Washington State Auditor's Office

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Financial Statements Audit Report

Public Utility District No. 2 of Pacific County

For the period January 1, 2014 through December 31, 2015

Published September 22, 2016

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Washington State Auditor's Office

September 22, 2016

Board of Commissioners
Public Utility District No. 2 of Pacific County
Raymond, Washington

Report on Financial Statements

Please find attached our report on Public Utility District No. 2 of Pacific County's financial statements.

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

Sincerely,

Troy X. Kelley

TROY KELLEY

STATE AUDITOR

OLYMPIA, WA

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Public Utility District No. 2 of Pacific County
January 1, 2014 through December 31, 2015

Board of Commissioners
Public Utility District No. 2 of Pacific County
Raymond, 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 Public Utility District No. 2 of Pacific County, Washington, as of and for the years ended December 31, 2015 and 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated August 10, 2016. As discussed in Note 1 to the financial statements, during the year ended December 31, 2014, the District implemented Governmental Accounting Standards Board Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audits of the financial statements, we considered the District'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 District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District'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 District'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 District in a separate letter dated August 10, 2016.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of the District'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 District'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 District'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

OLYMPIA, WA

August 10, 2016

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

Public Utility District No. 2 of Pacific County
January 1, 2014 through December 31, 2015

Board of Commissioners
Public Utility District No. 2 of Pacific County
Raymond, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of Public Utility District No. 2 of Pacific County, Washington, as of and for the years ended December 31, 2015 and 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed on page 9.

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 District'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 District'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 Public Utility District No. 2 of Pacific County, as of December 31, 2015 and 2014, 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.

Matters of Emphasis

As discussed in Note 1 to the financial statements, in 2014, the District adopted new accounting guidance, Governmental Accounting Standards Board *Statement No. 68, Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*. Our opinion is not modified with respect to this matter.

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 10 through 14, information on postemployment benefits other than pensions on page 52 and pension plan information on pages 53 through 54 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 August 10, 2016 on our consideration of the District'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 District's internal control over financial reporting and compliance.

TROY KELLEY

STATE AUDITOR

OLYMPIA, WA

August 10, 2016

FINANCIAL SECTION

Public Utility District No. 2 of Pacific County
January 1, 2014 through December 31, 2015

REQUIRED SUPPLEMENTARY INFORMATION

BASIC FINANCIAL STATEMENTS

REQUIRED SUPPLEMENTARY INFORMATION

PUBLIC UTILITY DISTRICT NO. 2 of PACIFIC COUNTY
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Year Ending December 31, 2015

The following discussion and analysis of the financial results of Public Utility District No. 2 of Pacific County (District) provides an overview of the District's financial activities for the years ended December 31, 2015 and 2014, with additional comparative data for 2013. This discussion is designed to be used in conjunction with the financial statements and notes, which follow this section.

Overview of the Financial Statements

The District is a municipal corporation with financial activities in the areas of electric and water. The operations of the District include the aforementioned electric system and three water systems. In addition, leases excess capacity on its fiber optic system.

In accordance with requirements set forth by the Governmental Accounting Standards Board, the District's financial statements employ the accrual basis of accounting in recognizing increases and decreases in economic resources. Accrual accounting recognizes all revenues when earned and expenses when incurred during the year, regardless of when cash is received or paid.

The basic financial statements, presented on a comparative format, are comprised of:

Comparative Statement of Net Position
The Statement of Net Position presents information on the District's assets and liabilities, with the difference between the two reported as net position. The net position section of the Statement is separated into three categories: net investment in capital assets; restricted net position; and unrestricted net position.

Comparative Statement of Revenues, Expenses, and Changes in Net Position
This comparative statement reflects the transactions and events that have increased or decreased the District's total economic resources during the period. Revenues are presented net of allowances and are summarized by major source. Revenues and expenses are classified as operating or non-operating based on the nature of the transaction.

Comparative Statement of Cash Flows
The Comparative Statement of Cash Flows reflects the sources and uses of cash separated into three categories of activities: operating, capital and related financing, and investing. The District does not include cash equivalents within its definition of cash.

The notes to the financial statements presented at the end of the basic financial statements are considered an integral part of the District's presentation of financial position, results of operations, and changes in cash flows.

Statement of Net Position (in thousands)	**2015**	**2014 As Restated**	**Change**	**% Change**	**2013**
Current and Other Assets	$28,257	$30,476	$(2,219)	-7.3%	$16,090
Net Capital Assets	50,074	48,913	1,161	2.4%	48,718
Other Noncurrent Assets	1,731	1,723	8	0.5%	683
Deferred Outflows of Resources	608	324	284	87.7%	42
Total Assets & Deferred Outflows	**80,670**	**81,436**	**(766)**	**-.9%**	**65,533**
Current Liabilities	4,782	4,285	497	11.6%	3,791
Noncurrent Liabilities	24,968	23,674	1,294	5.5%	4,813
Deferred Inflows of Resources	728	1,458	(730)	-50.1%	167
Total Liabilities & Deferred Inflows	**30,478**	**29,417**	**1,061**	**3.6%**	**8,771**
Net Investment in Capital Assets	49,075	48,522	553	1.1%	48,323
Restricted for Debt Service	1,251	1,249	2	.2%	178
Restricted for Construction	2,721	2,717	4	.1%	3,961
Unrestricted	(2,854)	(468)	(2,386)	-509.8%	4,300
Total Net Position	**$50,193**	**$52,020**	**($1,827)**	**-3.5%**	**$56,762**

Capital Asset and Long-Term Debt Activity

The District's net (after depreciation) capital additions, including construction work-in-progress, were approximately $1.2 million in 2015 and $195,000 in 2014.

These additions consisted of various improvements to the District's electric infrastructure, customer line extensions and the expansion to the District's broadband system and water systems. More detailed information about the District's capital assets is presented in Note 4 to the financial statements.

At the end of the 2015 fiscal year, the District had $14.6 million in outstanding long term debt, which includes unamortized bond premium and the amount coming due within one year. This represents a decrease of 993,000 when compared to the same figure for 2014. At the end of 2014, the District had $15.6 million in outstanding long term debt which was an increase of 15.2 million from 2013.

The District issued no new bonds in 2015. In 2014, the District issued $14.7 million in new debt and retired $151,000 in existing debt, including final payment of the 2007 issue. See Note 6 to the financial statements and for additional information on the long-term debt.

Summary of Financial Position

The assets of the District exceeded its liabilities at the end of 2015 by $50.2 million (net position). ($2.9) million of this amount represents unrestricted net position, which may be used to meet ongoing obligations. Net (of related debt) investment in capital assets accounted for $49.1 million or 98 percent of the Districts net position. The District's overall financial position decreased $1.8 in 2015, when compared to 2014 (as restated).

At the end of 2014 (as restated), the assets of the District exceeded its liabilities by $52.0 million (net position). Of this, ($468,000) represents unrestricted net position, which may be used to meet ongoing obligations. Net investment in capital assets accounted for $48.5 million or 93 percent of the Districts net position. The District's overall financial position decreased in 2014, with a drop in net position of $4.7 million. The bulk of this decrease is related to the District's implementation of GASB 68.

Statement of Revenues, Expenses and Change in Net Position (in thousands)	2015	2014 As Restated	Change	% Change	2013
Operating Revenues					
Utility Sales & Service Fees	$22,031	$22,265	(234)	-1.1%	$22,317
Other Operating Revenues	1,009	650	359	55.2%	568
Non-operating Revenues					
Interest Income	37	19	18	94.7%	20
Other Income	43	547	(504)	-92.3%	2,525
Total Revenues	**23,120**	**23,481**	**(361)**	**-1.5%**	**25,430**
Operating Expenses					
Power Supply	11,790	11,079	(711)	-6.4%	11,390
Operations & Maintenance	2,526	2,443	(83)	-3.4%	2,432
Administrative	6,549	6,800	251	3.7%	5,633
Taxes & Depreciation	4,346	4,351	5	.1%	4,161
Non-operating Expenses					
Interest & Other Non-Operating Exp.	429	484	55	-11.4%	16
Total Expenses	**25,640**	**25,157**	**(483)**	**-1.9%**	**23,632**
Income (Loss) Before Capital Contributions	**(2,520)**	**(1,676)**	**(844)**	**-50.4%**	**1,798**
Capital Contributions	693	1,030	(336)	-32.7%	2,019
Change in Net Position	**(1,827)**	**(646)**	**(1,180)**	**-182.7%**	**3,817**
Beginning Net Position	52,020	56,762	(4,742)		52,945
GASB 68 Restatement		(4,096)	4,096		
Ending Net Position	**$50,193**	**$52,020**	**($1,827)**	**-3.4%**	**$56,762**

Financial Analysis

During 2015, the District's overall financial position decreased and results of operations again declined when compared to the previous year. The District's net position decreased by $1.8 million compared to a decrease in net position of $4.7 million in 2014.

The following narrative is an analysis of the change in net position by major components of income.

Operating Revenues

Total Utility Sales and Service Fees for 2015 was down $234,000 from 2014. In 2014, revenue in this category was relatively flat when compared to the prior year. Broadband and Other Operating revenue was up $359,000 from 2014, the bulk coming in Broadband revenue.

In October 2015, the District implemented a 4% Power Cost Adjustment (PCA) to its retail rates in response to increases by Bonneville in its wholesale power and transmission rates. This brought the total PCA to 7%. No rate changes were made in 2014.

Non-operating Revenues

During 2015, non-operating revenue decreased $486,000 when compared to 2014. Most of this was due to the final grant reimbursement associated with the BTOP program being received in 2014.

In 2014, Other Non-operating revenue decreased just under $2.0 million when compared to 2013. The $547,000 reported in 2014 is the final receipt of reimbursement associated with the District's BTOP Grant.

Operating Expenses

The Operating Expense category includes: Power Supply, Operation and Maintenance, Administrative and Taxes and Depreciation.

In 2015, overall Operating Expenses were up $538,000, or 2.2%, when compared to 2014. During 2014, Operating Expenses were up $1,019,000 when compared to 2013. The following explains significant year to year changes by Operating Expense category.

Power Supply

Power Supply, the largest single category of operating expenses, came in at $11.8 million in 2015, which is up 6% from $11.1 million in 2014.

In 2015, the District paid the Bonneville Power Administration (BPA) $12.2 million for power and transmission which was up 12% or $1.3 million over 2014 due in part to the Bonneville rate increase.

