017 compared with 2016 and were matched with an increase in human services expenses.
- Expenses grew by \$888.7 million for K-12 education in 2017 as compared to fiscal year 2016. The state is working to meet the requirements of the state Supreme Court's 2012 McCleary ruling to meet its constitutional duty to fund basic education.

Business-Type Activities. Business-type activities increased the state of Washington's net position by \$42.8 million. Workers' compensation, unemployment compensation, and guaranteed education tuition activities contributed to the increase. Key factors contributing to the operating results of business-type activities are:

- The workers' compensation activity increase in net position in fiscal year 2017 was \$70.5 million compared to an increase of \$202.2 million in fiscal year 2016. Premium revenue increased by \$202.1 million as a result of an increase in the number of hours reported by employers and an increase in the number of hours reported by businesses in higher rate classes. Claim costs increased by \$13.4 million in fiscal year 2017 compared

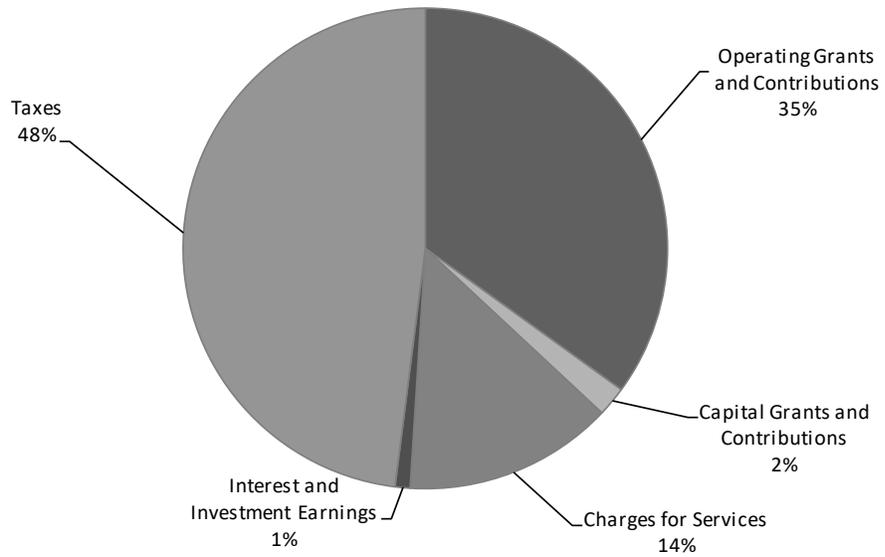
with fiscal year 2016, reflecting little change in the number of time-loss claims. Nonoperating investment income decreased by \$323.6 million as compared to fiscal year 2016, due predominately to a net decrease in realized and unrealized gains on debt securities. The workers' compensation portfolio is 85.9 percent debt securities.

- The unemployment compensation activity reported an operating income in fiscal year 2017 of \$3.8 million compared to \$157.6 million in fiscal year 2016. Washington's unemployment insurance program is an experience-based system with the largest part of an individual employer's tax rate being based on the employer's layoff experience over the past four years. The unemployment rate for the state for June 2017 was 4.5 percent, down from 5.5 percent in June 2016, and the insured rate declined to 1.4 percent in fiscal year 2017 from 1.5 percent in fiscal year 2016. The insured rate decline, results in premium revenue decreasing by 12.9 percent. The \$2.0 million decline in federal aid also reflects the decrease in the unemployment rate.
- The Guaranteed Education Tuition (GET) Program reported a decrease in net position of \$54.8 million, decreasing its funded status to 132.4 percent, down from 136 percent the previous year. This is due to the GET Board authorizing account holders to request refunds of contributions with no penalties.

