Washington State Auditor's Office

Troy Kelley

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Financial Statements Audit Report

Port of Pend Oreille
(Pend Oreille Valley Railroad)

Pend Oreille County

For the period January 1, 2012 through December 31, 2013

Published November 24, 2014

Report No. 1013030

Washington State Auditor
Troy Kelley

November 24, 2014

Board of Commissioners
Pend Oreille Valley Railroad
Usk, Washington

Report on Financial Statements

Please find attached our report on the Pend Oreille Valley Railroad's financial statements.

We are issuing this report in order to provide information on the Port's financial condition.

Sincerely,

TROY KELLEY

STATE AUDITOR

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Independent Auditor's 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*

Pend Oreille Valley Railroad
Pend Oreille County
January 1, 2012 through December 31, 2013

Board of Commissioners
Pend Oreille Valley Railroad
Usk, Washington

We have audited, in accordance with 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 the Pend Oreille Valley Railroad, Pend Oreille County, Washington, as of and for the years ended December 31, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the Port's basic financial statements, and have issued our report thereon dated November 14, 2014.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audits of the financial statements, we considered the Port'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Port's internal control. Accordingly, we do not express an opinion on the effectiveness of the Port'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 the Port'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.

In addition, we noted certain matters that we have reported to the management of the Port in a separate letter dated November 18, 2014.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the Port's financial statements are free from material misstatement, we performed tests of the Port's 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 the Port's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Port's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Troy X. Kelley

TROY KELLEY
STATE AUDITOR

November 14, 2014

Independent Auditor's Report on Financial Statements

Pend Oreille Valley Railroad
Pend Oreille County
January 1, 2012 through December 31, 2013

Board of Commissioners
Pend Oreille Valley Railroad
Usk, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the Pend Oreille Valley Railroad, Pend Oreille County, Washington, as of and for the years ended December 31, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the Port's basic financial statements as listed on page 8.

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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 Port'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 Port'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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Pend Oreille Valley Railroad, as of December 31, 2013 and 2012, and the changes in financial position and cash flows thereof for the years 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 9 through 18 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 REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2014 on our consideration of the Port'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 the Port's internal control over financial reporting and compliance.

Troy X. Kelley

TROY KELLEY
STATE AUDITOR

November 14, 2014

Financial Section

Pend Oreille Valley Railroad
Pend Oreille County
January 1, 2012 through December 31, 2013

REQUIRED SUPPLEMENTARY INFORMATION

BASIC FINANCIAL STATEMENTS

2013 Management's Discussion and Analysis

Our discussion and analysis of the Port of Pend Oreille's financial performance provides an overview of the Port's financial activities for the fiscal year ended December 31, 2013.

The Port of Pend Oreille is a Special Purpose Municipal Government. Ports exist to build infrastructure and promote economic development within their districts. Ports are often, though not always, involved in transportation activities. The Port of Pend Oreille operates a Railroad for shipping and receiving operations.

The Port of Pend Oreille was created in 1979 by a vote of the citizens of the Port District. The district encompasses all of Pend Oreille County, Washington. The Port is a special purpose government entity that owns land and operates the Pend Oreille Valley Railroad. The Port's primary mission is to operate the Pend Oreille Valley Railroad.

Three elected Port Commissioners administer the Port. In accordance with the laws of Washington the Commissioners have appointed an Administrative Team which consists of a Manager, Roadmaster, and Chief Mechanical Officer to manage all operations and finances.

The Port owns 61 miles of track in Washington, leases 24 miles of track in Idaho, on which it operates the Pend Oreille Valley Railroad. The Pend Oreille Valley Railroad currently has many customers. The Pend Oreille Valley Railroad interchanges with the Burlington Northern Santa Fe Railway Company at Sandpoint, Idaho to ship and receive cars from the Burlington Northern Santa Fe and Union Pacific Railroads.

Ports do their accounting and financial reporting for their activities very much like a business. The Port of Pend Oreille does not levy nor collect any real or personal property taxes.

The Government Accounting Standards Board has prescribed a new method of financial reporting for all government entities. The Port of Pend Oreille continues to use the model of reporting adopted in 2003.

Issues Facing the Port

With the demand increasing to ship products, the storage cars revenue will decrease as the cars are being taken out of storage as needed. We are hopeful that the freight revenue will increase with an increase in freight operations in the next year. The Port has also invested in their capital projects with the construction of the new shop building addition and paint booth. The Port finds it beneficial that our investment in our shop building and paint booth will increase our shop capabilities and thus increase our shop revenues.

Financial Highlights

- In 2013, the Port's overall business revenues decreased $45,171 or approximately 2.2% under the 2012 business revenue levels.

- The Port's overall operating costs increased in 2013 by $11,656, or approximately less than .01% over 2012 operating expense levels.

- The Port had an overall Net Operating Income of $115,519 in 2013.

- The Port's operating revenues were more than budgeted by $212,894, and the operating expenses were more than budgeted by $97,376.

Using the Annual Report

This report consists of a series of financial statements. The Statement of Net Position, the Statement of Revenues, Expenses, and Changes in Net Position, and the Statement of Cash Flows provide information about the activities of the Port as a whole, and present a longer-term view of the Port's finances.

All of the Port's transactions are reported in one fund. The Port does not maintain any trustee or agency funds.

Reporting the Port as a Whole

Understanding the financial trend of the Port begins with understanding the Statement of Net Position and the Statement of Revenues, Expenses, and Changes in Net Position. Looking at these two reports, you should be able to determine if the Port is financially better this year than it was in the past.

The Statement of Net Position and the Statement of Revenues, Expenses, and Changes in Net Position report information about the Port's financial activities. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private sector companies. All of the current year's revenues and expenses are taken into account regardless of when the cash is received or paid by the Port.

These two reports show the Port's net positon and the changes in them during 2013. The Port's net position is its assets minus its liabilities. This is one measure of financial position of the Port. Over time, increases or decreases in the Port's net position is a good indicator of whether its financial strength is improving or deteriorating. You need to consider other factors not shown on these two financial reports in order to assess the Port's true financial condition. A change in the condition of the Port's asset base is an important factor when assessing the overall financial condition of the Port.

Fund Financial Statements

When the Port charges someone to use property or Port services, the revenue earned is like businesses revenue. The Statement of Revenues, Expenses, and Changes in Net Position is the Port's fund based financial statement.

Since the Port accounts for all of its transactions in one Proprietary Fund, The Port's fund based financial statement is also its entity-wide governmental financial statement as required by GASB 34-38.

The Port as a Whole

The discussion below explains the Ports overall financial situation for the year ended 12/31/2013.

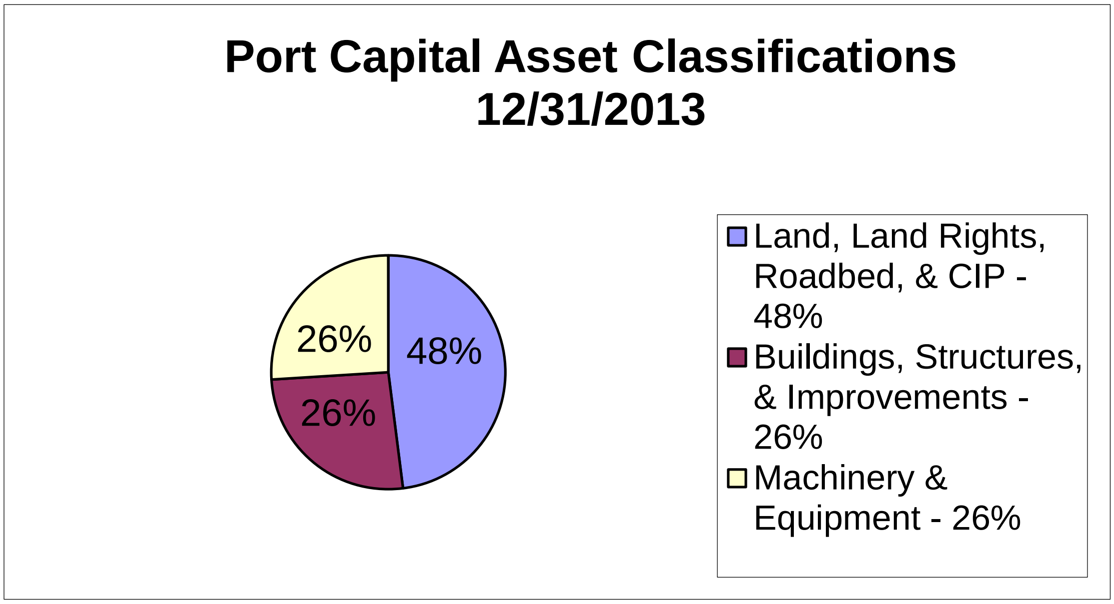
The Port's total assets increased from approximately $6.2 million to $6.5 million since last year. Our analysis below focuses on the change in total assets.