The District, as a slice customer is a participant in the output of the Federal Columbia River Power System (FCRPS), which includes the Columbia Generating Station at Hanford, WA. Hydro-electric generation however contributes the majority of the power produced by the FCRPS. The District is generally a net seller, meaning its share of the systems output exceeds it load. Therefore surplus sales can help offset total cost of power. Many factors, including precipitation, snow pack, natural gas prices, and others contribute to the market price for electric energy. These factors impact the prices the District receives for surplus power sales, or pays when it makes market purchases to meet its load.

The District reported net balance market activity of $1.3 million in 2015 which is up for 2014 when the District reported net balance market activity of $638,000.

Other Operating Expenses

During 2015, operating expenses (other than power supply) decreased $73,000 when compared to 2014 with most categories at or near 2014 levels. Customer Accounting, Collection and Information showed the most reduction coming in $316,000 favorable to 2014. This was driven by reduced levels of conservation rebates given in 2015.

In 2014, operating expenses (other than power supply) increased 11% or $1.3 million over 2013. The most significant increase was in the Administrative category, which was up 20% or $1.1 million. Major causes for this increase include: a $331,000 increase in the District's Other Post-Employment Benefits (OPEB) accrual driven by the release of the 2014 actuary study. The study cites the Excise Tax for 'Cadillac' Health Plans, changes in demographic experience and changes to the medical trend assumptions used in the study as primary reasons for the increase; $236,000 increase in weatherization rebates given; $196,000 increase in health care costs; and a $117,000 increase in uncollectible accounts expense which resulted from a year end entry to return the Districts reserve for uncollectible accounts to a reasonable level. It is important to note that the increased OPEB accrual and the increase in uncollectible accounts are non-cash items.

In addition, 2014 the taxes and depreciation expense exceeded the previous year by $190,000, due largely to placing telecom assets (funded by the BTOP grant) in service which 'triggers' depreciation.

Non-Operating Expenses

In 2015 Interest and Other expenses came in at $429,000 which compares favorably to 2014, when $483,000 was expended. 2014 included $189,000 of Bond issue costs however.

In 2014, this category was up $468,000 when compared to 2013. This was due to Bond issue costs and interest payments associated with the 2014 Bond issue.

Capital Contributions
Capital Contributions, primarily reimbursement received from customers for extending District facilities on their behalf, decreased $337,000 from 2014 to 2015. Customer line extension activity has yet to recover to 'normal' after the financial crisis.

In 2014, this category decreased $1 million from 2013 customer line extensions.

Requests for Information

The basic financial statements, notes and management discussion and analysis are designed to provide a general overview of the District's finances. Questions concerning any of the information provided in this report should be directed to the District at Post Office Box 472, or 405 Duryea Street, Raymond, WA 98577.

PUD No. 2 of Pacific County

MCAG 1793

STATEMENT OF NET POSITION

As of December 31, 2015 and 2014

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	2015	2014 *(As Restated)*
ASSETS		
CURRENT ASSETS		
Cash & Cash Equivalents		
Unrestricted Cash & Cash Equivalents	$ 3,045,275	$ 4,223,363
Restricted Construction Account	16,363,294	17,959,416
Accounts Receivable, net	2,796,792	2,465,781
Accrued Unbilled Revenues (Note 9)	2,073,127	1,811,984
Inventory - Materials & Supplies	3,913,100	3,905,841
Prepaid Expenses & Option Premiums	65,076	109,427
Total Current Assets	**28,256,664**	**30,475,812**
NONCURRENT ASSETS		
Restricted Bond Reserve Fund (Note 1)	1,250,385	1,248,333
Other Receivables	385,327	369,879
Other Charges (Note 9)	95,618	104,777
Subtotal Noncurrent Assets	**1,731,330**	**1,722,989**
Utility Plant (Note 4)		
Land and Non-Depreciable Assets	1,170,998	1,162,808
Electric & Water Plant in Service	100,038,103	95,468,701
Construction Work in Progress	4,980,693	6,390,183
Less: Accumulated Depreciation	(56,116,166)	(54,108,453)
Net Utility Plant	50,073,628	48,913,239
Total Noncurrent Assets	**51,804,958**	**50,636,228**
TOTAL ASSETS	**80,061,622**	**81,112,040**
DEFERRED OUTFLOWS OF RESOURCES		
Accumulated Decrease in Fair Value of Hedging Derivatives (Note 3)	115,230	53,846
Pension Defferred Outflow	492,815	270,054
Total Deferred Outflows of Resources	**608,045**	**323,900**
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	**$ 80,669,667**	**$ 81,435,940**

The accompanying notes are an integral part of the financial statements.

PUD No. 2 of Pacific County

MCAG 1793

STATEMENT OF NET POSITION

As of December 31, 2015 and 2014

(CONTINUED)

		2015		2014
NET POSITION, LIABILITIES AND DEFERRED INFLOWS OF RESOURCES				***(As Restated)***
LIABILITIES				
CURRENT LIABILITIES				
Accounts Payable	$	2,581,466	$	2,103,046
Accrued Taxes Payable		528,264		524,998
Current Portion Of Compensated Absences		559,056		545,735
Accrued Interest Payable		153,885		157,005
Revenue Bonds, Current Portion (Note 6)		959,321		954,321
Total Current Liabilities		**4,781,992**		**4,285,105**
NONCURRENT LIABILITIES				
Revenue Bonds & Other Long Term Debt (Note 6)		13,681,197		14,679,097
Compensated Absences		35,684		32,341
Net Pension Liability		3,960,083		3,050,745
Accrued Other Post Employment Benefits		6,416,464		5,198,011
Customer Deposits		758,955		659,153
Other Liabilities		115,230		53,846
Total Noncurrent Liabilities		**24,967,613**		**23,673,193**
Total Liabilities		**29,749,605**		**27,958,298**
DEFERRED INFLOWS OF RESOURCES				
Accumulated Increase in Fair Value of Hedging Derivatives (Note 3)		95,618		104,777
Pension Deferred Inflow		631,945		1,353,095
Total Deferred Inflows of Resources		**727,563**		**1,457,872**
NET POSITION				
Net Investment in Capital Assets		49,075,099		48,522,395
Restricted for Debt Service		1,250,385		1,248,333
Restricted for Construction		2,721,306		2,716,842
Unrestricted		(2,854,291)		(467,800)
Total Net Position		**50,192,499**		**52,019,770**
TOTAL NET POSITION, LIABILITIES AND DEFERRED INFLOWS OF RESOURCES	**$**	**80,669,667**	**$**	**81,435,940**

The accompanying notes are an integral part of the financial statements.

PUD No. 2 of Pacific County

MCAG 1793

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

For the year ended December 31, 2015 and 2014

	2015	2014 *(As Restated)*
OPERATING REVENUES		
Sales of Electric Energy & Water - Retail	$ 22,030,551	$ 22,265,436
Broadband Revenue	692,234	320,675
Other Operating Revenue	316,791	328,874
Total Operating Revenues	**23,039,576**	**22,914,985**
OPERATING EXPENSES		
Power Supply	11,790,190	11,079,012
Distribution Operation & Maintenance	2,276,274	2,208,136
Broadband Expense	249,414	234,973
Customer Accounting, Collection and Information	849,468	1,165,789
Administrative & General Expense	5,699,164	5,634,074
Taxes	1,319,349	1,334,999
Depreciation	3,026,150	3,016,207
Total Operating Expenses	**25,210,009**	**24,673,190**
OPERATING INCOME (LOSS)	**(2,170,433)**	**(1,758,205)**
NONOPERATING REVENUES & (EXPENSES)		
Interest Income	37,170	18,581
Other Nonoperating Income	42,577	2,444
Grant Reimbursement	-	544,924
Interest Expense	(429,381)	(294,029)
Bond Issue Costs	-	(189,425)
Total Nonoperating Revenues & Expenses	**(349,634)**	**82,495**
INCOME BEFORE CONTRIBUTIONS	**(2,520,067)**	**(1,675,710)**
CAPITAL CONTRIBUTIONS	692,796	1,029,313
CHANGE IN NET POSITION	**(1,827,271)**	**(646,397)**
TOTAL NET POSITION, BEGINNING OF YEAR	**52,019,770**	**56,762,097**
GASB 68 Restate		**(4,095,930)**
TOTAL NET POSITION, END OF YEAR	**$ 50,192,499**	**$ 52,019,770**

The accompanying notes are an integral part of the financial statements.

PUD No. 2 of Pacific County

MCAG 1793

STATEMENT OF CASH FLOWS

For the year ended December 31, 2015 and 2014

	2015	2014 *(As Restated)*
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash Received from Customers and Counterparties	$ 22,191,977	$ 22,400,720
Cash Paid to Suppliers and Counterparties	(15,227,738)	(15,488,095)
Cash Paid to Employees for Services	(3,579,473)	(3,522,148)
Taxes Paid	(1,319,349)	(1,334,999)
Net Cash Provided by Operating Activities	**2,065,417**	**2,055,478**
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition of Capital Assets	(4,186,540)	(3,211,836)
Proceeds from Sale of Revenue Bonds	-	15,390,212
Bond Principal Paid	(992,900)	(151,362)
Bond Interest Paid	(429,381)	(483,454)
Capital Contributions	692,796	1,029,313
Grant Reimbursement	0	544,924
Other	41,280	983
Net Cash Used by Capital and Related Financing Activities	**(4,874,745)**	**13,118,780**
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest Income	37,170	18,581
Net Cash Provided (Used) by Investing Activities	**37,170**	**18,581**
NET INCREASE (DECREASE) IN CASH	**(2,772,158)**	**15,192,839**
CASH BALANCE, BEGINNING OF YEAR	**23,431,112**	**8,238,273**
CASH BALANCE, END OF YEAR	**20,658,954**	**23,431,112**
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating Income (Loss)	($2,170,433)	(1,758,205)
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation & Amortization	3,026,150	3,016,207
(Increase) Decrease in Unbilled Revenues	(261,143)	65,059
Increase (Decrease) in Net OPEB Obligation	1,218,453	1,276,380
GASB 68 Pension Expense	(34,573)	37,856
Misellaneous Other Revenue & Receipts	1,297	1,461
Decrease (Increase) in Accounts Receivable	(251,939)	118,050
Decrease (Increase) in Inventories	(7,259)	(324,796)
Decrease (Increase) in Prepaids and Deposits	28,902	(75,205)
Increase (Decrease) in Accounts Payable	416,014	(584,826)
Increase (Decrease) in Accrued Taxes Payable	3,266	23,083
Increase (Decrease) in Customer Deposits	99,802	105,421
Increase (Decrease) in Other Current Liabilities	(3,120)	154,993
Net Cash Provided by Operating Activities	**$2,065,417**	**$ 2,055,478**

The accompanying notes are an integral part of the financial statements.