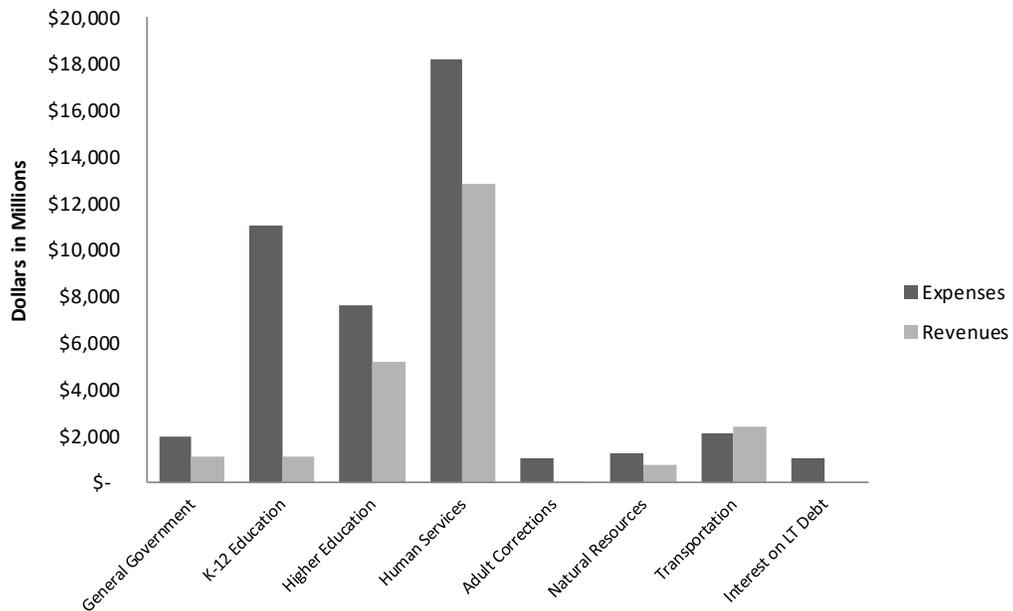
While current year investment returns were up, the actuarial valuation of the obligation for future tuition benefits assumed a higher rate of investment return based on a recent experience study. The valuation also assumed a lower rate of tuition growth in response to recently enacted legislation. Overall the tuition benefit obligation increased by less than a percent.

- The remaining business-type activities reported relatively proportional increases in both operating revenues and expenses when compared to the prior year.

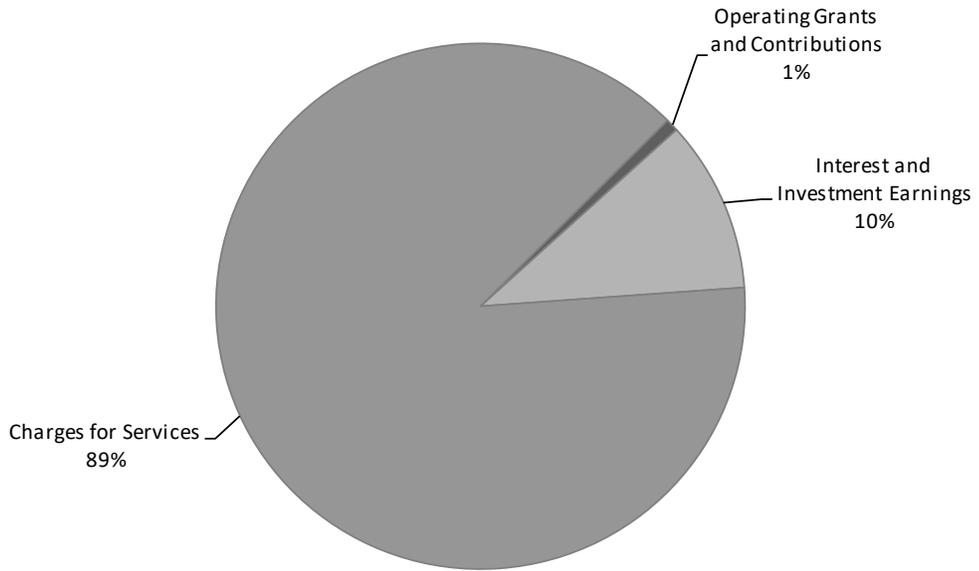
Revenues by Source: Governmental Activities