Change in Total Assets (in Millions of Dollars)

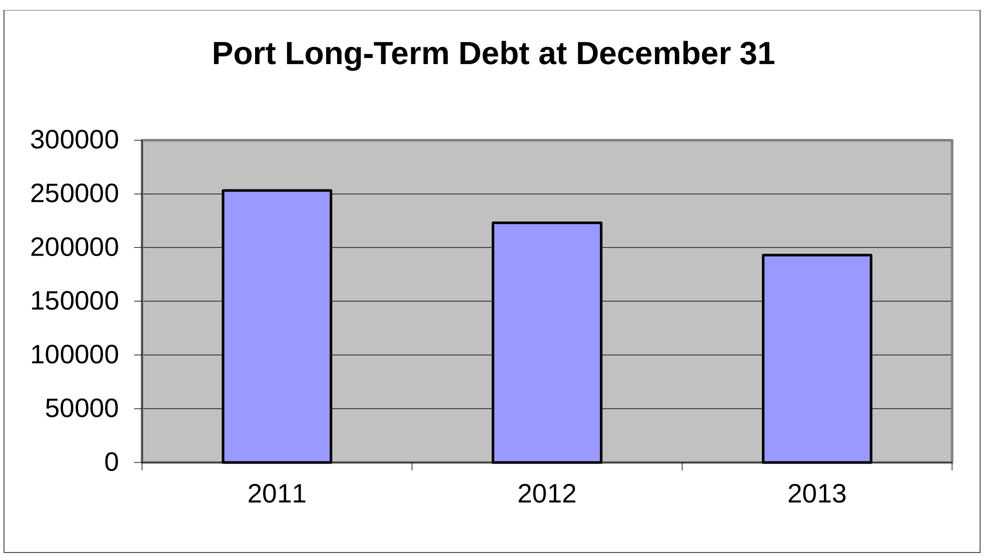
	2012	2013
Total Current Assets	3.8	3.0
Total Restricted Assets	.9	.3
Total Net Capital Assets	1.5	3.2
Total Assets	6.2	6.5

The total current assets and total restricted assets decreased due to the transfer of funds from Capital Improvements Reserves and Operating Expense Fund - Investment for the construction of the new shop building addition and paint booth in 2013. The total restricted assets also decreased due to a decrease in long term investments. Respectively, the total net capital assets increased with the construction of the new shop building addition and paint booth.

The Port maintained a capital asset base of $3,184,731 in 2013, and a capital asset base in 2012 of $1,500,440. The book value of the asset base increased due to the construction of the new shop addition and paint booth. The Port expensed $59,280.50 in depreciation charges in 2013. When the Port invests more than that amount in new capital assets in a year, then the book value of its asset base increases.



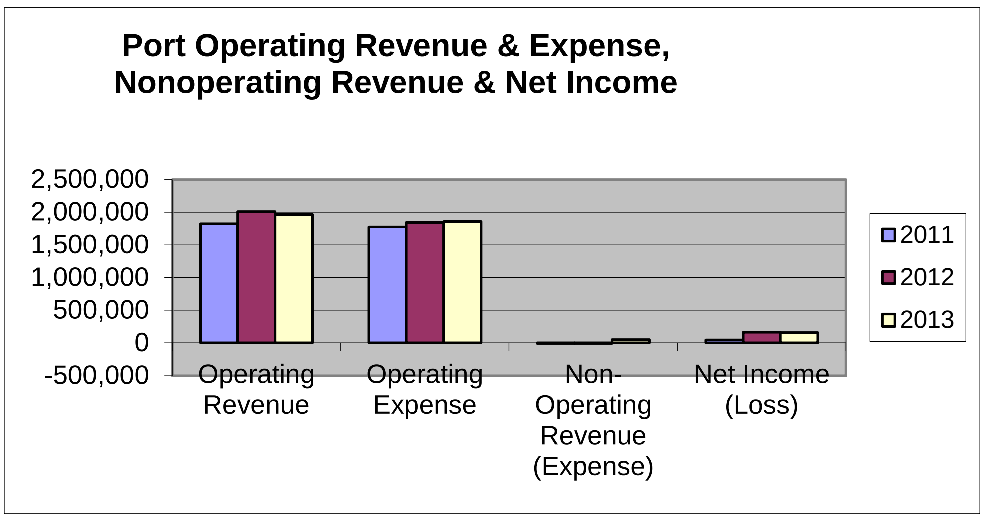
The Port's current liabilities as of 12/31/2013 are debt's that the Port will repay in 2014. The total current liabilities increased in 2013 to $205,950 from $89,002 in 2012 due to the construction costs of the new shop building addition and paint booth. The Port's long term liabilities decreased in 2013 due to the bond debt obligations decreasing each year. The Revenue Bonds outstanding at 12/31/2013 amounted to $193,000, a decrease of $30,000 from $223,000 in 2012.



The Port's Net Investment in Capital Assets, increased by $1,684,291, from $1,500,440 in 2012 to $3,184,731 in 2013. The Unrestricted Net Position decreased by $1,518,677, from $4,414,675 in 2012 to $2,895,998 in 2013. This increase in assets and liabilities in association with the investment in capital assets has resulted consequently in an increase in the Port's overall financial position.

Our further analysis shows our business activities. The Port's total operating revenues decreased by approximately $45,171 from $2,011,545 in 2012 to $1,966,374 in 2013, while the total cost of operations increased by approximately $11,656 from $1,839,200 in 2012 to $1,850,856 in 2013. Thus, creating a net operating income of $115,519 for 2013 compared to a net operating income of $172,345 for 2012. Operating revenues decreased with the decrease in freight operations.

Non operating revenues increased due to a Gain on Disposition of Assets and a decrease in interest income. There was a gain on the disposition of assets in the amount of $47,501 in 2013. Grant revenue was received to aid in the construction of capital assets in the amount of $13,000. There was also grant revenue received which offset the non-operating expense for a signals upgrade project completed in 2013 in the amount of $39,999. Interest income decreased from $6,899 in 2012 to $6,179 in 2013 due to a decline in interest rates and the decrease in Investments. Non operating expenses show a decrease in interest expense on revenue bonds. Interest expense on revenue bonds decreased from $13,525 in 2012 to $12,150 in 2013. Non operating expenses also show an election expense of $4,435 for 2013.



	2011	2012	2013
Operating Revenue	1,825,506	2,011,545	1,966,374
Operating Expense	1,772,431	1,839,200	1,850,856
Non-Operating Revenue (Expense)	-6,346	-6,626	50,095
Net Income (Loss)	46,729	165,719	165,614

Overall, the Port's balance of net position at the beginning of the year was $5,915,115 and increased by $165,614 to arrive at the ending balance in net position of $6,080,729 at the end of 2013.

Contacting the Port's Financial Management

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the Port's finances and to show the Port's accountability for the money it receives. If you have questions about this report, or if you need additional financial information, please contact Kelly Driver, Port Manager, or Susan Bluff, Port Financial Officer, at 1981 Black Road, Usk, WA 99180 or by phone at (509) 445-1090.

2012 Management's Discussion and Analysis

Our discussion and analysis of the Port of Pend Oreille's financial performance provides an overview of the Port's financial activities for the fiscal year ended December 31, 2012. Please read it in conjunction with the Port's financial statements.

The Port of Pend Oreille is a Special Purpose Municipal Government. Ports exist to build infrastructure and promote economic development within their districts. Ports are often, though not always, involved in transportation activities. The Port of Pend Oreille operates a Railroad for shipping and receiving operations.

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Ports do their accounting and financial reporting for their activities very much like a business. The Port of Pend Oreille does not levy nor collect any real or personal property taxes.

The Government Accounting Standards Board has prescribed a new method of financial reporting for all government entities. The Port of Pend Oreille continues to use the model of reporting adopted in 2003.

Issues Facing the Port

There are no material issues facing the Port that could result in material changes in its financial position in the long term.

<u>Financial Highlights</u>

- In 2012, the Port's overall business revenues increased $186,039 or approximately 10% over 2011 business revenue levels.

- The Port's overall operating costs increased in 2012 by $66,769, or approximately 4% over 2011 operating expense levels.

- The Port had an overall Net Operating Income of $172,345 in 2012.

- The Port's operating revenues were more than budgeted by $336,086, and the operating expenses were more than budgeted by $163,741.

Using the Annual Report

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These two reports show the Port's net position and the changes during 2012. The Port's net position is its assets minus its liabilities. This is one measure of financial position of the Port. Over time, increases or decreases in the Port's net position is a good indicator of whether its financial strength is improving or deteriorating. You need to consider other factors not shown on these two financial reports in order to assess the Port's true financial condition. A change in the condition of the Port's asset base is an important factor when assessing the overall financial condition of the Port.

Fund Financial Statements

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Since the Port accounts for all of its transactions in one Proprietary Fund, The Port's fund based financial statement is also its entity-wide governmental financial statement as required by GASB 34-38.