PUBLIC UTILITY DISTRICT NO. 2 OF PACIFIC COUNTY

Notes to Financial Statements

For Fiscal Years Ended December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of Public Utility District No. 2 of Pacific County (District) conform to generally accepted accounting principles (GAAP) as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principals. The District has applied all applicable GASB pronouncements. The following is a summary of the more significant policies:

A. Reporting Entity

Public Utility District No. 2 of Pacific County was incorporated on March 1, 1940, and operates under the laws of the State of Washington applicable to a public utility district. The District is organized as a municipal corporation, authorized under Title 54 RCW and is governed by an elected three-member Board. The District provides retail electricity to the majority of Pacific County and provides water to three areas of the County and is authorized under State law to provide wholesale telecommunication service.

B. Basis of Accounting

The accounting and reporting policies of the District are regulated by the Washington State Auditor's Office under chapter 43.09 RCW and are based on the Uniform System of Accounts prescribed for public utilities and licensees by the Federal Energy Regulatory Commission (FERC). The District uses the full accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Revenues and expenses related to the District's principal operations are considered to be operating revenues and expenses; while revenues and expenses related to capital, financing, and investing activities are considered to be non-operating revenues and expenses.

The District's financial statements include the financial position of electric and water systems and results of their operations. In the combined statements certain intersystem transactions, such as intersystem loans, interest on intersystem loans, and intersystem administrative charges are eliminated to combine total balances.

<u>New Accounting Standard</u>

The Governmental Accounting Standards Board (GASB) issued Statement No. 68 and related Statement No. 67, Financial Reporting for Pension Plans, in June 2012. GASB Statement No. 68 applies to state and local government employers in fiscal years ending after June 15, 2014. Effective for fiscal year 2015, the District implemented provisions of GASB Statement No. 68. As a result, the Statement of Net Position now includes the District's proportionate share of the net pension liability for the cost-sharing, multiple-employer plans in which the district participates. See Note 7 for additional information.

C. Cash and Cash Equivalents

For the purpose of the Statement of Cash Flows, the District considers all highly liquid investments, with maturity of three months or less when purchased, to be cash equivalents.

D. Utility Plant and Depreciation

Major expenditures (exceeding $1,500) for capital assets, including capital leases and major repairs that increase useful lives, are capitalized. Maintenance, repairs, and minor renewals are accounted for as expenses when incurred.

All capital assets are valued at historical cost or estimated historical cost, where historical cost is not known. Preliminary costs incurred for proposed projects are deferred until construction of the project is completed. Costs relating to projects ultimately constructed are transferred to the utility's plant assets. Charges that relate to abandoned projects are expensed.

See Note 4 – Capital Assets for additional information.

E. Restricted Funds

In accordance with bond resolutions (and certain related agreements) separate restricted funds are required to be established. The assets held in these funds are restricted for specific uses including construction, debt service and other special reserve requirements.

The restricted assets are composed of the following:

	2015	2014
Bond Reserve	1,250,385	1,248,333
Construction Funds	16,363,294	17,959,416

F. Receivables and Allowance for Doubtful Accounts

Management periodically assesses the collectability of accounts receivable. This assessment provides the basis for the allowance for doubtful accounts and the related bad debt expense. The District’s allowance for doubtful accounts was $132,845 and $117,285 as of December 31, 2015 and 2014.

G. Inventories

Inventories are valued at average cost, which approximates the market value.

H. Compensated Absences

Personal Leave

The District provides its employees with a single Personal Leave (PL) plan, in lieu of separate programs for vacation and illness benefits. Employees accrue PL based upon their length of service. PL is charged as a component of payroll overhead as time is incurred by an employee. A corresponding liability is recognized until such time an employee uses or sells PL to the District in accordance with the terms of the plan.

In accordance with the terms and conditions of the Health Reimbursement Arrangement – Voluntary Employees' Beneficiary Association (HRA-VEBA) Plan, the CBA and/or District Resolution:

- Personal Leave is payable in full upon an employee's resignation or death.
- At retirement, the District will deposit the cash value of any unused PL hours to the retirees HRA-VEBA account.

Supplemental Leave Bank

Employees with sick leave balances remaining under the terms of the former sick leave plan were able to transfer the balance into a Supplemental Leave Bank (SLB). No additional hours may be posted to the SLB.

In accordance with the terms and conditions of the HRA-VEBA Plan, the CBA and/or District Resolution:

- An employee on Short Term Disability may utilize SLB hours to make up the difference between the 70% pay they received while on STD and 100% of their regular earnings.
- Employees with SLB balances receive an annual transfer of the cash value of up to 16 SLB hours to their respective HRA-VEBA accounts.
- Employees who leave employment due to resignation or retirement forfeit any remaining hours in their respective SLBs.
- In the event of the death of an active employee, the surviving dependents shall receive 50% of the cash value remaining in the deceased employee's SLB.

Changes in the Compensated Absences during the current and prior fiscal period are as follows:

Balance as of December 31, 2014	$578,076
Earned during 2015	564,379
Taken during 2015	547,714
Balance as of December 31, 2015	$594,741
Balance as of December 31, 2013	$577,464
Earned during 2014	518,742
Taken during 2014	518,130
Balance as of December 31, 2014	$578,076

The District estimates $559,057 will be used in the next fiscal year. The current and noncurrent liability for unpaid personal time off appears on the statement of net position.

See Note 7 – Pension Plans for additional information on the HRA-VEBA plan.

I. Purchase Commitments

See Note 13 – Power Supply; for contracts with the Bonneville Power Administration and others for future power supply.

J. Revenue Recognition

Revenues from retail sales of electricity include an estimate for energy delivered to customers between the last billing date and the end of the year. This amount is reflected in the accompanying financial statements in the amount of $2,073,127 at December 31, 2015 and $1,811,984 at December 31, 2014. This estimate impacted electric revenue by $261,143 in 2015 and ($65,059) in 2014.

K. Capital Contributions

Capital contributions for the District consist mainly of line extension fees. Line extension fees represent amounts collected to recover the costs of installing new lines. Capital contributions are recorded as revenues when received.

L. Unamortized Bond Premium

Bond premium is amortized to interest expense using the effective interest method over the term of the bonds.

M. Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of all state sponsored pension plans and additions to/deductions from those plans' fiduciary net position have been determined on the same basis as they are reported by the Washington State Department of Retirement Systems. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

N. Reclassification

Certain amounts reported with the 2014 financial statements have been reclassified to conform to the 2015 presentation. Such reclassifications would have no effect on previously reported results of operations and cash flows. See note 14 for additional information.

NOTE 2 - DEPOSITS AND INVESTMENTS

<u>Deposits</u>

The District's deposits and certificates of deposits are entirely covered by federal depository insurance Federal Depository Insurance Commission (FDIC) and/or Federal Savings and Loan Insurance Commission (FSLIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

Custodial credit risk – Deposits. For a deposit, this is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District's deposits and certificates of deposit are entirely covered by the FDIC and/or FSLIC and by collateral held in a multiple financial institution collateral pool administered by the PDPC. Under state law, public depositories under the PDPC are required to pledge securities as collateral at 100 percent of all deposited uninsured public funds. As a result, deposits covered by collateral held in the multiple financial institution collateral pool are considered to be insured. State law requires that deposits may only be made with institutions that are approved by the PDPC.

For balance sheet purposes, the Washington State Treasurer's Local Government Investment Pool (LGIP) is considered a cash equivalent. The LGIP is unrated.

NOTE 3 - DERIVATIVE INSTRUMENTS

The District enters into derivative energy transactions to hedge its known or expected positions within its approved Risk Management policy. Decisions are made to enter into forward transactions to protect its financial position, specifically to deal with expected long and short positions as determined by projected load and resource balance positions, with the objective of providing stable rates and meeting budget.

The District has adopted GASB Statement No. 53, Accounting and Financial Reporting for Derivative Instruments. Subject to certain exceptions, GASB Statement No. 53 requires that every derivative instrument be recorded on the statement of net position as an asset or liability measured at its fair value, and that changes in the derivative's fair value be recognized currently in earnings unless such derivatives meet specific hedge accounting criteria to be determined as effective. Effective hedges qualify for hedge accounting and such changes in fair values are deferred. These are recorded on the statement of net position as deferred inflows/outflows of resources as accumulated increase/decrease in fair value of hedging derivatives.

It is the District's policy to document and apply as appropriate the normal purchase and normal sales exceptions under GASB Statement No. 53. The District has reviewed its various contractual arrangements to determine applicability of these standards. Purchases and sales of forward electricity and option contracts that require the physical delivery and which are expected to be used or sold by the reporting entity in the normal course of business are generally considered "normal purchases and normal sales." These transactions are excluded from GASB Statement No. 53 and therefore are not required to be recorded at fair value in the financial statements. Financial swaps for electricity are considered to be derivatives under GASB Statement No. 53, but generally do not meet the "normal purchases and normal sales" criteria. Options are amortized to power costs over the exercise period of the option.

At December 31, 2015 and 2014 the District had the following hedging derivative instruments outstanding.

Changes in Fair Value		Fair Value at December 31, 2015		
Classification	Amount	Classification	Amount	Notional
Other Credit	$ 115,230	Deferred Outflow	$ 115,230	19,195 MWh
Other Charge	$ 95,618	Deferred Inflow	$ 95,618	21,435MWh

Changes in Fair Value		Fair Value at December 31, 2014		
Classification	Amount	Classification	Amount	Notional
Other Credit	$ 53,846	Deferred Outflow	$ 53,846	8,840 MWh
Other Charge	$ 104,777	Deferred Inflow	$ 104,777	2,240 MWh

Options and Swaps Hedging Derivatives:

	2015	2014
Notional value	$247,760	$107,046
Volumes (MWH)	48,070	24,520
Fair value - asset	$115,230	$53,846
Fair value - liability	$95,618	$104,777
Reference rates	Mid-C index	Mid-C index
Dates entered into	4/14/15 – 11/18/15	1/16/13-12/16/14
Dates of maturity	1/16 – 12/17	1/15 – 12/15
Cash paid	$36,785	$11,552

The fair values used for mark-to-market amounts are based on the future price curve for the Mid-Columbia Intercontinental Exchange.

The District has developed a credit policy that establishes guidelines for setting credit limits and monitoring credit exposure on a continuous basis. The policy addresses frequency of counterparty credit evaluations, credit limits per specific counterparty and counterparty credit concentration limits. Commodity transactions, both physical and financial, are entered into only with counterparties approved by the District's Risk Management Committee for creditworthiness. The District has entered into master enabling agreements with various counterparties, such as International Swaps and Derivatives Association (ISDA) Agreements for financial transactions. All of the enabling agreements have provisions addressing credit exposure and provide for various remedies to assure financial performance, including the ability to call on additional collateral as conditions warrant, generally as determined by the exposed party. The District also uses netting provisions in the agreements to diffuse a portion of the risk.