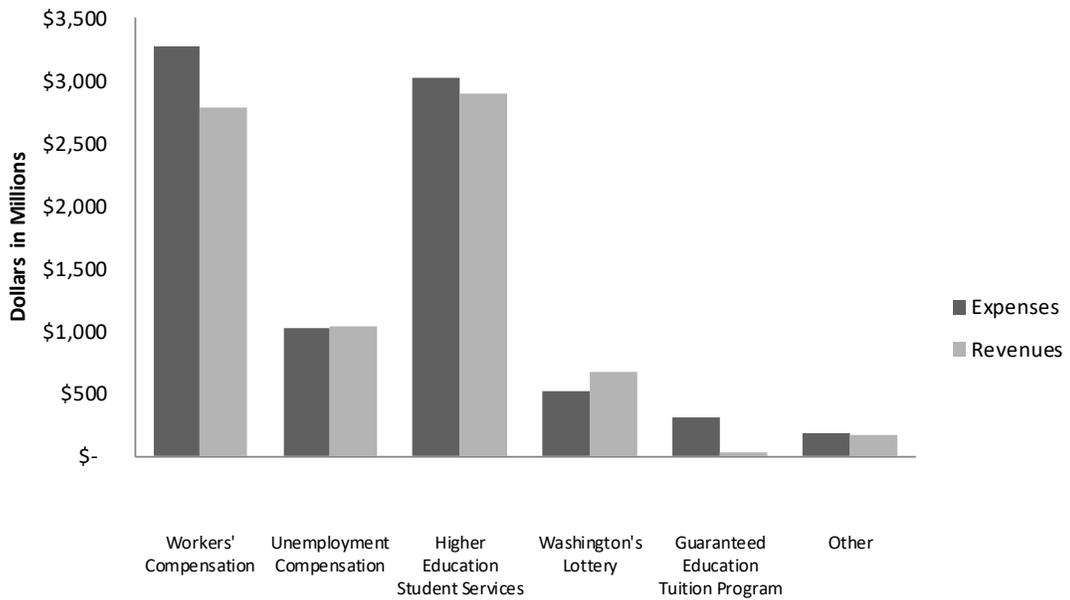
Program Revenues and Expenses: Governmental Activities



Revenues by Source: Business-Type Activities



Program Revenues and Expenses: Business-Type Activities



Financial Analysis of the State's Funds

As noted earlier, the state of Washington uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds. As previously discussed, the focus of the state of Washington's governmental funds is to provide information on near-term inflows, outflows, and fund balances. Such information is useful in assessing the state of Washington's financing requirements.

Fund Balances. At June 30, 2017, the state's governmental funds reported combined ending fund balances of \$16.89 billion. Of this amount, \$2.68 billion or 15.9 percent is nonspendable, either due to its form or legal constraints; and \$6.00 billion or 35.5 percent is restricted for specific programs by external constraints,

constitutional provisions, or contractual obligations. An additional \$5.91 billion or 35.0 percent of total fund balance has been committed to specific purposes. Committed amounts cannot be used for any other purpose unless approved by the Legislature. An additional \$1.28 billion or 7.6 percent of total fund balance has been assigned to specific purposes by management.

The General Fund is the chief operating fund of the state of Washington. The fund balance improved as a result of operations by \$970.8 million in fiscal year 2017, as compared to an \$564.8 million gain in fiscal year 2016. Increased revenues from taxes and targeted spending increases in K-12 education and social and health services combined with a concerted effort to hold the line on other spending were the key contributing factors. Assigned fund balance of \$1.26 billion is reported for fiscal year 2017 and relates to certain accrued and non-cash revenues which are not considered by management to be available for budgetary purposes.

STATE OF WASHINGTON			
General Fund			
<i>(in millions of dollars)</i>			
	Fiscal Year		Difference
	2017	2016	Increase (Decrease)
REVENUES			
Taxes	\$ 19,341	\$ 18,188	\$ 1,153
Federal grants	12,680	12,196	484
Investment revenue (loss)	(5)	26	(31)
Other	1,130	728	402
Total	<u>33,146</u>	<u>31,138</u>	<u>2,008</u>
EXPENDITURES			
Human services	17,959	17,072	887
Education	12,176	11,403	773
Other	1,584	1,646	(62)
Total	<u>31,719</u>	<u>30,121</u>	<u>1,598</u>
Net transfers in (out)	(587)	(628)	41
Other financing sources	131	176	(45)
Net increase (decrease) in fund balance	<u>\$ 971</u>	<u>\$ 565</u>	<u>\$ 406</u>

General Fund expenditures continue to be concentrated in services and programs most vital to citizens – primarily human services and public education.