The Port as a Whole

The discussion below explains the Ports overall financial situation for the year ended 12/31/2012.

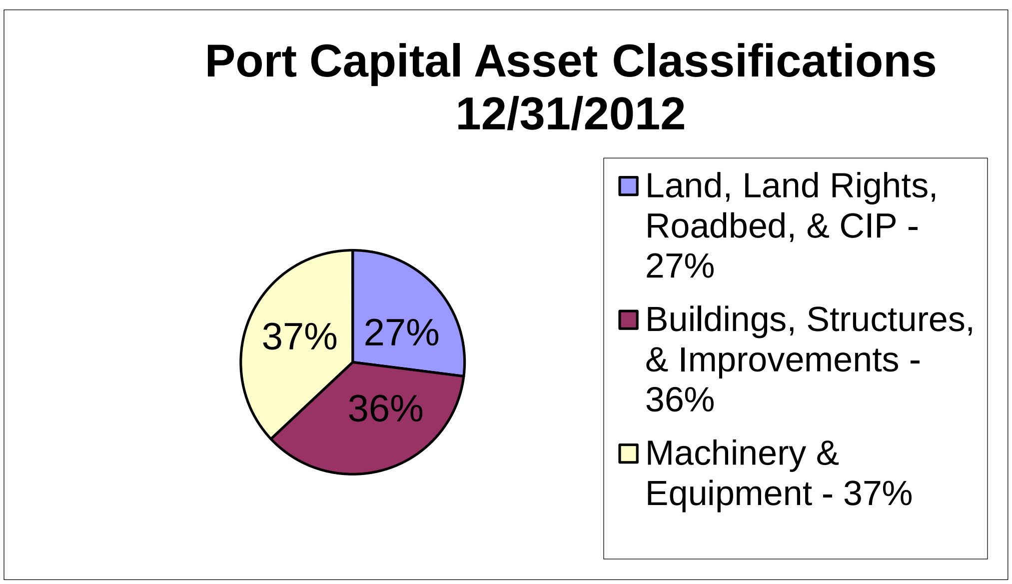
The Port's total assets increased from approximately $6.1 million to $6.2 million since last year. Our analysis below focuses on the change in total assets.

Change in Total Assets (in Millions of Dollars)

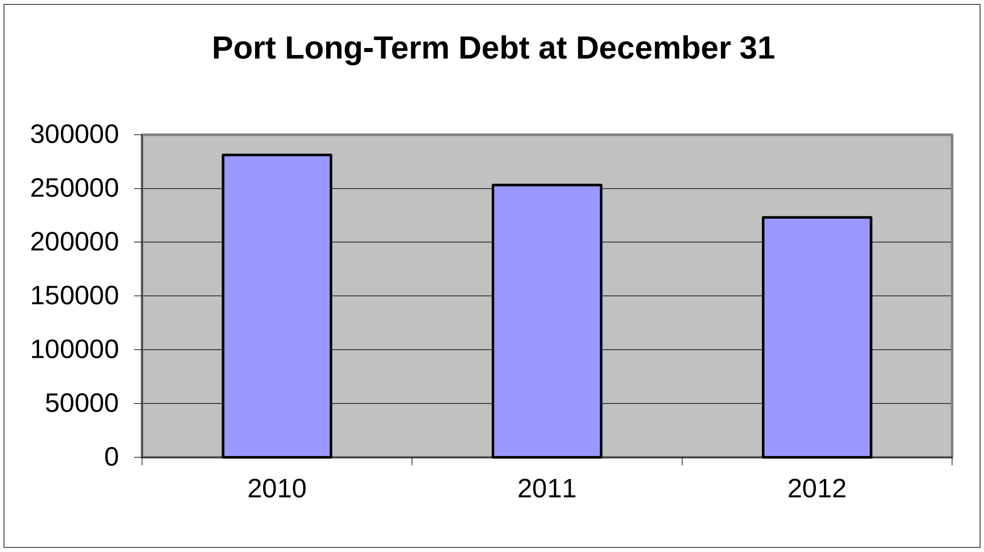
	2011	2012
Total Current Assets	3.6	3.8
Total Restricted Assets	1.0	.9
Total Net Capital Assets	1.5	1.5
Total Assets	6.1	6.2

The total current assets increased due to an increase in short-term residual investments in 2012. The total restricted assets decreased due to a decrease in long term investments.

The Port maintained a capital asset base of $1,500,440 in 2012, and a capital asset base in 2011 of $1,496,181. The book value of the asset base increased due to the shop expansion project starting. The Port expensed $66,955 in depreciation charges in 2012. When the Port invests more than that amount in new capital assets in a year, then the book value of its asset base increases.



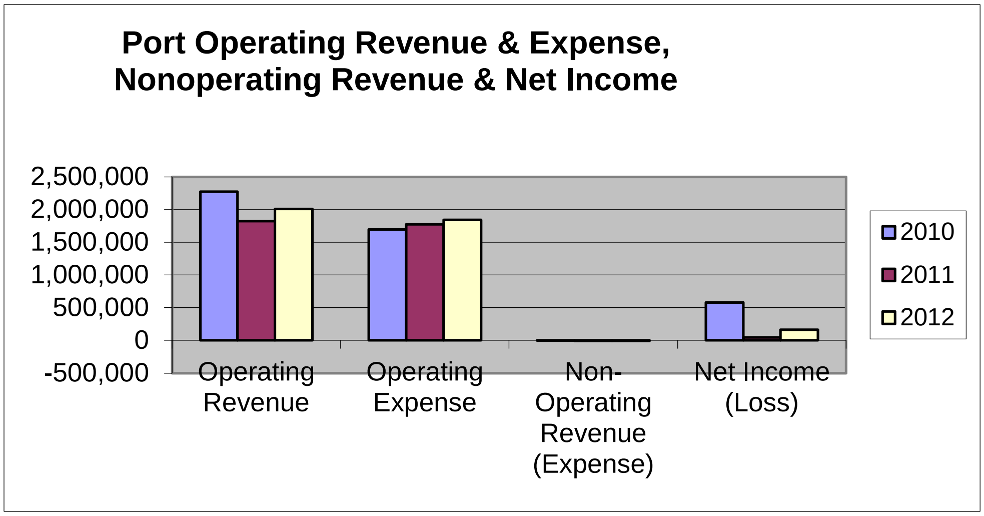
The Port's current liabilities as of 12/31/2012 are debt's that the Port will repay in 2013. The total current liabilities increased in 2012 to $89,002 from $70,603 in 2011 due to an increase in salaries and salaries related expenses. The Port's long term liabilities decreased in 2012 due to the bond debt obligations decreasing each year. The Revenue Bonds outstanding at 12/31/2012 amounted to $223,000, a decrease of $30,000 from $253,000 in 2011.



The Port's Net Investment in Capital Assets, increased by $4,259 from $1,496,181 in 2011 to $1,500,440 in 2012. The Unrestricted Net Position increased by $161,460, from $4,253,215 in 2011 to $4,414,675 in 2012. This increase in assets and decrease in liabilities has resulted consequently in an increase in the Port's overall financial position.

Our further analysis shows our business activities. The Port's total operating revenues increased by approximately $186,039 from $1,825,506 in 2011 to $2,011,545 in 2012, respectively the total cost of operations increased by approximately $66,769 from $1,772,431 in 2011 to $1,839,200 in 2012. Thus, creating a net operating income of $172,345 for 2012 compared to a net operating income of $53,075 for 2011. Operating revenues increased with the increase in freight operations and shop project revenues.

Non operating revenues decreased due to a decrease of interest income. Interest income decreased from $8,449 in 2011 to $6,899 in 2012 due to a decline in interest rates. Non operating expenses show a decrease in interest expense on revenue bonds. Interest expense on revenue bonds decreased from $14,950 in 2011 to $13,525 in 2012.



	2010	2011	2012
Operating Revenue	2,272,690	1,825,506	2,011,545
Operating Expense	1,689,324	1,772,431	1,839,200
Non-Operating Revenue (Expense)	-3,986	-6,346	-6,626
Net Income (Loss)	579,380	46,729	165,719

Overall, the Port's balance of net position at the beginning of the year was $5,749,396 and increased by $165,719 to arrive at the ending balance in net position of $5,915,115 at the end of 2012.

Contacting the Port's Financial Management

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the Port's finances and to show the Port's accountability for the money it receives. If you have questions about this report, or if you need additional financial information, please contact Kelly Driver, Port Manager, or Susan Bluff, Port Financial Officer, at 1981 Black Road, Usk, WA 99180 or by phone at (509) 445-1090.