The District proactively works to eliminate or minimize basis risk on energy transactions by entering into derivative transactions that settle pursuant to an index derived from market transactions at the point physical delivery is expected to take place. There are no derivative transactions outstanding that carry basis risk as of December 31, 2015. As of December 31, 2015, no termination events have occurred, and there are no outstanding transactions with material termination risk. There is no rollover, interest rate or market access risk for these derivative products at December 31, 2015.

NOTE 4 - CAPITAL ASSETS

Electric and Water plant activity for the year ended December 31, 2015, was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Utility Plant Not Being Depreciated:				
Land	$1,162,808	8,190		$1,170,998
Construction in Progress	6,390,183		(1,409,490)	4,980,693
Total	**7,552,991**	**8,190**	**(1,409,490)**	**6,151,691**
Utility Plant Being Depreciated:				
Transmission Plant	4,757,896			4,757,896
Distri bution Plant	66,762,668	4,486,966	(618,498)	70,631,136
Telecom Plant	10,140,305	892,326	(47,151)	10,985,480
General Plant	11,233,408	113,634	(290,918)	11,056,124
Water Plant	2,574,424	50,802	(17,759)	2,607,467
Total	**95,468,701**	**5,543,728**	**(974,325)**	**100,038,103**
Less: Accumulated Depreciation	(54,108,453)	(3,026,150)	1,018,437	(56,116,166)
Total Net Utility Plant	**$48,913,239**	**2,525,768**	**(1,365,379)**	**$50,073,628**

Electric and Water plant activity for the year ended December 31, 2014, was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Utility Plant Not Being Depreciated:				
Land	$1,132,808	30,000		$1,162,808
Construction in Progress	6,114,625	275,558		6,390,183
Total	**7,247,433**	**305,558**		**7,552,991**
Utility Plant Being Depreciated:				
Transmission Plant	4,757,896			4,757,896
Distribution Plant	64,546,109	2,465,645	(249,086)	66,762,668
Telecom Plant	9,288,509	861,292	(9,496)	10,140,305
General Plant	11,242,106	172,502	(181,200)	11,233,408
Water Plant	2,577,068		(2,644)	2,574,424
Total	**92,411,688**	**3,499,439**	**(442,426)**	**95,468,701**
Less: Accumulated Depreciation	(50,941,511)	(3,671,756)	504,814	(54,108,453)
Total Net Utility Plant	**$48,717,610**	**$133,241**	**$62,388**	**$48,913,239**

Property, plant and equipment are depreciated using the straight-line method over the following estimated useful lives:

Buildings & Improvements	25-40 years
Electric Plant – Transmission	17-30 years
Electric Plant – Distribution	17-33 years
Transportation Equipment	7-10 years
General Plant & Equipment	5-20 years
Water Plant	5-40 years
Telecommunications	7-20 years

The estimated original cost of operating property retired or otherwise disposed of and the cost of removal, less salvage, is charged to accumulated depreciation. However, in the case of the sale of a significant operating unit or system, the original cost is removed from the utility plant accounts; accumulated depreciation is charged with accumulated depreciation related to the property sold, and the net gain or loss on disposition is credited or charged to income. There were no sales of significant units or systems in 2014 or 2015.

NOTE 5 - LEASES

The District is committed under annual operating leases for office equipment. Lease expense for the years ended December 31, 2015 and 2014 amounted to $13,871 and $12,812 respectively. For these leases, the minimum annual lease commitments for 2016 are $14,000. These leases expire in October 2016. The District had no capital leases during 2015.

NOTE 6 - LONG-TERM DEBT

Revenue Bonds

In April 2014 the District issued $10.0 million in Tax Exempt, Bank Qualified Electric System Revenue Bonds (2014A) to fund capital improvements, pay for bond issuance costs (including bond insurance) and fund bond debt service and reserve accounts ($850,374). Principal payments on these bonds begin in September 2015, maturing annually in varying amounts through September 2033. The bonds have annual interest rates ranging from 3.00% to 5.00%.

In April 2014 the District issued $4.67 million in Taxable Electric System Revenue Bonds (2014B) to fund capital improvements, pay for bond issuance costs (including bond insurance) and fund bond debt service and reserve accounts ($397,124). Principal payments on these bonds begin in September 2015, maturing annually in varying amounts through September 2019. The bonds have annual interest rates ranging from 1.00% to 2.42%.

During the year ended December 31, 2015, the following changes occurred in long-term debt:

Issue	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
2014A (BQ) Electric Revenue Bonds, interest at 3.00% - 5.00%, maturing in 2033; Original Issue amount: $10,000,000	10,000,000	-	-	10,000,000	-
2014B Electric Revenue Bonds, interest at 1.00% - 2.420%, maturing in 2019; Original Issue amount: $4,670,000	4,670,000	-	(930,000)	3,740,000	935,000
DWSRF Loan – Bay Center Water, interest at .5%, maturing in 2024; Original Issue amount: $462,091	243,206	-	(24,320)	218,886	24,321
Subtotal	14,913,206	-	(954,320)	13,958,886	959,321
Plus: Unamortized Premium	720,212	-	(38,580)	681,632	-
Totals	**$15,633,418**	**-**	**($992,900)**	**$14,640,518**	**$959,321**

During the year ended December 31, 2014, the following changes occurred in long-term debt:

Issue	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
2007 Electric Refunding Bonds, interest at 3.95%, maturing in 2018; Original Issue amount: $1,756,150	$127,041	-	($127,041)	-	-
2014A (BQ) Electric Revenue Bonds, interest at 3.00% - 5.00%, maturing in 2033; Original Issue amount: $10,000,000	-	10,000,000	-	10,000,000	-
2014B Electric Revenue Bonds, interest at 1.00% - 2.420%, maturing in 2019; Original Issue amount: $4,670,000	-	4,670,000	-	4,670,000	930,000
DWSRF Loan – Bay Center Water, interest at .5%, maturing in 2024; Original Issue amount: $462,091	267,526	-	(24,320)	243,206	24,321
Subtotal	394,567	14,670,000	(151,361)	14,913,206	954,321
Plus: Unamortized Premium	-	752,363	(32,151)	720,212	-
Totals	**$394,567**	**$15,422,363**	**($183,512)**	**$15,633,418**	**$954,321**

Scheduled principal maturities and interest requirements on the Revenue Bonds are as follows:

Year	Principal	Interest	Total
2016	$959,321	$461,660	$1,420,981
2017	969,321	452,188	1,421,509
2018	984,321	439,781	1,424,102
2019	1,004,321	420,459	1,424,780
2020	1,024,320	396,158	1,420,478
2021-2025	4,267,282	1,470,166	5,737,448
2026-2030	2,785,000	821,725	3,606,725
2031-2035	1,965,000	196,375	2,161,375
Total	$13,958,886	$4,658,512	$18,617,398

In accordance with Bond Resolutions and the Official Bond Statements, separate restricted fund accounts are required to be established. The assets held in these fund accounts are restricted for specific uses, including debt service and other specific uses.

Applicability of Federal Arbitrage Regulations

Certain debt issuances of the District issued after the Tax Reform Act of 1986 are subject to the federal arbitrage regulations. The arbitrage rebate regulations require that all earnings from the investment of gross proceeds of an issue in excess of the amount that could have been earned had the yield on the investment been equal to the yield on the bonds be remitted to the federal government. These carry strict penalties for noncompliance including taxability of interest retroactive to the date of the issue. The District's management believes it is in compliance with these rules and regulations.

Intersystem Loan to Lebam Water System

During 2004, the Electric Department issued a $50,000 Long Term loan to the Lebam Water System to help cover startup costs associated with the new system. Lebam Water pays monthly interest to the Electric Department. The interest rate is based on percentage of interest earned on the District's funds in the LGIP. This loan is eliminated in the combined financial statements and is not included in the totals presented in the accompanying financial statements.

NOTE 7 - PENSION PLAN

The following table represent the aggregate pension amounts for all plans subject to the requirements of the GASB Statement 68, *Accounting and Financial Reporting for Pensions* for the year 2015 and 2014:

Aggregate Pension Amounts – All Plans		
	2015	**2014**
Pension liabilities	$3,960,083	$3,050,745
Deferred outflows of resources	$492,815	$270,054
Deferred inflows of resources	$631,945	$1,353,095
Pension expense/expenditures	$34,573	$37,856

State Sponsored Pension Plans

Substantially all District full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing, multiple-employer public employee defined benefit and defined contribution retirement plans. The state Legislature establishes, and amends, laws pertaining to the creation and administration of all public retirement systems.

The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to:

Department of Retirement Systems
Communications Unit
P.O. Box 48380
Olympia, WA 98540-8380

Or the DRS CAFR may be downloaded from the DRS website at www.drs.wa.gov.

Public Employees' Retirement System (PERS)
PERS members include elected officials; state employees; employees of the Supreme, Appeals and Superior Courts; employees of the legislature; employees of district and municipal courts; employees of local governments; and higher education employees not participating in higher education retirement programs. PERS is comprised of three separate pension plans for membership purposes. PERS plans 1 and 2 are defined benefit plans, and PERS plan 3 is a defined benefit plan with a defined contribution component.

PERS Plan 1 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service. The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service. Members retiring from active status prior to the age of 65 may receive actuarially reduced benefits. Retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries. PERS 1 members were vested after the completion of five years of eligible service. The plan was closed to new entrants on September 30, 1977.

Contributions
The **PERS Plan 1** member contribution rate is established by State statute at 6 percent. The employer contribution rate is developed by the Office of the State Actuary and includes an administrative expense component that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates.

The PERS Plan 1 required contribution rates (expressed as a percentage of covered payroll) for 2015 and 2014 were as follows:

PERS Plan 1		
Actual Contribution Rates:	**Employer**	**Employee**
January through June 2015	9.21%	6.00%
July through December 2015	11.18%	6.00%

PERS Plan 1		
Actual Contribution Rates:	**Employer**	**Employee**
January through December 2014	9.21%	6.00%

The District's actual contributions to the plan were $0.00 for the year ended December 31, 2015 and $0.00 for the year ended December 31, 2014.

PERS Plan 2/3 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service for Plan 2 and 1 percent of AFC for Plan 3. The AFC is the average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older, are eligible for early retirement with a benefit that is reduced by a factor that varies according to age for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions:

- With a benefit that is reduced by three percent for each year before age 65; or

- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules.