In addition to the General Fund, the state reports the Higher Education Special Revenue and the Higher Education Endowment Funds as major governmental funds. Significant changes are as follows:

- The change in fund balance of the Higher Education Special Revenue Fund in fiscal year 2017 was a decrease of \$167.7 million compared to an increase of \$31.6 million in fiscal year 2016. The decline in fiscal year 2017 was largely due to a 2.5 percent decrease in federal grants. Revenues showed a modest gain of 2.7 percent reflecting the state’s decision to limit tuition growth to the average percentage growth in the state’s median hourly wage.
- The fund balance for the Higher Education Endowment Fund increased by \$402.8 million in fiscal year 2017. Fiscal year 2017 reported an increase of \$450.5 million in investment earnings compared to last fiscal year.

Proprietary Funds. The state of Washington’s proprietary funds financial statements provide the same type of information found in the government-wide financial statements, but in more detail. Significant changes reported in fiscal year 2017 are as follows:

- The Workers’ Compensation Fund reported an increase in net position of \$70.5 million in fiscal year 2017. Operating revenues increased by \$222.9 million and operating expenses increased by \$31.2 million as compared to fiscal year 2016. As previously reported, operating revenues increased due to an increase in reported hours in higher rate classes and claims expense increased slightly due to an increase in the state’s average annual wage. Investment income decreased \$323.6 million over fiscal year 2016 due to a decrease in net realized and unrealized capital gains.
- Washington’s Unemployment Compensation Fund reported an increase in net position of \$96.3 million. As reported previously, premium revenue increased reflecting a growing workforce and higher taxable wage base. Unemployment benefit claims expense increased slightly by \$6.9 million in fiscal year 2017 as compared to 2016 and federal aid decreased by \$2.0 million over the same period. The slight increase in benefit claims and slight decrease in federal aid are consistent with an overall stable unemployment rate.
- The Guaranteed Education Tuition (GET) Program Fund reported a decrease in net position of \$54.8 million

in fiscal year 2017. As previously reported, the decrease is due primarily to account holders taking advantage this year of the opportunity to receive a refund on their contributions without penalties.

- The Higher Education Student Services Fund and the nonmajor enterprise funds reported consistent activity when compared to the prior year.

Adjustments to Beginning Proprietary Fund Net Position. As described in Note 2 to the financial statements on pages 80 and 81, beginning fund net position of the Higher Education Student Services Fund were adjusted as a result of implementing GASB Statement Nos. 73 and 80.

General Fund Budgetary Highlights

Differences between the original budget of the General Fund and the final amended budget reflect increases in mandatory costs driven by rising caseloads and school enrollment as well as other high priority needs. Changes to estimates are summarized as follows:

- Estimated biennial resources increased by \$3.14 billion over the course of the biennium. The major increase in estimated resources is additional sales tax and excise tax collected.
- Appropriated expenditure authority increased by \$2.17 billion over the biennium to address increases in the state’s mental health and children services programs. The other major increase in appropriation authority was in K-12 education. This is the state working on meeting its obligation under the Supreme Court’s 2012 McCleary ruling to meet its constitutional duty to fund basic education.

The state did not overspend its legal spending authority for the 2015-17 biennium. Actual General Fund revenues and expenditures were 97.9 and 97.4 percent of final budgeted resources and appropriations, respectively, for the 2015-17 biennium.

Capital Assets, Infrastructure, and Bond Debt Administration

Capital Assets. The state of Washington’s investment in capital assets for its governmental and business-type activities as of June 30, 2017, totaled \$43.62 billion (net of accumulated depreciation). This investment in capital assets includes land, infrastructure, museum and historical collections, buildings and other improvements, furnishings,

equipment, and intangible assets, as well as construction in progress.

Washington’s fiscal year 2017 investment in capital assets, net of current year depreciation, increased \$1.63 billion over fiscal year 2016, including increases to the state’s transportation infrastructure of \$808.5 million. The state’s construction in progress includes both new construction and major improvements to state capital facilities and infrastructure. Remaining commitments on these construction projects total \$2.92 billion.

Additional information on the state of Washington’s capital assets can be found in Note 6 beginning on page 118 of this report.