PORT OF PEND OREILLE STATEMENT OF NET POSITION As of December 31, 2013	
ASSETS	**2013**
Current Assets	
Cash and Cash Equivalents (Note C1)	17,832
Investments (Note C2)	2,805,500
Accounts Receivable	70,118
Prepaid Insurance	52,938
Total Current Assets	2,946,389
Noncurrent Assets	
Restricted Assets:	
Cash and Cash Equivalents (Note C1)	200
Investments (Note C2)	348,360
Total Restricted Assets	348,560
Capital assets not being depreciated:	
Land and Land Rights	446,293
Roadbed	705,281
Construction in Progress - Shop Building	1,770,827
Total Capital assets not being depreciated	2,922,401
Capital assets being depreciated:	
Buildings, Structures, & Improvements	1,610,862
Machinery & Equipment	1,588,077
Less - Accumulated Depreciation	-2,936,609
Total Capital assets being depreciated	262,330
Total Capital Assets (Net)	3,184,731
Total Noncurrent Assets	3,533,290
Total Assets	6,479,679
LIABILITIES	
Current Liabilities	
Accounts Payable	130,631
Accrued Expense	45,319
Current Portion of Long-Term Obligations	30,000
Total Current Liabilities	205,950
Noncurrent Liabilities	
Revenue Bonds (Note 7)	193,000
Total Noncurrent Liabilities	193,000
Total Liabilities	398,950
NET POSITION	
Net investment in capital assets	3,184,731
Unrestricted	2,895,998
TOTAL NET POSITION	6,080,729

The notes to the financial statements are an integral part of this statement.

PORT OF PEND OREILLE STATEMENT OF NET POSITION As of December 31, 2012	
ASSETS	**2012**
Current Assets	
Cash and Cash Equivalents (Note C1)	47,746
Investments (Note C2)	3,608,500
Accounts Receivable	78,629
Prepaid Insurance	51,938
Total Current Assets	3,786,813
Noncurrent Assets	
Restricted Assets:	
Cash and Cash Equivalents (Note C1)	100
Investments (Note C2)	939,764
Total Restricted Assets	939,864
Capital assets not being depreciated:	
Land and Land Rights	446,293
Roadbed	705,281
Construction in Progress - Shop Building	63,460
Total Capital assets not being depreciated	1,215,034
Capital assets being depreciated:	
Buildings, Structures, & Improvements	1,610,862
Machinery & Equipment	1,639,640
Less - Accumulated Depreciation	-2,965,097
Total Capital Assets being depreciated	285,406
Total Capital Assets (Net)	1,500,440
Total Noncurrent Assets	2,440,304
Total Assets	6,227,117
LIABILITIES	
Current Liabilities	
Accrued Expense	59,002
Current Portion of Long-Term Obligations	30,000
Total Current Liabilities	89,002
Noncurrent Liabilities	
Revenue Bonds (Note 7)	223,000
Total Noncurrent Liabilities	223,000
Total Liabilities	312,002
NET POSITION	
Net investment in capital assets	1,500,440
Unrestricted	4,414,675
TOTAL NET POSITION	5,915,115

The notes to the financial statements are an integral part of this statement.

PORT OF PEND OREILLE STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION For the Year Ended December 31, 2013	
	2013
OPERATING REVENUES:	
Railroad Operations	1,201,565
Property Lease/Rental Operations	7,975
Other Railroad Operations	756,835
Total Operating Revenues	1,966,374
OPERATING EXPENSES:	
General Operations	886,718
Maintenance	313,670
General and Administrative	591,187
Depreciation	59,281
Other: Railroad Operations	
Total Operating Expenses	1,850,856
OPERATING INCOME (LOSS)	115,519
NON-OPERATING REVENUES (EXPENSES):	
Grant Revenue	52,999
Interest Income (Net)	6,179
Gain (Loss) on Disposition of Assets	47,501
Interest Expense	-12,150
Election Expense	-4,435
Other Non-Operating Revenues (Expenses)	-39,999
Total Non-Operating Revenues (Expenses)	50,095
Income (loss) before other expense	165,614
Increase (decrease) in Net Position	165,614
Net Position - Beginning of Period	5,915,115
Net Position - End of Period	6,080,729

The notes to the financial statements are an integral part of this statement.

PORT OF PEND OREILLE STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION As of December 31, 2012	
	2012
OPERATING REVENUES:	
Railroad Operations	1,276,829
Property Lease/Rental Operations	3,485
Other Railroad Operations	731,231
Total Operating Revenues	2,011,545
OPERATING EXPENSES:	
General Operations	910,596
Maintenance	256,397
General and Administrative	605,253
Depreciation	66,955
Other: Railroad Operations	
Total Operating Expenses	1,839,200
OPERATING INCOME (LOSS)	172,345
NON-OPERATING REVENUES (EXPENSES):	
Interest Income (Net)	6,899
Gain (Loss) on Disposition of Assets	0
Interest Expense	-13,525
Election Expense	0
Other Non-Operating Revenues (Expenses)	
Total Non-Operating Revenues (Expenses)	-6,626
Income (loss) before other expense	165,719
Increase (decrease) in Net Position	165,719
Net Position - Beginning of Period	5,749,396
Net Position - End of Period	5,915,115

The notes to the financial statements are an integral part of this statement.

PORT OF PEND OREILLE STATEMENT OF CASH FLOWS For The Year Ended December 31, 2013	
	2013
CASH FLOWS FROM OPERATING ACTIVITIES	
Payments Received from Customers	1,974,885
Payments to Suppliers	-904,185
Payments to Employees	-775,877
Net Cash Provided (Used) by Operating Activities	294,823
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES	
Grants Received	39,999
Grants Expended	-39,999
Net Cash Provided (Used) by Noncapital and Financing Activities	0
CASH FLOWS FROM CAPITAL AND REALATED FINANCING ACTIVITIES	
Acquisition and Construction of Capital Assets	-1,743,571
Principle Paid on Revenue Bonds and Loans	-30,000
Interest Paid on Revenue Bonds/Loans	-12,150
Proceeds from Sale of Plant, Property, and Equipment	47,501
Capital Contributed in Aid of Construction	13,000
Net Cash Provided (Used) by Capital and Related Financing Activities	-1,725,220
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of Investment Securities	-674,245
Proceeds From Sales and Maturities of Investments	2,068,650
Interest on Investments (Net)	6,179
Net Cash Provided (Used) by Investing Activities	1,400,584
Net Increase (Decrease) in Cash and Cash Equivalents	-29,814
Cash and Cash Equivalents at the Beginning of the Year	47,846
Cash and Cash Equivalents at the End of the Year	18,032
Reconciliation of Operating Income (Loss) to	
Net Cash Provided (Used) by Operating Activities:	
Operating Income (loss)	115,519
Adjustments to Reconcile Operating Income to Net	
Cash Provided (Used) by Operating Activities:	
Depreciation	59,281
Change in Assets and Liabilities:	
Accounts Receivables, Net	8,510
Prepaid Expenses	-1,000
Accounts Payables	116,948
Election Expense	-4,435
Net Cash Provided by Operating Activities.	294,823

The notes to the financial statements are an integral part of this statement.

PORT OF PEND OREILLE STATEMENT OF CASH FLOWS For The Years Ended December 31, 2012	
	2012
CASH FLOWS FROM OPERATING ACTIVITIES	
Payments Received from Customers	1,994,835
Payments to Suppliers	-973,640
Payments to Employees	-791,010
Net Cash Provided (Used) by Operating Activities	230,185
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES	
Grants Received	**0**
Grants Expended	0
Net Cash Provided (Used) by Noncapital and Financing Activities	0
CASH FLOWS FROM CAPITAL AND REALATED FINANCING ACTIVITIES	
Acquisition and Construction of Capital Assets	-71,214
Principle Paid on Revenue Bonds and Loans	-28,000
Interest Paid on Revenue Bonds/Loans	-13,525
Proceeds from Sale of Plant, Property, and Equipment	0
Capital Contributed in Aid of Construction	0
Net Cash Provided (Used) by Capital and Related Financing Activities	-112,739
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of Investment Securities	-649,156
Proceeds From Sales and Maturities of Investments	523,050
Interest on Investments (Net)	6,899
Net Cash Provided (Used) by Investing Activities	-119,207
Net Increase (Decrease) in Cash and Cash Equivalents	-1,761
Cash and Cash Equivalents at the Beginning of the Year	49,607
Cash and Cash Equivalents at the End of the Year	47,846
Reconciliation of Operating Income (Loss) to	
Net Cash Provided (Used) by Operating Activities:	
Operating Income (loss)	172,345
Adjustments to Reconcile Operating Income to Net	
Cash Provided (Used) by Operating Activities:	
Depreciation	66,955
Change in Assets and Liabilities:	
Accounts Receivables, Net	-16,711
Prepaid Expenses	-8,804
Accounts Payables	16,399
Election Expense	
Net Cash Provided by Operating Activities.	230,185

The notes to the financial statements are an integral part of this statement.

2013 Notes to the Financial Statements

Note 1 – Summary of Significant Accounting Policies

The Port of Pend Oreille was created in 1979 and operates under the laws of the State of Washington applicable to Port Districts. The financial statements of the Port of Pend Oreille have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governments.