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service credit. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit. Other PERS Plan 2/3 benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the CPI), capped at three percent annually and a one-time duty related death benefit, if found eligible by the Department of Labor and Industries. PERS 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service if 12 months of that service are earned after age 44.

PERS Plan 3 defined contribution benefits are totally dependent on employee contributions and investment earnings on those contributions. PERS Plan 3 members choose their contribution rate upon joining membership and have a chance to change rates upon changing employers. As established by statute, Plan 3 required defined contribution rates are set at a minimum of 5 percent and escalate to 15 percent with a choice of six options. Employers do not contribute to the defined contribution benefits. PERS Plan 3 members are immediately vested in the defined contribution portion of their plan.

<u>Contributions</u>
The **PERS Plan 2/3** employer and employee contribution rates are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. The Plan 2/3 employer rates include a component to address the PERS Plan 1 UAAL and an administrative expense that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and

Plan 3 contribution rates. The PERS Plan 2/3 required contribution rates (expressed as a percentage of covered payroll) for 2015 and 2014 were as follows:

PERS Plan 2/3		
Actual Contribution Rates:	**Employer 2/3**	**Employee 2**
January through June 2015	9.21%	4.92%
July through December 2015	11.18%	6.12%
Employee PERS Plan 3		Varies

PERS Plan 2/3		
Actual Contribution Rates:	**Employer 2/3**	**Employee 2**
January through December 2014	9.21%	4.92%
July through 2014	9.21%	4.92%
Employee PERS Plan 3		Varies

Both the District and its employees made the required contributions during fiscal years 2015 and 2014. The District's required contributions for the years ending December 31, were as follows:

	2015	**2014**
PERS Plan 1 UAAL	$210,911	$183,792
PERS Plan 2/3	$271,015	$227,569
Total	**$481,926**	**$411,361**

Actuarial Assumptions

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2015 with a valuation date of June 30, 2014. The actuarial assumptions used in the valuation were based on the results of the Office of the State Actuary's (OSA) *2007-2012 Experience Study*.

Additional assumptions for subsequent events and law changes are current as of the 2014 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2015. Plan liabilities were rolled forward from June 30, 2014, to June 30, 2015, reflecting each plan's normal cost (using the entry-age cost method), assumed interest and actual benefit payments.

- **Inflation:** 3% total economic inflation; 3.75% salary inflation
- **Salary increases**: In addition to the base 3.75% salary inflation assumption, salaries are also expected to grow by promotions and longevity.
- **Investment rate of return:** 7.5%

Mortality rates were based on the RP-2000 report's Combined Healthy Table and Combined Disabled Table, published by the Society of Actuaries. The OSA applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100 percent Scale BB. Mortality rates are applied on a generational basis; meaning, each member is assumed to receive additional mortality improvements in each future year throughout his or her lifetime.

There were minor changes in methods and assumptions since the last valuation.

- The OSA updated demographic assumptions, consistent with the changes from the *2007-2012 Experience Study Report*, used when valuing the PERS 1 and TERS 1 Basic Minimum COLA.

- The OSA corrected how valuation software calculates a member's entry age under the entry age normal actuarial cost method. Previously, the funding age was rounded, resulting in an entry age one year higher in some cases.

- For purposes of calculating the Plan 2/3 Entry Age Normal Cost contribution rates, the OSA now uses the current blend of Plan 2 and Plan 3 salaries rather than using a long-term membership assumption of two-thirds Plan 2 members and one-third Plan 3 members.

- The OSA changed the way it applies salary limits, as described in the *2007-2012 Experience Study Report*.

Discount Rate

The discount rate used to measure the total pension liability for all DRS plans was 7.5 percent. To determine that rate, an asset sufficiency test included an assumed 7.7 percent long-term discount rate to determine funding liabilities for calculating future contribution rate requirements. (All plans use 7.7 percent except LEOFF 2, which has assumed 7.5 percent). Consistent with the long-term expected rate of return, a 7.5 percent future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue being made at contractually required rates (including PERS 2/3, PSERS 2, SERS 2/3, and TRS 2/3 employers, whose rates include a component for the PERS 1, and TRS 1 plan liabilities). Based on these assumptions, the pension plans' fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.5 percent was used to determine the total liability.

Long-Term Expected Rate of Return

The long-term expected rate of return on the DRS pension plan investments of 7.5 percent was determined using a building-block-method. The Washington State Investment Board (WSIB) used a best estimate of expected future rates of return (expected returns, net of pension plan investment expense, including inflation) to develop each major asset class. Those expected returns make up one component of WSIB's capital market assumptions. The WSIB uses the capital market assumptions and their target asset allocation to simulate future investment returns at various future times. The long-term expected rate of return of 7.5 percent approximately equals the median of the simulated investment returns over a 50-year time horizon.

Estimated Rates of Return by Asset Class

Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2015, are summarized in the table below. The inflation component used to create the table is 2.2 percent and represents the WSIB's most recent long-term estimate of broad economic inflation.

Asset Class	Target Allocation	% Long-Term Expected Real Rate of Return Arithmetic
Fixed Income	20%	1.70%
Tangible Assets	5%	4.40%
Real Estate	15%	5.80%
Global Equity	37%	6.60%
Private Equity	23%	9.60%
	100%	

Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2014, are summarized in the table below. The inflation component used to create the table is 2.7 percent and represents the WSIB's most recent long-term estimate of broad economic inflation.

Asset Class	Target Allocation	% Long-Term Expected Real Rate of Return Arithmetic
Fixed Income	20%	0.80%
Tangible Assets	5%	4.10%
Real Estate	15%	5.30%
Global Equity	37%	6.05%
Private Equity	23%	9.05%
	100%	

Sensitivity of NPL

The table below presents the District's proportionate share of the net pension liability calculated using the discount rate of 7.5 percent, as well as what the District's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (6.5 percent) or 1-percentage point higher (8.5 percent) than the current rate.

12/31/2015	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
PERS 1	$2,561,479	$2,103,880	$1,710,386
PERS 2/3	5,427,634	1,856,203	(878,308)

12/31/2014	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
PERS 1	$2,479,424	$2,011,543	$1,609,913
PERS 2/3	4,334,734	1,039,202	(1,477,971)

Pension Plan Fiduciary Net Position

Detailed information about the State's pension plans' fiduciary net position is available in the separately issued DRS financial report.

Pension Liabilities (Assets), Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At June 30, 2015, the District reported a total pension liability of $3,960,083 for its proportionate share of the net pension liabilities as follows:

	Liability (or Asset)
PERS 1	$2,103,880
PERS 2/3	1,856,203
TOTAL	$3,960,083

At June 30, 2014, the District reported a total pension liability of $3,050,745 for its proportionate share of the net pension liabilities as follows:

	Liability (or Asset)
PERS 1	$2,011,543
PERS 2/3	1,039,202
TOTAL	$3,050,745

At June 30, 2015 the District's proportionate share of the collective net pension liabilities was as follows:

	Proportionate Share 6/30/14	Proportionate Share 6/30/15	Change in Proportion
PERS 1	0.039931%	0.040220%	0.000289%
PERS 2/3	0.051411%	0.051950%	0.000539%

At June 30, 2014 the District's proportionate share of the collective net pension liabilities was as follows:

	Proportionate Share 6/30/13	Proportionate Share 6/30/14	Change in Proportion
PERS 1	0.037239%	0.039931%	0.002692%
PERS 2/3	0.049592%	0.051411%	0.001819%

Employer contribution transmittals received and processed by the DRS for the fiscal year ended June 30 are used as the basis for determining each employer's proportionate share of the collective pension amounts reported by the DRS in the *Schedules of Employer and Nonemployer Allocations* for all plans.

The collective net pension liability (asset) was measured as of June 30, 2015, and the actuarial valuation date on which the total pension liability (asset) is based was as of June 30, 2014, with update procedures used to roll forward the total pension liability to the measurement date.

Pension Expense

For the year ended December 31, 2015, the District recognized pension expense as follows:

	Pension Expense
PERS 1	$48,805
PERS 2/3	(14,232)
TOTAL	$34,573

For the year ended December 31, 2014, the District recognized pension expense as follows:

	Pension Expense
PERS 1	$82,491
PERS 2/3	(44,635)
TOTAL	$37,856

Deferred Outflows of Resources and Deferred Inflows of Resources

At December 31, 2015 and December 31, 2014, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

PERS 1	Deferred Outflows of Resources 2015	2014	Deferred Inflows of Resources 2015	2014
Effect of change in the employers proportionate share	$ -	$ -	$ -	$ -
Net difference between projected and actual investment earnings on pension plan investments	-	-	136,427	251,532
Changes in proportion and differences between contributions and proportionate share of contributions	-	-	-	-
Contributions subsequent to the measurement date	119,322	93,285	-	-
TOTAL	**$119,322**	**$93,285**	**$136,427**	**$251,532**

PERS 2/3	Deferred Outflows of Resources 2015	2014	Deferred Inflows of Resources 2015	2014
Effect of change in the employers proportionate share	$17,343	$ -	$ -	$ -
Differences between expected and actual experience	197,315	-	-	-
Net difference between projected and actual investment earnings on pension plan investments	-	-	495,518	1,101,563
Changes of assumptions	2,991	-	-	-
Changes in proportion and differences between contributions and proportionate share of contributions	-	-		-
Contributions subsequent to the measurement date	155,844	116,357	-	-
TOTAL	**$373,493**	**$116,357**	**$495,518**	**$1,101,563**
TOTAL ALL PLANS	**$492,815**	**$209,642**	**$631,945**	**$1,353,095**

Deferred outflows of resources related to pensions resulting from the District's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2016. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	PERS 1	PERS 2/3
2016	$ -	$5,101
2017	-	$5,101
2018	-	$5,101
2019	-	$2,040
2020	-	-
Thereafter	-	-

The District's payroll subject to PERS plans for the years ended December 31, 2015 and 2014 was $4,791,219 and $4,555,486 respectively. The District's total payroll for all employees for the same periods was $4,956,342 and $4,675,826 respectively.

HRA VEBA

In 2006, the Commissioners approved Resolution No. 1248 authorizing participation in a Health Reimbursement Arrangement / Voluntary Employees' Beneficiary Association Plan., as allowed under IRS Code section 501(C)(9).

Under the plan, the District participates in the Voluntary Employees' Beneficiary Association (VEBA) for Public Service Employees in the Northwest trust, commonly referred to as the HRA VEBA Plan that was established on October 21, 1992 for public sector employees with updated IRS letter of determination March 14, 2000. Contributions are made for the benefit of District employees under three different VEBA groups - for "A" Group or "B" Group IBEW Local Union No. 77 employees, and for non-union employees.