Infrastructure. The state uses the modified approach for

reporting selected infrastructure assets. The modified approach requires that the state meet certain requirements regarding the inventory and maintenance of eligible capital assets, including condition assessments. Under the modified approach, assets are not depreciated and certain maintenance and preservation costs associated with those assets are expensed. Assets accounted for under this approach include approximately 20,797 lane miles of pavement, 3,312 bridges, and 47 highway safety rest areas. Infrastructure asset categories are assessed on a two-year cycle, either on a calendar year or fiscal year basis.

In the past five fiscal years, the state has invested fewer resources for the preservation and maintenance of pavement and bridges than was planned, and invested more than planned for rest areas preservation and maintenance.

STATE OF WASHINGTON						
Capital Assets - Net of Depreciation						
<i>(in millions of dollars)</i>						
	Governmental Activities		Business-Type Activities		Total	
	2017	2016	2017	2016 *	2017	2016
Land	\$ 2,666	\$ 2,666	\$ 70	\$ 69	\$ 2,736	\$ 2,735
Transportation infrastructure and other assets not depreciated	24,838	24,030	5	5	24,843	24,035
Buildings	8,434	7,951	2,521	2,581	10,955	10,532
Furnishings, equipment, and intangible assets	2,009	1,793	220	215	2,229	2,008
Other improvements and infrastructure	1,390	1,277	77	78	1,467	1,355
Construction in progress	1,176	1,245	215	81	1,391	1,326
Total	\$ 40,513	\$ 38,962	\$ 3,108	\$ 3,029	\$ 43,621	\$ 41,991

*Prior year balances restated for comparability

The state’s goal is to maintain 85 percent of pavements and 90 percent of bridges at a condition level of fair or better. The condition of these assets, along with the rating scales, and additional detail comparing planned to actual preservation and maintenance spending are available in the required supplementary information beginning on page 206.

The most recent pavements condition assessment indicates that 93.2 percent of pavements were in fair or better condition. The condition of pavements has remained steady in the last three assessment periods, averaging 92.4 percent in fair or better condition. For fiscal year 2017, actual maintenance and preservation expenditures were 13.1 percent lower than planned, and over the past five fiscal years, the actual expenditures were 8.7 percent lower than planned.

The most recent bridge condition assessment indicates that 91.8 percent of bridges were in good or fair condition. The condition of bridges has remained steady over the last three assessment periods, averaging 91.8 percent in good or fair

condition. For fiscal year 2017, the actual maintenance and preservation expenditures were 1.7 percent lower than planned, and over the past five fiscal years, the actual expenditures were 8.6 percent lower than planned.

Bond Debt. At the end of fiscal year 2017, the state of Washington had general obligation bond debt outstanding including accreted interest and issuance premiums of \$21.03 billion, an increase of 2.5 percent from fiscal year 2016. This debt is secured by a pledge of the full faith and credit of the state. Additionally, the state had authorized \$10.44 billion general obligation debt that remains unissued.

General obligation debt is subject to the limitation prescribed by the State Constitution. The aggregate debt contracted by the state as of June 30, 2017, does not exceed that amount for which payments of principal and interest in any fiscal year would require the state to expend more than 8.3 percent of the arithmetic mean of its general state revenues for the six immediately preceding fiscal years. The arithmetic mean of its general state revenues for fiscal years

2011-2016 is \$16.33 billion. The debt service limitation, 8.30 percent of this mean, is \$1.35 billion. The state's maximum annual debt service as of June 30, 2017, subject to the constitutional debt limitation is \$1.17 billion, or \$176.0 million less than the debt service limitation.

For further information on the debt limit, refer to Schedule 11 in the statistical section of this report or the

Certification of the Debt Limitation of the State of Washington, available from the Office of the State Treasurer at:

<http://tre.wa.gov/wp-content/uploads/Debt-Limit-Report-2017-Final.pdf>.

By statutory provision, the State Finance Committee (SFC) is authorized to supervise and control the issuance of all state bonds, notes, or other evidences of indebtedness. The SFC is composed of the Governor, Lieutenant Governor, and State Treasurer, the latter serving as chairman.

As of June 30, 2017, the state of Washington's general obligation debt was rated Aa1 by Moody's Investor Service, AA+ by Standard & Poor's Rating Group (S & P), and AA+ by Fitch Ratings.