A. Reporting Entity

The Port of Pend Oreille is a special purpose government and provides railroad services to the general public and is supported primarily through user charges.

The Port of Pend Oreille is governed by an elected three member board. As required by generally accepted accounting principles, management has considered all potential component units in defining the reporting entity. The Port of Pend Oreille has no component units.

B. Basis of Accounting and Reporting

The accounting records of the Port of Pend Oreille are maintained in accordance with the methods prescribed by the State Auditor under the authority of Chapter 43.09 RCW. The Port of Pend Oreille uses the *Budgeting, Accounting, and Reporting System for Classified Port Districts* in the State of Washington.

The Port continues to use the general provisions of the GASB Statement 34 as implemented in fiscal year 2003. Since the Port accounts for all of its transactions in one Proprietary Fund, the Statement of Revenues, Expenses, and Changes in Net Position is the Port's fund based financial statement.

Funds are accounted for on a cost for services or an economic resources measurement focus. This means that all assets and all liabilities (whether current or non-current) associated with their activity are included on the statement of net position (or balance sheet). Their reported fund position is segregated into net investment in capital assets, restricted and unrestricted components of net position. Operating statements present increases (revenues and gains) and decreases (expenses and losses) in net position. The Port of Pend Oreille discloses changes in cash flows by a separate statement that presents their operating, noncapital financing, capital and related financing and investing activities.

The Port of Pend Oreille uses the full-accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Capital asset purchases are capitalized and long-term liabilities are accounted for in the appropriate fund(s).

The Port of Pend Oreille distinguishes between operating revenues and expenses from non-operating ones. The operating revenues are revenues that are incurred in the daily operations of the Pend Oreille Valley Railroad. Non-operating revenues are revenues incurred through investments and activities not directly related with daily operations.

C. Assets, Liabilities, and Net Position

1. Cash and Cash Equivalents

It is the Port of Pend Oreille's policy to invest all temporary cash surpluses. Total Cash and Cash Equivalents in Current Assets and Restricted Assets as of December 31, 2013 was $18,032. In addition, the District had short-term residual investments totaling $3,153,860. These amounts are classified on the statement of net position as cash and cash equivalents and investments.

The Port of Pend Oreille's deposits are entirely covered by federal depository insurance (FDIC and FSLIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commissioner (PDPC).

2. Short-Term Investments - See Note 2 - *Deposits and Investments*

3. Receivables

Customer accounts receivable consist of amounts owed from private individuals or organizations for goods and services. There is no allowance for doubtful accounts.

4. Inventories

Inventories are expensed when purchased. This is a departure from GAAP.

5. Restricted Assets & Liabilities

In accordance with bond regulations, separate restricted accounts are required to be established. Specific debt service reserve requirements are described in Note 7 – *Long-Term Debt*. On December 31, 2013, the Port had $138,034.21 invested in the Debt Services Account. Other investments included $59,957.76 in Capital Improvements Fund and $150,367.57 in Insurance Reserves at year end December 31, 2013.

6. Capital Assets and Depreciation - See Note 3 - *Capital Assets and Depreciation*

These accounts also include costs incurred for a Shop Building and Paint Booth construction project. The related costs have become part of the cost of the asset.

7. Other Property and Investments – See Note 2 – *Deposits and Investments*

8. Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation (and sick) leave. The Port recognizes vacations only when paid, although this does not conform to GAAP.

Vacation pay may accumulate indefinitely and is payable upon resignation, retirement, or death. Employees may request to "sell back" their vacation. Upon resignation, retirement, or death, any outstanding sick leave is lost. Sick leave may accumulate up to 480 hours.

The unrecorded liability for unpaid vacation benefits at December 31, 2013 was approximately $53,200. Sick leave benefits are not accrued. At December 31, 2013 the unrecorded liability for sick pay was approximately $21,905.

9. Long-Term Debt - See Note 7 - *Long-Term Debt* and Note 8 – *Leases*.

10. Risk Management – See Note 6 – *Risk Management.*

Note 2 – Deposits and Investments

A. Deposits

The Port of Pend Oreille's deposits and certificates of deposit are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Protection Commission (PDPC).

B. Investments

As required by state law, all investments of the Port of Pend Oreille's funds are obligations of the U.S. Government, deposits with Washington State Banks and Savings and Loan Institutions, or other investments allowed by Chapter 39.59 RCW. The temporary investments are stated at $2,805,500 and $348,360 respectively on the Statement of Net Position.

The Port of Pend Oreille's deposits and investments are Category 1 which includes deposits and investments that are either insured, registered or held by the Port or its agents, in the Port's name. All temporary investments are stated at cost.

	Category 1	Market Value
Time Deposits	$3,153,860	$3,153,860

Management intends to hold the time deposits and securities until maturity. Restricted assets shown on the Statement of Net Position include the following investment:

	Market Value
Time Deposits	$348,360

Note 3 – Capital Assets and Depreciation

A. Major expenses for capital assets including major repairs or additions that increase useful lives are capitalized. Maintenance and minor repairs are accounted for as expenses when incurred.

All capital assets are valued at cost. In the case of the sale of a significant operating unit or system, the original cost is removed from the Port's accounts and accumulated depreciation is expensed, the gain or loss is credited or charged to income.

Capital assets are recorded at cost where historical cost is known. Where historical cost is not known, assets are recorded at fair market value. Donations by developers and customers are recorded at contract price or donor cost or appraised value.

The cost accumulated by year end, December 31, 2013, for the construction of the new shop building addition and paint booth was $1,770,827. This amount is shown as Construction in Progress on the Statement of Net Position. This construction project will be finished in 2014. This capitalized amount will be depreciated over the useful life of 40 years as determined by management.

Depreciation expense is charged to operations to allocate the cost of capital assets over their estimated useful lives using the straight-line method.

B. Depreciation Expense on assets in the year 2013 totaled $59,280.50.

Current Asset	Useful Life	Depreciation in 2013
Rehabilitation	30 + Years	$29,395.20
Buildings	10 + Years	$9,407.88
Hyrails & Autos	5 Years	$10,790.04
Office, Shop, & Maintenance Equip.	1-20 Years	$9,687.38

Due to the nature of the railroad industry and the high costs associated with repair parts for specialized equipment, a set dollar figure cannot be set in determining when to expense or capitalize a purchase. Port staff looks at each purchase separately in making this determination.

C. Capital assets activity for the year ended December 31, 2013 was as follows:

	Beginning Balance 1/1/13	Increases	Decreases	Ending Balance 12/31/13
Capital assets, not being depreciated:				
Land	$351,723.54	$0.00	$0.00	$351,723.54
Land - Industrial	$94,569.00	$0.00	$0.00	$94,569.00
Roadbed	$705,281.46	$0.00	$0.00	$705,281.46
Construction in Progress – Shop Building	$63,460.30	$1,707,366.72	$0.00	$1,770,827.02
Total capital assets, not being depreciated	$1,215,034.30	$1,707,366.72	$0.00	$2,922,401.02
Capital assets, being depreciated:				
Buildings	$542,485.47	$0.00	$0.00	$542,485.47
Machinery and equipment	$1,639,640.43	$36,204.49	$87,768.40	$1,588,076.52
Rehabilitation	$1,068,376.17	$0.00	$0.00	$1,068,376.17
Total Capital assets being depreciated	$3,250,502.07	$36,204.49	$87,768.40	$3,198,938.16
Less Accumulated depreciation for:				
Buildings	$443,823.51	$9,407.88	$0.00	$453,231.39
Machinery and equipment	$1,494,434.10	$20,477.42	$87,768.40	$1,427,143.12
Rehabilitation	$1,026,838.94	$29,395.20	$0.00	$1,056,234.14
Total accumulated depreciation	$2,965,096.55	$59,280.50	$87,768.40	$2,936,608.65
Total Capital assets, being depreciated, net	$285,405.52	($23,076.01)	$0.00	$262,329.51

Note 4 – Construction Commitments

The construction of the shop building addition and paint booth project is nearly completed as of December 31, 2013. The contract with ALSC Architects for professional services which included the Design Development, Construction Documents, Bid & Negotiation, and Construction Administration of the shop building addition and paint booth in the amount of $139,856.24, (the original contract price of $147,600 less a change order credit of $7,743.76) is complete as of December 31, 2013.

POVA had entered into a contract with James W. Elmer Construction Company for the actual construction of the shop building and paint booth in 2013 in the amount of $1,590,054.71 after change orders plus tax. At year end of December 31, 2013 the project was 98% complete with a balance to finish of $39,137.52 plus sales tax. There is also a recorded cumulative retainage of $77,545.86 which will be due in 2014 upon finalization of the project.