The plan covers all District employees. All employees within their respective VEBA group contribute an amount as described in the plan's documentation. Contributions may be adjusted from time-to-time by a majority vote of the specific VEBA group.

For 2015, employee contributions totaled $98,806 and the District contributed an additional $38,546 on behalf of its employees. In 2014, employee contributions were $82,770 and the District contributed $33,008.

Deferred Compensation Plans

By resolution, the District offers its employees two deferred compensation plans created in accordance with Internal Revenue Code Section 457. These plans are with The Hartford Financial Services Group, Inc., and with the Washington State Department of Retirement Systems (DRS) Deferred Compensation Program (DCP). The plans, available to all active employees, permit them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

The IRC of 1986, as amended, required the District to establish a trust exempt from tax under IRC Section 457 (g) and 501 (a). A trust was established with each of the plan administrators and the plan is operated for the exclusive benefit of the participants and their beneficiaries. The assets in the plans are not subject to any claims of the District's general creditors. The District has no liability for losses under the plan but does have the duty of due care that would be required of an ordinary prudent investor.

Participation in the Districts deferred compensation plans is voluntary on the part of the employee. Contributions to these plans are 100% employee funded.

NOTE 8 - TELECOMMUNICATION SERVICES

The District has installed and continues to build out a fiber optic backbone system in its service area for internal use by the Electric Department. In July of 2003, the District connected its fiber optic system to Northwest Open Access Network's (NoaNet's) fiber optic communications system and began making excess capacity available at wholesale rates to retail service providers. These retail providers are in turn offering end users access to the District's fiber for Internet and point-to-point interconnections on a retail basis.

Wholesale Telecommunications operations and capital activity for the years ended December 31, 2015 and 2014 follows:

Telecommunication Services	2015	2014
Operating Revenues:		
Wholesale Fiber Services to ISP	$395,867	$285,855
Installation Charges (Capital Contributions)	$274,647	$96,959
Other	$21,720	$34,820
Total Revenues	$692,234	$417,634
Operating Expenses		
Administration and General	$81,205	$75,905
Repairs and Maintenance	$89,563	$79,587
Network Coordinated Services	$46,157	$44,031
Tower Lease	$9,900	$10,800
Interconnection Access	$17,820	$19,440
NoaNet Repayments	$4,200	$4,200
Other	$569	$1,010
Total Operating Expenses	$249,414	$234,973
Plant in Service	$10,985,479	$10,140,305
Construction Work in Progress	$539,583	$274,614

Northwest Open Access Network, Inc. (NoaNet)

The District, along with several other Washington State Public Utility Districts and Energy Northwest, is a member of NoaNet, a Washington nonprofit mutual corporation. NoaNet was incorporated in February 2000 to provide a broadband communications backbone, over Public Benefit Fibers leased from Bonneville Power Administration, throughout the Pacific Northwest for assisting its members in the efficient management of load, conservation and acquisition of electric energy as well as other purposes. The network began commercial operation in January 2001.

As a member of NoaNet, and as allowed by RCW 54.16, the District has guaranteed certain portions of NoaNet debt based on its proportionate share and has entered into Repayment Agreements to guarantee the debt of NoaNet (see Note 9). The District's current membership interest is 8.19% Under the Repayment Agreements, each Member acknowledges and agrees that it is a guarantor of the payment of principal and interest on the Bonds and is liable by assessment or otherwise to repay NoaNet for amounts due and owing with respect to such principal and interest up to each Member's Percentage Interest. NoaNet may assess its Members for their percentage share of principal and interest on the debt to the extent that NoaNet does not have sufficient funds to pay the debt.

The management of NoaNet anticipates meeting debt obligations through profitable operations; however, there is no assurance NoaNet's plan will be achieved. There were no member assessments in 2015 or 2014. In December of 2014, NoaNet secured a $13,000,000 line of credit to retire both the 2012 and 2014 lines of credit as well as to finance additional capital construction. Both of the pre-existing lines of credit were paid off and closed as of December 31, 2014. NoaNet drew $5,771,729 for the retirement of the lines of credit during 2014 and through fourth quarter 2015, NoaNet has drawn $2,000,000 on this new line for capital expenditures. As of December 31, 2015, the outstanding balance is $6,254,827.

Operationally, NoaNet reported a positive net position of $83,190,094 (unaudited) as of December 31, 2015, and a positive net position of $87,441,885 as of December 31, 2014. NoaNet recorded a decrease in net position of ($4,251,792) (unaudited) in 2015, and a decrease of ($1,214,475) for 2014.

In accordance with Accounting Principles Board Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock, as well as a position statement issued by the Washington State Auditor concerning the appropriate accounting treatment for NoaNet, a proportionate share of the changes in net position has not been recorded by the District. In accordance with GASB 70 – Financial Reporting for Non-exchange Financial Guarantees, the District has included all required disclosures for its guarantee of NoaNet debt (see Note 9).

Financial statements for NoaNet may be obtained by writing to: Northwest Open Access Network, Chief Financial Officer, 5802 Overlook Ave NE, Tacoma, WA 98422.

Broadband Technology Opportunities Program Grant

At its March 10th, 2010 meeting, the NoaNet Board of Directors adopted a resolution accepting an American Recovery and Reinvestment Act - Broadband Technology Opportunities Program (BTOP) grant from the National Telecommunications and Information Administration. The total amount of the grant was $84,347,997. The District was one of seven sub-recipients and was scheduled to receive $4,149,031 for two fiber build projects to underserved areas of Pacific County. At its March 16th, 2010 meeting the District's Board of Commissioners, by motion, accepted the conditions and regulations of the award as stated in the grant. As a condition of the grant, the District provided $2,627,194 in cash and in-kind contributions towards the two fiber builds, the cash portion being an amount that the District budgeted for over the ensuing three years, the term of construction per the requirements of the grant. During 2011, the District received $609,874 in BTOP grant reimbursement. No BTOP reimbursement was received in 2012. BTOP reimbursement received in 2013 totaled $2,450,021 which included $2,245,568 in cash and $204,453 in assets transferred from NoaNet to the District. All remaining funds, approximately $544,924, were received in 2014.

NOTE 9 - FINANCIAL GUARANTEES

Repayment Agreement: NoaNet Revenue Bonds and Lines of Credit (see Note 8)

In July 2001, NoaNet issued $27 million in Telecommunications Network Revenue Bonds (2001 Bonds) to finance the repayment of the founding members and the costs of initial construction, operations, and maintenance. The Bonds became due beginning in December 2003 through December 2016 with interest due semi-annually at rates ranging from 5.05% to 7.09%. In June 2011, NoaNet issued $13,165,000 in Telecommunications Network Revenue Refunding Bonds (2011 Refunding Bonds) to refinance certain 2001 Bonds. The 2011 Refunding Bonds become due in December 2012 through December 2016 with interest due semi-annually at rates ranging from 0.75% to 3.0%. The final principal payment on the non-refunded 2001 Bonds was made in December 2011.

The amount of outstanding Bonds was $2,790,000 and $5,510,000 at December 31, 2015 and 2014, respectively. Current and former Members of NoaNet have entered into a Repayment Agreement to guarantee the debt of NoaNet. Under the Repayment Agreement, each guarantor acknowledges and agrees that it is a guarantor of the payment of the principal of and interest on the Bonds and is liable by assessment or otherwise to repay NoaNet for amounts due and owing with respect to such principal and interest up to each Member's percentage interest. The District's guarantee is 4.31% of the outstanding Bonds, or $120,249 and $237,481 as of December 31, 2015 and 2014, respectively.

In the event of a failure by any guarantor to pay such amounts when due, NoaNet may bill from time to time as necessary, and each guarantor is obligated to pay 30 days after receipt of the bill, an additional amount up to a maximum of 25% of such Member's percentage interest (the "Step-Up"), up to the maximum percentage interest, in order to cover the deficiency caused by such Member(s) failure to pay. Any Member that pays an additional amount to cover a deficiency reserves all rights to seek reimbursement from the Member(s) that failed to pay. The District's maximum percentage interest is 5.39% or $150,381 and $269,989 as of December 31, 2015 and 2014, respectively.

In August 2009, NoaNet opened a $1.5 million Line of Credit with Bank of America to fund capital expenditures. This Note was guaranteed by the Members. The outstanding balance on the 2009 Line of Credit was $166,667 as of December 31, 2013. The District's guarantee is 5.6% of the outstanding balance or $9,333 as of December 31, 2013. This balance was paid off in 2014.

In October 2012, NoaNet opened a $5.0 million Line of Credit with Bank of America to fund capital expenditures. This Note was guaranteed by the Members. The outstanding balance on the 2012 Line of Credit was $5,000,000 as of December 31, 2013. The District's guarantee was 6.78% of the outstanding balance or $339,000 as of December 31, 2013. This balance was paid off in 2014.

As of the end of December 2014 there are no longer any member guarantees on NoaNet's Line of Credit debt. The existing lines of credit were paid off and a new line of credit was established with Wells Fargo without the need for member guarantees.

NOTE 10 - CONTINGENCIES AND LITIGATIONS

Pole Attachment Lawsuit

On December 28, 2007, the District filed a lawsuit in Pacific County Superior Court against three telecom companies (companies) that maintain their facilities as attachments on District owned poles. The suit alleged breach of contract, unjust enrichment and trespass and sought a declaratory judgment and injunctive relief. The lawsuit stems from the telecom company's refusal to enter into an agreement governing their attachment to District owned poles as well as their refusal to pay the District's approved fees for attachment to its poles. The outcome of this lawsuit is not expected to have a material impact on the District's financial position. A trial was held on this matter during October 2010.

In March 2011, the Superior Court ruled in favor of the District, awarding over $600,000 in damages. In September 2011, a hearing was held to review the proposed findings of fact and conclusions of law. In December 2011, the judge signed both the judgment as well as the proposed findings of fact and conclusions of law, without changes, in support of his March decision.

In January 2012, after missing the statutory deadline for filing an appeal of the superior court decision, the companies filed anyway and petitioned the court of appeals to accept their late filing. In February 2012, the court of appeals granted the companies petition to allow late filing. In March 2012, the District filed a petition for discretionary review with the Washington State Supreme Court asking the Court to overturn the court of appeals decision to allow the case to proceed to appeal. In June 2012, a panel of Supreme Court Judges Denied the Districts motion for review.

In January 2014, after receiving extensive briefing from both sides, the court of appeals notified the District that oral arguments would be heard in March. In October 2014, Division I of the Washington State Court of Appeals heard oral arguments from the District and the companies. In October 2014, the Court of Appeals handed down their ruling siding with the District with regard to terms and conditions and pre-2008 rates, but remanding the rate decision back to the superior court. In November 2014, the companies filed a motion for reconsideration with the court of appeals. See Note 14 - Subsequent Events for additional information.