STATE OF WASHINGTON						
Bond Debt						
<i>(in millions of dollars)</i>						
	Governmental		Business-Type		Total	
	Activities		Activities			
	2017	2016	2017	2016	2017	2016
General obligation (GO) bonds	\$ 20,576	\$ 20,039	\$ -	\$ -	\$ 20,576	\$ 20,039
Accreted interest on zero interest rate GO bonds	458	479	-	-	458	479
Revenue bonds	2,326	2,377	2,307	2,215	4,633	4,592
Total	\$ 23,360	\$ 22,895	\$ 2,307	\$ 2,215	\$ 25,667	\$ 25,110

The state had revenue debt outstanding at June 30, 2017, of \$4.63 billion, an increase of \$41.0 million over fiscal year 2016. The increase is primarily related to revenue bonds issued by state colleges and universities. This debt is not supported or intended to be supported by the full faith and credit of the state. Revenue bond debt is generally secured by specific sources of revenue. The exception is the University of Washington and Washington State University which issue general revenue bonds that are payable from general revenues of each university.

General obligation and revenue bonds totaling \$1.16 billion were refunded during the year. Washington's refunding activity produced \$189.8 million in gross debt service savings.

Additional information on the state's bond debt obligations is presented in Note 7 beginning on page 122 of this report.

Conditions with Expected Future Impact

Economic Outlook. Washington is well positioned for economic and population expansion. The state has a diverse industrial and environmental base that supports trade with Pacific Rim countries as well as knowledge-based industries including information technology, health, business, and financial services.

Washington's expanding economy, accelerated gains in hiring, and recovering housing markets have had a positive effect on revenue growth. Further economic growth and a continued expansion in the housing and commercial building markets should keep revenues growing at a sound pace.

That said, in the coming year, legislative leaders and management will be facing a number of challenges including:

- Under legislation approved in 2012, and beginning with the 2013-15 biennium, Washington became the only state in the nation required to pass a budget that balances spending against anticipated revenue over a four-year period.
- Washington continues to address the requirements of the state Supreme Court 2012 McCleary ruling that found the state has failed to meet its constitutional requirement to amply fund basic education. To address these issues, the 2017 Legislature added significant funding, along with a number of policy changes, in HB 2242 and the 2017-19 biennial operating budget.
- During the 2017 legislative session, the Legislature passed a capital budget that only included reappropriations for projects originally funded but not completed in the 2015-17 biennium. No new capital projects have been authorized in the 2017-19 biennium.

Rainy Day Account. In November 2007, Washington state voters ratified Engrossed Substitute Senate Joint Resolution 8206, amending the state's Constitution and establishing the Budget Stabilization Account (BSA). The Constitution details a limited number of circumstances under which funds can be appropriated from the BSA, one of which is a favorable vote of at least three-fifths of the members of each house of the Legislature.

On June 30, 2017, \$1.12 billion was transferred to the BSA from the General Fund in accordance with the provisions of the Constitution. During fiscal year 2017, by three-fifths

vote of each house, the Legislature appropriated \$38.1 million from the BSA solely for emergency fire service mobilization, fire suppression, and fire damage recovery costs. The BSA had a fund balance of \$1.64 billion as of June 30, 2017.

The Guaranteed Education Tuition Program. The funded status of the Guaranteed Education Tuition (GET) Program decreased during fiscal year 2017 reflecting account holders requesting refunds. Engrossed Second Substitute Bill (E2SSB) 5954, which was signed into law by the Governor on July 6, 2015, reduced tuition at all public institutions of higher education during the 2015-16 and 2016-17 academic years and limits tuition growth in future years. Subsequent to the passage of E2SSB 5954, the GET Program Committee authorized account holders, upon request, to receive a refund of their contributions or a fixed payout value, whichever is greater. Account holders have until September 1, 2017, or until 60 days after a new 529 savings plan opens (whichever is later), to request a refund. GET will reopen for new enrollment on November 1, 2017.

Requests for Information

This financial report is designed to provide a general overview of the state of Washington's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Office of Financial Management, Accounting Division, P.O. Box 43127, Olympia, WA 98504-3127.