At year-end the Port's commitment with this contractor is as follows:

PROJECT	SPENT TO DATE	REMAINING COMMITMENT
Shop Building Addition	$1,591,241.03	$ 39,137.52
And Paint Booth		$ 2,974.45 Sales Tax
		$ 77,545.86 Retainage Due
		$119,657.83

Note 5 – Pension Plan

All employees of the Port are covered by one of the following systems:

a. Non-railroad employees of the Port are covered only by Social Security;
b. All railroad employees of the Port are covered under the Railroad Retirement Act.

Railroad Retirement Act
The Railroad Retirement Act is a federal law that provides retirement and disability annuities for qualified railroad employees, spouse annuities, and survivors' benefits for the families of the deceased employees who were injured under the act. The Railroad Retirement Act is supported by taxes levied against the employees and the employer. Tax amounts payable by railroad employers are calculated by applying appropriate tax rates to the total monthly taxable payroll earned by the entire railroad employees.
In addition to the regular railroad retirement taxes, employers must also pay: (1) A tax rate determined quarterly by the Railroad Retirement Board (RRB) on each hour of compensated service performed by the employees, to finance the railroad retirement supplemental annuity program; (2) A tax rate of 5.91% percent for 2013, determined by the balance in the railroad unemployment insurance account, on the first $1,405 of employee's monthly earnings to support the railroad unemployment program. The Port's contribution under the Railroad Retirement Act represents its full liability under the system.

Contribution rates for 2013 are as follows:

	Employee	Employer
Medicare	1.45%	1.45%
Tier I	6.20%	6.20%
Tier II	4.40%	12.60%

Note 6 – Risk Management

The Port has an insurance deductible for general liability, bill of lading/property losses, bodily injury, personal injury and Federal Employer Liability Act (FELA) coverage up to $25,000 per incident with an annual aggregate of $25,000. The Port has a deductible for foreign rolling stock losses up to $5,000 per occurrence. In addition, the Port has a deductible under its Error and Omissions Policy for up to $10,000 per occurrence. General liability insurance reserves at December 31, 2013 were $150,367.57.

The Port has an insurance policy to cover any litigation with a $10,000 to $25,000 deductible. In the opinion of management, the Port's insurance policy and $10,000 to $25,000 deductible retained by the Port are adequate to pay all known or pending claims.

The reporting requirement for risk management, schedule 21, is not applicable to the Port because the Port's only risk financed or assumed is an annual deductible of a purchased insurance policy.

Risk Pool: The Port of Pend Oreille is a member of Enduris. Chapter 48.62 RCW provides the exclusive source of local government entity authority to individually or jointly self-insure risks, jointly purchase insurance or reinsurance, and to contract for risk management, claims, and administrative services. Enduris was formed July 10, 1987 pursuant to the provisions of Chapter 48.62 RCW, Chapter 200-100 WAC, and Chapter 39-34 RCW. Two (2) counties and two (2) cities in the State of Washington joined together by signing an Interlocal Governmental Agreement to fund their self-insured losses and jointly purchase insurance and administrative services. As of August 31, 2013, there are 486 Enduris members representing a broad array of special purpose districts throughout the state.

Enduris members share in the self-insured retention, jointly purchase excess and/or reinsurance coverage and provide risk management services and other related administrative services. Enduris provides "per occurrence" based policies for all lines of liability coverage including Public Official's Liability. The Property coverage is written on an "all risk", blanket basis using current Statement of Values. The Property coverage includes but is not limited to mobile equipment, electronic data processing equipment, and business interruption, course of construction and additions, property in transit, fine arts, and automobile physical damage to insured vehicles. Boiler and machinery coverage is included on a blanket limit of $100 million for all members. Enduris offers employee dishonesty coverage up to a liability limit of $1,000,000.

Members make an annual contribution to fund Enduris. Enduris acquires reinsurance from unrelated insurance companies on a "per occurrence" basis.

$1,000,000 deductible on liability loss – the member is responsible for the first $1,000 of the deductible amount of each claim, while Enduris is responsible for the remaining $999,000 on liability loss; $250,000 deductible on property loss – the member is responsible for the first $1,000 of the deductible amount of each claim, while Enduris is responsible for the remaining $249,000 on property loss. Enduris is responsible for the $4,000 deductible on boiler and machinery loss.

Insurance carriers cover all losses over the deductibles as shown to the policy maximum limits. Since Enduris is a cooperative program, there is a joint liability among the participating members.

The contract requires members to continue membership for a period of not less than one (1) year and must give notice 60 days before terminating participation. The Master Agreement (Intergovernmental Contract) is automatically renewed after the initial one (1) full fiscal year commitment. Even after termination, a member is still responsible for contribution to Enduris for any unresolved, unreported and in-process claims for the period they were a signatory to the Master Agreement.

Enduris is fully funded by its member participants. Claims are filed by members with Enduris and are administered in house.

A Board of Directors consisting of seven (7) board members governs Enduris. Its members elect the Board and the positions are filled on a rotating basis. The Board meets quarterly and is responsible for conducting the business affairs of Enduris.

Note 7 – Long-Term Debt

The Port of Pend Oreille entered into revenue bonds debt to purchase the railroad and complete rehabilitation construction work. The revenue bonds currently outstanding are as follows:

Purpose	Interest Rate	Outstanding
1979 Series A	5%	$ 54,000
1979 Series B	5%	$114,000
1981 Series A	5%	$ 16,000
1981 Series B	5%	$ 39,000
Total		$223,000

This annual requirement to redeem all debts outstanding as of December 31, 2013, including interest, is as follows:

Years Ending December 31	Principal	Interest	Total
2014	$ 30,000.00	$ 11,150.00	$ 41,150.00
2015	$ 32,000.00	$ 9,650.00	$ 41,650.00
2016	$ 34,000.00	$ 8,050.00	$ 42,050.00
2017	$ 35,000.00	$ 6,350.00	$ 41,350.00
2018	$ 37,000.00	$ 4,600.00	$ 41,600.00
2019-2021	$ 55,000.00	$ 3,950.00	$ 58,950.00
Totals	$223,000.00	$ 43,750.00	$266,750.00

The maturity date of the bonds is April 1, 2021. However, the bond covenant provides for earlier retirement by purchase or redemption at any time. No partial payment shall extend or postpone the due date of any subsequent installments and are to be made in multiples of $1,000. In addition, the covenant requires the Port to maintain a reserve account into which shall be deposited sufficient sums each year so that within a period of 10 years from the date of the bonds, said reserves shall be sufficient to pay one year's debt service requirement on the bonds. The Port currently has $138,034.21 to meet this current reserve requirement.

Port of Pend Oreille covenants with the holder of each of the Port bonds that among other things, the Port will maintain reserves sufficient to cover all operation and maintenance expenses and an amount equal to or exceeding 1.3 times the average annual principal and interest payments on the outstanding bonds, if more issues are to be authorized. There are a number of other limitations and restrictions contained in the various bond indentures.

Note 8 – Leases

The Port leases the Sandpoint rail line under a non-cancelable 20 year operating lease. The lease payments were $6,670.00 monthly through March 31, 2001. Commencing as of April 1, 2001, the monthly charge was to be adjusted annually according to the Rail Cost Adjustment Factor. The Rail Cost Adjustment Factor is based on 50% of the increase or decrease between the first quarter of that year compared to the first quarter of the prior year. This contractual adjustment increase was not implemented until May 2008. The Port was charged for the past three years contract difference in 2008, and then preceded monthly with the correct amount based on the Rail Cost Adjustment Factor. The current monthly rate at November 30, 2008 was $7,899.37.

Another change was put into effect as of December 1, 2008 due to economic factors. The change allowed for a reduction in the lease payments to $5,000.00 monthly from December 1, 2008 to December 31, 2012. Due to economic factors the monthly lease payment of $5,000.00 will remain unchanged through March 31, 2014.

The total cost of the lease was $60,000 ($5,000.00 x 12 months) for the period ended December 31, 2013.

The future lease payments are as follows:

Year ending December 31	Amount	
March 31, 2014	$ 15,000	
Apr. – Dec. 31, 2014	$ 60,030	+/- Rail Cost Adjustment
2015	$ 80,040	+/- Rail Cost Adjustment
2016	$ 80,040	+/- Rail Cost Adjustment
2017	$ 80,040	+/- Rail Cost Adjustment
2018	$ 80,040	+/- Rail Cost Adjustment
Total	$ 395,190	+/- Rail Cost Adjustment

Note 9 – Restricted Component of Net Position

The Port does not have any restricted components of net position.

Note 10 – Contingencies and Litigation

The Port’s financial statements include all material liabilities. There was one OSHA claim in 2013 that was taken to mediation and the Port was responsible for $57,345 of the settlement. In the opinion of management, the Port’s Insurance Policies are adequate to pay all known litigation or pending claims.

2012 Notes to the Financial Statements

Note 1 – Summary of Significant Accounting Policies

The Port of Pend Oreille was created in 1979 and operates under the laws of the State of Washington applicable to Port Districts. The financial statements of the Port of Pend Oreille have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governments.