In February of 2015, the court of appeals denied the companies motion for reconsideration and in March the companies filed a petition for review with the Washington Supreme Court. In August 2015, the Washington State Supreme Court denied the companies petitions for review, essentially upholding the court of appeals decision and remanding the ruling on the proper rate formula back to Pacific County Superior Court. As of this writing, the District is preparing for the remand trial which is tentatively set for August 2016.

NOTE 11 – RISK MANGEMENT

PURMS

The District is a member of the Washington Public Utility District's Utilities System Joint Self Insurance Fund (WPUDUS). RCW 48.62 authorizes the governing body of any one or more governmental entities to form or join a pool or organization for joint purchasing of insurance and/or joint self-insurance, and/or joint hiring or contracting for risk management services to the same extent that they may individually purchase the same. A decision to create a pooling agreement was made according to the provisions of RCW 54.16. The Pool was formed on December 31, 1976 when certain Washington State PUDs joined together by signing an Agreement to pool their self-insured losses and jointly purchase insurance and administrative services. Public Utility Risk Management Services (PURMS) provides the aforementioned services to its participating members.

LIABILITY RISK POOL

PURMS provides liability insurance coverage for its members participating in the Liability Risk Pool, and to a limited extent for the benefit of their employees, under an agreement entitled "PURMS Joint Self-Insurance Agreement". The Liability Pool had a self-insured retention (Liability Coverage Limit) of $1,000,000 per occurrence and mandatory participation in a first layer of Excess Liability Insurance in the amount of $35,000,000. The Liability Pool also offers an optional second layer of excess liability insurance in the amount of $25,000,000. The District will be adding this second layer beginning January 2016.

The Liability Pool also offers public officials liability coverage for a subgroup of members of the Liability Pool who chose to participate in the coverage. For 2015, the Public Officials coverage was $35,000,000 in excess of the liability coverage limit. The District is a member of this subgroup.

This pool is financed through assessment of its members. These assessments occur at the beginning of each calendar year and at any time the Liability Pool Balance falls below the designated $3,000,000 Liability Pool Balance by $500,000 or more.

As of December 31, 2015, there were 74 known incidents or unresolved liability claims pending against one or more members or former members of the Liability Pool. The total dollar amount of the risk posed by these claims to such members and to the Liability Pool itself is unknown and can only be estimated. The case reserves set by the administrator for these Claims, as of December 31, 2015, was $257,345. The Liability Pool's actual balance was replenished to the $3,000,000 designated balance via the automatic annual assessment issued in January 2016.

<u>PROPERTY RISK POOL</u>

PURMS provides property insurance coverage for its members participating in the Property Risk Pool in accordance with the terms of the Self Insurance Agreement (SIA). Under the SIA the Property Pool has had a self-insured retention or (Property Coverage Limit) of $250,000 per property loss.

At all times, PURMS also maintains excess property insurance for its members in the Property Pool. For 2015, the amount of the excess property insurance was $200,000,000 with excess coverage attaching at the $250,000 property coverage limit for all property losses except those subject to increased retention levels for certain property risks.

The Property Pool also provides its members with automatic extended property coverage for property losses that exceed the Property Pool's $250,000 property coverage limit if those losses were also subject to increased retentions under the excess property insurance. Under the excess property insurance retentions in effect for 2015, the maximum exposure to the Property Pool from a property loss that exceeded $250,000, and that was subject to an increased retention, was $250,000, less the applicable deductible, or a maximum of $250,000 more than the Property Coverage Limit.

The Property Pool is funded to the amount of its designated Property Pool balance, which in 2015 was $750,000. Of this amount, $250,000 is used to pay claims costs as they are incurred and ongoing Property Pool operating expenses, including program administration. The $250,000 of Operating Funds is replenished by assessments of property pool members. The remaining $500,000 of the Designated Balance is held by the Property Pool to meet regulatory reserve requirements.

The total paid for property claims in 2015 was $562,503, including claims adjustment expenses (but excluding Property Pool Operating Expenses). As of December 31, 2015, there were 14 known property claims pending from the members of the Property Pool. The total dollar amount of the risk posed by these claims to the Property Pool is unknown and can only be estimated. The case reserves set by the administrator for these claims, as of December 31, 2015, was $32,443. The Property Pool's actual balance was replenished to its $750,000 designated balance via the automatic annual assessment issued in January 2016.

HEALTH & WELFARE (H&W) RISK POOL

PURMS provides health and welfare insurance coverage for the employees of each of its members participating in the Health & Welfare (H&W) Risk Pool in accordance with the terms of the Health & Welfare Coverage of the SIA and the terms of each Member's respective Coverage Booklet provided to its Employees.

The H&W Pools operations are financed through assessments of its members under the H&W General Assessment Formula. Each month, each Member of the H&W Pool is assessed for the cost the H&W Pool incurred during the preceding month for such member's employees and for such member's share of Shared H&W Costs which includes administrative expenses, premiums for Stop-Loss Insurance, PPO charges and Shared H&W Claims.

The exposure of each H&W Pool Member to the H&W Claims Costs of its employees is limited by stop-loss points. The first two Stop-Loss Points are established annually by the Excess Stop-Loss Insurance that the H&W Pool acquires and maintains for its Members. These Stop-Loss Points represent the dollar amounts at which the Stop-Loss Insurance attaches and begins paying either the H&W Claim Costs for an individual employee's total medical claims for the year or the H&W Claims Costs of all employees of all members for the year.

For 2015, the H&W Pool Individual Stop-Loss Point was $250,000 per employee and the H&W Pool Aggregate Stop-Loss Point was $17,037,729 for the combined H&W Claims Costs of the employees of all members of the H&W Pool.

In Addition, each H&W Pool member's exposure to the H&W claims costs of its employees is further limited by even lower Stop-Loss Points determined by the H&W Pool for its members. Medical expenses that exceed these Stop-Loss Points become Shared H&W Claims and are paid by all H&W Pool members except the member whose employee's H&W Claim exceeded the applicable Stop-Loss Point. The member Stop-Loss Points are calculated annually under the H&W assessment formula.

The total paid by the H&W Pool for H&W Claims Costs in 2015 was $13,035,969 (including shared H&W claims but excluding H&W pool operating expenses).

OTHER COVERAGE

District Official Bond / Employee Practices

The District also maintains with a commercial carrier, additional coverage in the amount of $250,000 per loss. The policy indemnifies any District official, required by law to give bonds for the faithful performance of their service, against loss through the failure of any employees under the official's supervision to faithfully perform his or her duties as prescribed by law, when such failure results in loss of money or property. The policy also covers employment practices claims.

Unemployment Insurance
The District is self-insured for unemployment compensation, in that it reimburses the State of Washington for actual claims made. Unemployment claims are infrequent; the District recognized no unemployment compensation expense in 2015 or 2014.

NOTE 12 - OTHER POSTEMPLOYMENT BENEFITS (OPEB)

Plan Description
In accordance with collective bargaining agreements, the District provides employer paid post-retirement medical, vision, prescription and dental benefits for qualified retired employees and their eligible dependents. For employees retiring before September 1, 2009 the District contributes the percentage of the annual cost that was paid at the time of their retirement, this percentage ranges from 80% to 100%. For employees retiring after September 1, 2009, the District pays the same percentage of annual cost that it contributes for active employees, currently 95%.

Funding Policy
The District funds its post-retirement health care benefits when the actual health care costs are incurred for retirees and their eligible dependents. The District is currently evaluating the option of pre-funding all or a portion of the actuarial calculated Annual Required Contribution (ARC), but no decision has been made.

Annual OPEB Cost
The District's annual OPEB cost is calculated based upon the ARC of the employer. The ARC is an amount actuarially determined based on the entry age normal method and is determined in accordance with the guidance of GASB Statement No. 45. The ARC represents level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities over a period of thirty years. The District implemented GASB 45 prospectively in 2008. The District's annual required OPEB cost (expense) for 2015 was $1,922,015 and $1,935,030 for 2014.

The following table shows the components for the District's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the District's net OPEB.

Determination of Annual Required Contribution	December 31, 2015	December 31, 2014	December 31, 2013
Normal Cost at year end	$796,298	$796,298	$706,484
Amortization of UAAL	$1,149,831	$1,149,831	$754,732
Annual Required Contribution (ARC)	$1,946,129	$1,946,129	$1,461,216
Determination of Net OPEB Obligation			
Annual Required Contribution	$1,946,129	$1,946,129	$1,461,216
Interest on prior year Net OPEB Obligation	$207,920	$156,865	$121,541
Adjustment to ARC	($232,034)	($167,964)	($121,541)
Annual OPEB Cost	$1,922,015	$1,935,030	$1,461,216
Contributions made	$703,562	$658,650	$578,100
Increase in Net OPEB Obligation	$1,218,453	$1,276,380	$883,116
Net OPEB Obligation – beginning of year	$5,198,011	$3,921,631	$3,038,515
Net OPEB Obligation – end of year	$6,416,464	$5,198,011	$3,921,631

Funded Status and Funding Progress

In 2015, the payment of employee health care benefits for retirees and qualified dependents totaled $703,562. The current year funding resulted in an accrued OPEB Liability of $6,416,464.

In 2014, the payment of employee health care benefits for retirees and qualified dependents totaled $658,650. The current year funding resulted in an accrued OPEB Liability of $5,198,011.

In 2013, the payment of employee health care benefits for retirees and qualified dependents totaled $578,100. 2013’s funding resulted in an accrued OPEB Liability of $3,921,631.

The District’s annual OPEB cost, the percentage of OPEB cost contributed to the plan, and the net OPEB obligation follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of OPEB Cost Contributed	Net OPEB Obligation
12/31/2013	$1,461,216	39.56%	$3,921,631
12/31/2014	$1,935,030	34.04%	$5,198,011
12/31/2015	$1,922,015	36.61%	$6,416,464

The Schedule of Funding Progress for the unfunded actuarial accrued liability (UAAL) is as follows:

	Valuation Dated Jan 1, 2014	Valuation Dated Jan 1, 2011
Actuarial Value of Assets	$0	$0
Actuarial Accrued Liability	$25,813,800	$19,594,003
UAAL	$25,813,800	$19,594,003
Funded Ratio	0%	0%
Covered Payroll	$4,555,486	$3,975,825

The Schedule of Funding Progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities, consistent with the long-term perspective of the calculations. In the January 1, 2014 actuarial valuation, the Entry Age Normal actuarial cost method was used. The actuarial assumptions used included a 4.00% discount rate, which is based upon the long-term investment yield on the investments that are expected to be used to finance the payment of benefits. The 2014 valuation used a projected payroll increase of 3.75% per year and a medical inflation rate of 6.0% grading down to 4.8%.