A. Reporting Entity

The Port of Pend Oreille is a special purpose government and provides railroad services to the general public and is supported primarily through user charges.

The Port of Pend Oreille is governed by an elected three member board. As required by generally accepted accounting principles, management has considered all potential component units in defining the reporting entity. The Port of Pend Oreille has no component units.

B. Basis of Accounting and Reporting

The accounting records of the Port of Pend Oreille are maintained in accordance with the methods prescribed by the State Auditor under the authority of Chapter 43.09 RCW. The Port of Pend Oreille uses the *Budgeting, Accounting, and Reporting System for Classified Port Districts* in the State of Washington.

The Port continues to use the general provisions of the GASB Statement 34 as implemented in fiscal year 2003. Since the Port accounts for all of its transactions in one Proprietary Fund, the Statement of Revenues, Expenses, and Changes in Net Position is the Port's fund based financial statement.

Funds are accounted for on a cost for services or an economic resources measurement focus. This means that all assets and all liabilities (whether current or non-current) associated with their activity are included on the statement of net position (or balance sheet). Their reported fund position is segregated into net investment in capital assets, restricted and unrestricted components of net position. Operating statements present increases (revenues and gains) and decreases (expenses and losses) in net position. The Port of Pend Oreille discloses changes in cash flows by a separate statement that presents their operating, noncapital financing, capital and related financing and investing activities.

The Port of Pend Oreille uses the full-accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Capital asset purchases are capitalized and long-term liabilities are accounted for in the appropriate fund(s). Unbilled revenues are recorded at year-end.

The operating revenues are revenues that are incurred in the daily operations of the Pend Oreille Valley Railroad. Non-operating revenues are revenues incurred through investments and activities not directly related with daily operations.

The Port's financial statements include the financial position and results of the operations of all enterprise operations which the Port manages.

C. Assets, Liabilities, and Net Position

1. <u>Cash and Cash Equivalents</u>
It is the Port of Pend Oreille's policy to invest all temporary cash surpluses. Total Cash and Cash Equivalents in Current Assets and Restricted Assets as of December 31, 2012 was $47,846. In addition, the District had short-term residual investments totaling $4,548,264. These amounts are classified on the statement of net position as cash and cash equivalents and investments.

The Port of Pend Oreille's deposits are entirely covered by federal depository insurance (FDIC and FSLIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commissioner (PDPC).

2. <u>Short-Term Investments</u> - See Note 2 - *Deposits and Investments*

3. <u>Receivables</u>
Customer accounts receivable consist of amounts owed from private individuals or organizations for goods and services. There is no allowance for doubtful accounts.

4. <u>Inventories</u>
Inventories are expensed when purchased. This is a departure from GAAP.

5. <u>Restricted Assets & Liabilities</u>
In accordance with bond regulations, separate restricted accounts are required to be established. Specific debt service reserve requirements are described in Note 7 – *Long-Term Debt*. On December 31, 2012, the Port had $180,439.80 invested in the Debt Services Account. Other investments included $609,169.82 in Capital Improvements Fund and $150,154.71 in Insurance Reserves at year end December 31, 2012.

6. <u>Capital Assets and Depreciation</u> - See Note 3 - *Capital Assets and Depreciation*
These accounts also include preliminary costs incurred for a proposed construction project. The related costs have become part of the cost of the asset; if the project is abandoned, related costs will be charged back to expense.

7. <u>Other Property and Investments</u> – See Note 2 – *Deposits and Investments*

8. Compensated Absences
Compensated absences are absences for which employees will be paid, such as vacation (and sick) leave. The Port recognizes vacations only when paid, although this does not conform to GAAP.

Vacation pay may accumulate indefinitely and is payable upon resignation, retirement, or death. Employees may request to "sell back" their vacation. Upon resignation, retirement, or death, any outstanding sick leave is lost. Sick leave may accumulate up to 480 hours.

The unrecorded liability for unpaid vacation benefits at December 31, 2012 was approximately $46,331. Sick leave benefits are not accrued. At December 31, 2012 the unrecorded liability for sick pay was approximately $18,427.

9. Long-Term Debt - See Note 7 - *Long-Term Debt* and Note 8 – *Leases*.

10. Risk Management - See Note 6 - *Risk Management*

Note 2 – Deposits and Investments

A. Deposits

The Port of Pend Oreille's deposits and certificates of deposit are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Protection Commission (PDPC).

B. Investments

As required by state law, all investments of the Port of Pend Oreille's funds are obligations of the U.S. Government, deposits with Washington State Banks and Savings and Loan Institutions, or other investments allowed by Chapter 39.59 RCW. The temporary investments are stated at $3,608,500 and $939,764 respectively on the Statement of Net Position.

The Port of Pend Oreille's deposits and investments are Category 1 which includes deposits and investments that are either insured, registered or held by the Port or its agents, in the Port's name. All temporary investments are stated at cost.

	Category 1	Market Value
Time Deposits	$4,548,264	$4,548,264

Management intends to hold the time deposits and securities until maturity. Restricted assets shown on the Statement of Net Position include the following investment:

	Market Value
Time Deposits	$939,764

Note 3 – Capital Assets and Depreciation

A. Major expenses for capital assets including major repairs or additions that increase useful lives are capitalized. Maintenance and minor repairs are accounted for as expenses when incurred.

All capital assets are valued at cost. In the case of the sale of a significant operating unit or system, the original cost is removed from the Port's accounts and accumulated depreciation is expensed, the gain or loss is credited or charged to income.

Capital assets are recorded at cost where historical cost is known. Where historical cost is not known, assets are recorded at fair market value. Donations by developers and customers are recorded at contract price or donor cost or appraised value.

The preliminary costs incurred by year end, December 31, 2012, for a proposed construction project to build on an addition to our shop building were $63,460.30. This amount is shown as Construction in Progress. This proposed construction project is proposed to be completed in 2013.

Depreciation expense is charged to operations to allocate the cost of capital assets over their estimated useful lives, using the straight-line method.

B. Depreciation Expense on assets in the year 2012 totaled $66,955.33.

Current Asset	Useful Life	Depreciation in 2012
Rehabilitation	30 + Years	$29,395.20
Buildings	10 + Years	$11,586.15
Hyrails & Autos	5 Years	$18,842.14
Office, Shop, & Maintenance Equip.	1-20 Years	$7,131.84

Due to the nature of the railroad industry and the high costs associated with repair parts for specialized equipment, a set dollar figure cannot be set in determining when to expense or capitalize a purchase. Port staff looks at each purchase separately in making this determination.

C. Capital assets activity for the year ended December 31, 2012 was as follows:

	Beginning Balance 1/1/12	Increases	Decreases	Ending Balance 12/31/12
Capital assets, not being depreciated:				
Land	$351,723.54	$0.00	$0.00	$351,723.54
Land - Industrial	$94,569.00	$0.00	$0.00	$94,569.00
Roadbed	$705,281.46	$0.00	$0.00	$705,281.46
Construction in Progress – Shop Building	$0.00	$63,460.30	$0.00	$63,460.30
Total capital assets, not being depreciated	$1,151,574.00	$63,460.30	$0.00	$1,215,034.30
Capital assets, being depreciated:				
Buildings	$542,485.47	$0.00	$0.00	$542,485.47
Machinery and equipment	$1,644,495.44	$7,753.90	$12,608.91	$1,639,640.43
Rehabilitation	$1,068,376.17	$0.00	$0.00	$1,068,376.17
Total Capital assets being depreciated	$3,255,357.08	$7,753.90	$12,608.91	$3,250,502.07
Less Accumulated depreciation for:				
Buildings	$432,237.36	$11,586.15	$0.00	$443,823.51
Machinery and equipment	$1,481,069.03	$25,973.98	$12,608.91	$1,494,434.10
Rehabilitation	$997,443.74	$29,395.20	$0.00	$1,026,838.94
Total accumulated depreciation	$2,910,750.13	$66,955.33	$12,608.91	$2,965,096.55
Total Capital assets, being depreciated, net	$344,606.95	($59,201.43)	$0.00	$285,405.52

Note 4 – Construction Commitments

The Port has an active proposed construction project as of December 31, 2012. The project includes building on an addition to the Port's shop building. The Port has contracted with ALSC Architects for professional services that include the Design Development, Construction Documents, Bid & Negotiation, and Construction Administration of the proposed shop building addition in the amount of $147,600.

At year-end the Port's commitment with ALSC Architects in regards to the proposed addition to the shop building is as follows:

	Percent Complete	Spent to date	Remaining Commitment
Design Development	100%	$44,280.00	$0.00
Construction Documents	25%	$14,760.00	$44,280.00
Bid & Negotiation	0%	$0.00	$7,380.00
Construction Administration	0%	$0.00	$36,900.00
Totals		$59,040.00	$88,560.00

Note 5 – Pension Plan

All employees of the Port are covered by one of the following systems:
a. Non-railroad employees of the Port are covered only by Social Security;
b. All railroad employees of the Port are covered under the Railroad Retirement Act.

<u>Railroad Retirement Act</u>
The Railroad Retirement Act is a federal law that provides retirement and disability annuities for qualified railroad employees, spouse annuities, and survivors' benefits for the families of the deceased employees who were injured under the act. The Railroad Retirement Act is supported by taxes levied against the employees and the employer. Tax amounts payable by railroad employers are calculated by applying appropriate tax rates to the total monthly taxable payroll earned by the entire railroad employees.

In addition to the regular railroad retirement taxes, employers must also pay: (1) A tax rate determined quarterly by the Railroad Retirement Board (RRB) on each hour of compensated service performed by the employees, to finance the railroad retirement supplemental annuity program; (2) A tax rate of 12 percent for 2012, determined by the balance in the railroad unemployment insurance account, on the first $1,365 of employee's monthly earnings to support the railroad unemployment program. The Port's contribution under the Railroad Retirement Act represents its full liability under the system.

Contribution rates for 2012 are as follows:

	Employee	Employer
Medicare	1.45%	1.45%
Tier I	4.20%	6.20%
Tier II	3.90%	12.10%

Note 6 – Risk Management

The Port has an insurance deductible for general liability, bill of lading/property losses, bodily injury, personal injury and Federal Employer Liability Act (FELA) coverage up to $25,000 per incident with an annual aggregate of $25,000. The Port has a deductible for foreign rolling stock losses up to $5,000 per occurrence. In addition, the Port has a deductible under its Error and Omissions Policy for up to $10,000 per occurrence. General liability insurance reserves at December 31, 2012 were $150,154.71.

The Port has an insurance policy to cover any litigation with a $10,000 to $25,000 deductible. In the opinion of management, the Port's insurance policy and $10,000 to $25,000 deductible retained by the Port are adequate to pay all known or pending claims.

The reporting requirement for risk management, schedule 21, is not applicable to the Port because the Port's only risk financed or assumed is an annual deductible of a purchased insurance policy.

Risk Pool: The Port of Pend Oreille is a member of Enduris. Chapter 48.62 RCW authorizes the governing body of any one or more governmental entity to form together into or join a pool or organization for the joint purchasing of insurance, and/or joint self-insuring, and/or joint hiring or contracting for risk management services to the same extent that they may individually purchase insurance, self-insure, or hire or contract for risk management services. An agreement to form a pooling arrangement was made pursuant to the provisions of Chapter 39.34 RCW, the Interlocal Cooperation Act. Enduris was formed July 10, 1987, when two (2) counties and two (2) cities in the State of Washington joined together by signing an Interlocal Governmental Agreement to pool their self-insured losses and jointly purchase insurance and administrative services. As of August 31, 2011, there are 468 Enduris members representing a broad range of special purpose districts.

Enduris allows members to jointly purchase excess insurance coverage, share in the self-insured retention, establish a plan for total self-insurance, and provide excellent risk management services and other related services. Enduris provides "occurrence" policies for all lines of liability coverage including Public Official's Liability. The Property coverage is written on an "all risk" basis blanket form using current Statement of Values. The Property coverage includes mobile equipment, electronic data processing equipment, valuable papers, building ordinance coverage, property in transit, extra expense, consequential loss, accounts receivable, fine arts, inventory or appraisal cost, automobile physical damage to insured vehicles. Boiler and machinery coverage is included on a blanket limit of $100 million for all members. Enduris offers employee dishonesty coverage up to a liability limit of $1,000,000.

Members make an annual contribution to fund Enduris. Enduris acquires insurance from unrelated insurance companies that is subject to a "per occurrence".

$1,000,000 deductible on liability loss – the member is responsible for the first $1,000 of the deductible amount of each claim, while Enduris is responsible for the remaining $999,000 on liability loss; $250,000 deductible on property loss – the member is responsible for the first $1,000 of the deductible amount of each claim, while Enduris is responsible for the remaining $249,000 on property loss. Enduris is responsible for the $4,000 deductible on boiler and machinery loss.

Insurance carriers cover all losses over the deductibles as shown to the policy maximum limits. Since Enduris is a cooperative program, there is a joint liability among the participating members.

The contract requires members to continue membership for a period of not less than one (1) year and must give notice 60 days before terminating participation. The Master Agreement (Intergovernmental Contract) is automatically renewed after the initial one (1) full fiscal year commitment. Even after termination, a member is still responsible for contribution to Enduris for any unresolved, unreported and in-process claims for the period they were a signatory to the Master Agreement.

Enduris is fully funded by its member participants. Claims are filed by members with Enduris and are administered in house.

A Board of Directors consisting of seven (7) board members governs Enduris. Its members elect the Board and the positions are filled on a rotating basis. The Board meets quarterly and is responsible for conducting the business affairs of Enduris.

Note 7 – Long-Term Debt

The Port of Pend Oreille entered into revenue bonds debt to purchase the railroad and complete rehabilitation construction work. The revenue bonds currently outstanding are as follows:

Purpose	Interest Rate	Outstanding
1979 Series A	5%	$ 62,000
1979 Series B	5%	$130,000
1981 Series A	5%	$ 18,000
1981 Series B	5%	$ 43,000
Total		$253,000

This annual requirement to redeem all debts outstanding as of December 31, 2012, including interest, is as follows:

Years Ending December 31	Principal	Interest	Total
2013	$ 30,000.00	$ 12,650.00	$ 42,650.00
2014	$ 30,000.00	$ 11,150.00	$ 41,150.00
2015	$ 32,000.00	$ 9,650.00	$ 41,650.00
2016	$ 34,000.00	$ 8,050.00	$ 42,050.00
2017	$ 35,000.00	$ 6,350.00	$ 41,350.00
2018-2021	$ 92,000.00	$ 8,550.00	$100,550.00
Totals	$253,000.00	$ 56,400.00	$309,400.00

The maturity date of the bonds is April 1, 2021. However, the bond covenant provides for earlier retirement by purchase or redemption at any time. No partial payment shall extend or postpone the due date of any subsequent installments and are to be made in multiples of $1,000. In addition, the covenant requires the Port to maintain a reserve account into which shall be deposited sufficient sums each year so that within a period of 10 years from the date of the bonds, said reserves shall be sufficient to pay one year's debt service requirement on the bonds. The Port currently has $180,439.80 to meet the current reserve requirement.

Port of Pend Oreille covenants with the holder of each of the Port bonds that among other things, the Port will maintain reserves sufficient to cover all operation and maintenance expenses and an amount equal to or exceeding 1.3 times the average annual principal and interest payments on the outstanding bonds, if more issues are to be authorized. There are a number of other limitations and restrictions contained in the various bond indentures.

Note 8 – Leases

The Port leases the Sandpoint rail line under a non-cancelable 20 year operating lease. The lease payments were $6,670.00 monthly through March 31, 2001. Commencing as of April 1, 2001, the monthly charge was to be adjusted annually according to the Rail Cost Adjustment Factor. The Rail Cost Adjustment Factor is based on 50% of the increase or decrease between the first quarter of that year compared to the first quarter of the prior year. This contractual adjustment increase was not implemented until May 2008. The Port was charged for the past three years contract difference in 2008, and then preceded monthly with the correct amount based on the Rail Cost Adjustment Factor. The current monthly rate at November 30, 2008 was $7,899.37.

Another change was put into effect as of December 1, 2008 due to economic factors. The change allowed for a reduction in the lease payments to $5,000.00 monthly from December 1, 2008 to December 31, 2012. Due to economic factors the monthly lease payment of $5,000.00 will remain unchanged through December 31, 2013.

The total cost of the lease was $60,000 ($5,000.00 x 12 months) for the period ended December 31, 2012.

The future lease payments are as follows:

Year ending December 31	Amount	
2013	$ 60,000	
2014	$ 80,040	+/- Rail Cost Adjustment
2015	$ 80,040	+/- Rail Cost Adjustment
2016	$ 80,040	+/- Rail Cost Adjustment
2017	$ 80,040	+/- Rail Cost Adjustment
2018	$ 80,040	+/- Rail Cost Adjustment
Total	$ 460,200	+/- Rail Cost Adjustment

Note 9 – Restricted Component of Net Position

The Port does not have any restricted components of net position.

Note 10 – Contingencies and Litigation

The Port's financial statements include all material liabilities. There are no material contingent liabilities to record. In the opinion of management, the Port's Insurance Policies are adequate to pay all known litigation or pending claims.

Note 11 – Termination Benefits

The Port paid out a one-time lump sum payment severance package upon the involuntary termination of one employee in the amount of $12,750.

ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

In fulfilling our mission to hold state and local governments accountable for the use of public resources, we also hold ourselves accountable by continually improving our audit quality and operational efficiency and developing highly engaged and committed employees.

As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments as well as fraud, state whistleblower and citizen hotline investigations.

The results of our work are widely distributed through a variety of reports, which are available on our website and through our free, electronic subscription service.

We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

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