The UAAL is being amortized on a closed basis at the assumed discount rate. The remaining amortization period at January 1, 2014 was 27 years.

NOTE 13 - POWER SUPPLY

BPA Power Contract

The District is a preference customer of the, Bonneville Power Administration (BPA) which operates under the authority of the U.S. Department of Energy. The BPA supplies the primary source of the District's power under a contract that was approved by the District’s Board of Commissioners (Resolution No. 1274) at its November 18, 2008 meeting. Resolution No.1274 authorized the execution of a Slice/Block Power Sales Agreement with the BPA commencing on October 1, 2011 and expiring on September 30, 2028.

These agreements incorporate provisions of the Pacific Northwest Electric Power Planning and Conservation Act of 1980 (Public Law 96-501) and the Bonneville Project Act of 1937 such as preference and priority in the distribution and marketing of BPA’s federal power to publicly owned preference customers, such as the District. The contract provides federal power in amounts based on the District's annual Net Requirements in the form of two products: Slice and Block.

The Slice product provides for the combined sale of power services to the District based on the actual generation shape of the Federal Columbia River Power System (FCRPS). As a Slice purchaser, the District accepts the risk of fluctuations in the actual output of the FCRPS and accepts responsibility for managing its percentage share of the output to serve load. There is no guarantee that the amount of the Slice output, combined with Firm Requirements Power made available under Block are sufficient to meet the Districts native load at any given time. As part of the BPA agreement, the District agrees to meet its load with its own resources and/or purchases beyond what BPA supplies.

The Block product provides power in pre-agreed upon flat, but shaped monthly amounts. The District's monthly Block power deliveries ranged from 12MW to 23MW. The rate for Block power is the lowest applicable Priority Firm Rate made available to BPA's preference customers. The Slice product provides the District with a 0.28252% share of the output of the FCRPS output made available to Slice customers.

The currently applicable base-rate for Slice purchases is $1,961,053 per month for each percent of Slice, with the adjusted base rate subject to an annual true up by BPA based upon updated actual costs allocated to the Slice System. Technical Operating Procedures have been established to provide Slice purchasers with the ability to calculate, schedule, and account for their share of Slice Output on an hourly basis. This product does not include transmission services. Moreover, by its nature, there is a greater degree of potential for exposure – and benefit – depending upon snow-pack amount and timing of runoff and other conditions that affect water, and therefore hydroelectric system output.

BPA reserves the right to implement a Load Based Cost Recovery Adjustment Charge (LBCRAC). The current LBCRAC is 0%.

<u>BPA Transmission Services</u>
The District traditionally purchased bundled electric power and transmission services from BPA under the District's power purchase contract. However, in response to changes in Federal Energy Regulatory Commission regulations in the late 1990s, BPA unbundled their electric power and transmission services, and required that transmission services be purchased separately.

As a result of BPA unbundling its Power Services from Transmission Services, the District entered into a Service Agreement for Network Integration Transmission Service with BPA on June 8, 2001. This agreement is set to expire on October 1, 2031. The agreement specifies that the transmission is used to serve the District's Net Requirements Load.

As a result of execution of the new Slice/Block Power Sales agreement, the District also executed a Point to Point Transmission (PTP) Service Agreement with BPA on September 8, 2011. The PTP agreement allows the District to move power and gives greater flexibility in transporting electricity.

The Energy Authority

The Energy Authority (TEA) provides professional power supply management services including wholesale market purchases and sales of electricity on behalf of the District. TEA also provides power scheduling services to the District.

Power Market Risk Management Policies and Procedures

In early 2010 the District commenced with a comprehensive assessment of its risk profile, and the development of policies and procedures for risk management and trading operations. The results of this effort, completed in September 2011, are detailed guidelines for considering and/or engaging in any Power Trading Agreements. The District's Risk Management Committee, with oversight and review by the Board of Commissioners, actively manages financial risk. The District will periodically update the risk management policy to incorporate improved procedures and practices.

Total power cost for the years ending December 31, 2015 and 2014 was $10,413,835 and $9,812,051, respectively. Power transmission cost for the years ending December 31, 2015 and 2014 was $1,376,355 and $1,266,961, respectively.

NOTE 14 – Restatement of Prior Year

With implementation of GASB Statements No. 68 and 71, the District restated its 2014 financial statements and reclassified certain 2014 account balances to conform to its 2015 presentation. The accounting policies of the District conform to generally accepted accounting principles applicable to governmental units. The GASB is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The GASB Board's stated goals for the new standards are to improve decision-usefulness information, support users' ability to assess accountability and inter-period equity, and to create additional transparency.

Change in Accounting Principle

In accordance with GASB Statement Nos. 68 and 71, the District now recognizes liabilities, deferred outflows of resources, deferred inflows of resources, and expenses relating to future pension liabilities.

The table below shows the changes in balances due to the restatement:

	2014 Restated	2014 Audited	Increase/(Decrease)
Statement of Net Position			
Pension Deferred Outflow	$270,054	-	($270,054)
Net Pension Liability	3,050,745	-	3,050,745
Pension Deferred Inflow	1,353,095	-	1,353,095
Unrestricted (Net Position)	(467,800)	3,665,986	(4,133,786)
Statement of Revenues, Expenses, and Changes in Net Position			
Administrative & General Expense	5,634,074	5,596,218	37,856
GASB 68 Restate	4,095,930	-	4,095,930
Statement of Cash Flows			
Operating Income	(1,758,205)	(1,720,349)	(37,856)
GASB 68 Pension Expense	37,856	-	37,856

In checking the Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities, the District discovered redundant lines and eliminated them from the reconciliation. The table below shows the changes:

	2014 Restated	2014 Audited	Increase/(Decrease)
Statement of Cash Flows			
Prepaids and Deposits	($75,205)	($63,517)	($11,688)
Deferred Derivative Outflow	-	(11,688)	11,688
Deferred Derivative Inflow	-	(61,979)	61,979
Other Credits	-	61,979	(61,979)

In 2015, the District corrected it’s method of calculating its net investment in capital assets to account for unspent bond proceeds. This required restatement of the 2014 balances reported in the “net investment in capital assets” and the “restricted for construction” components of net position.

	2014 Restated	2014 Audited	Increase/(Decrease)
Statement of Net Assets			
Net Investment in Capital Assets	$48,522,395	$33,279,821	$15,242,574
Restricted for Construction	2,716,842	17,959,416	(15,242,574)

Reclassification

In 2015, the District reclassified the 2014 presentation of unamortized premium and discount to include it with the face amount of the revenue bonds debt it is associated with. With this reclassification there was no change in the total liabilities presented.

Required Supplementary Information

Other Postemployment Benefits
For the Year Ended December 31, 2015

Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (AAL)* (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b-a)/c]
1/1/2008	-	$11,747,549	$11,747,549	0%	N/A	N/A
12/31/2008	-	$11,747,549	$11,747,549	0%	$3,602,534	326.1%
12/31/2009	-	$11,747,549	$11,747,549	0%	$3,794,016	309.6%
12/31/2010	-	$11,747,549	$11,747,549	0%	$3,761,334	312.3%
12/31/2011	-	$19,594,003	$19,594,003	0%	$3,975,825	492.8%
12/31/2012	-	$19,594,003	$19,594,003	0%	$3,983,723	491.9%
12/31/2013	-	$19,594,003	$19,594,003	0%	$4,296,846	456.0%
12/31/2014	-	$25,813,800	$25,813,800	0%	$4,555,486	566.0%
12/31/2015	-	$25,813,800	$25,813,800	0%	$4,791,219	538.8%

**based on Entry Age actuarial cost method*
N/A Indicates data not available
Source: Milliman, Inc.

Fiscal Year Ending	Total Employer Contributions	Annual Required Contribution (ARC)	Percentage of ARC Contributed
12/31/2008	$430,739	$774,549	55.6%
12/31/2009	$425,347	$774,549	54.9%
12/31/2010	$415,061	$774,549	53.6%
12/31/2011	$447,037	$1,461,216	30.6%
12/31/2012	$508,594	$1,461,216	34.8%
12/31/2013	$578,100	$1,461,216	39.6%
12/31/2014	$671,188	$1,946,129	34.0%
12/31/2015	$703,562	$1,946,129	36.2%

Schedule of Proportionate Share of the Net Pension Liability

PERS Plan 1
As of June 30, 2015
Last 10 Fiscal Years

	2015	2014
Employer's proportion of the net pension liability (asset)	0.040220%	0.039931%
Employer's proportionate share of the net pension liability	$2,103,880	$2,011,543
Employer's covered employee payroll	-	-
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	-	-
Plan fiduciary net position as a percentage of the total pension liability (DRS PEFI)	59%	61%

Notes to Schedule:
There are no factors at year-end that significantly affect trends in the amounts reported above.
The ten year information will be provided as it is available.

Schedule of Proportionate Share of the Net Pension Liability

PERS Plan 2/3
As of June 30, 2015
Last 10 Fiscal Years*

	2015	2014
Employer's proportion of the net pension liability (asset)	0.040220%	0.039931%
Employer's proportionate share of the net pension liability	$1,856,203	$1,039,202
Employer's covered employee payroll	$4,791,219	$4,555,486
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	39%	23%
Plan fiduciary net position as a percentage of the total pension liability (DRS PEFI)	89%	93%

Notes to Schedule:
There are no factors at year-end that significantly affect trends in the amounts reported above.
*The ten year information will be provided as it is available.

Schedule of Employer Contributions

PERS Plan 1
As of December 31, 2015
Last 10 Fiscal Years*

	2015	2014
Statutorily required contributions	-	-
Contributions in relation to Statutorily required contributions	-	-
Contribution deficiency (excess)	-	-
Covered employer payroll	-	-
Contributions as a percentage of covered employee payroll	-	-

Notes to Schedule:
There are no factors at year-end that significantly affect trends in the amounts reported above.
*The ten year information will be provided as it is available.

Schedule of Employer Contributions

PERS Plan 2/3
As of December 31, 2015
Last 10 Fiscal Years*

	2015	2014
Statutorily required contributions	$490,551	$419,560
Contributions in relation to Statutorily required contributions	($490,551)	($419,560)
Contribution deficiency (excess)	-	-
Covered employer payroll	$4,791,219	$4,555,486
Contributions as a percentage of covered employee payroll	10.24%	9.21%

Notes to Schedule:
There are no factors at year-end that significantly affect trends in the amounts reported above.
*The ten year information will be provided as it is available.

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.

Contact information for the State Auditor's Office	
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