



**Office of the Washington State Auditor**  
**Pat McCarthy**

**Financial Statements Audit Report**  
**Public Utility District No. 1 of Franklin**  
**County**

**For the period January 1, 2015 through December 31, 2016**

**Published July 24, 2017**

**Report No. 1019409**





**Office of the Washington State Auditor**  
**Pat McCarthy**

July 24, 2017

Board of Commissioners  
Public Utility District No. 1 of Franklin County  
Pasco, Washington

**Report on Financial Statements**

Please find attached our report on Public Utility District No. 1 of Franklin County's financial statements.

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

Sincerely,

Pat McCarthy  
State Auditor  
Olympia, WA

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**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL  
OVER FINANCIAL REPORTING AND ON COMPLIANCE AND  
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL  
STATEMENTS PERFORMED IN ACCORDANCE WITH  
GOVERNMENT AUDITING STANDARDS**

**Public Utility District No. 1 of Franklin County  
January 1, 2015 through December 31, 2016**

Board of Commissioners  
Public Utility District No. 1 of Franklin County  
Pasco, 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. 1 of Franklin County, Washington, as of and for the years ended December 31, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated June 27, 2017. As discussed in Note 1 to the financial statements, during the year ended December 31, 2016, the District implemented Governmental Accounting Standards Board Statement No. 72, *Fair Value Measurement and Application* and Statement No. 79, *Certain External Investment Pools and Pool Participants*.

**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.

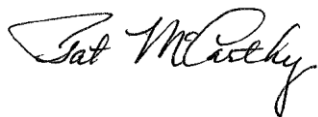
## COMPLIANCE AND OTHER MATTERS

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.



Pat McCarthy

State Auditor

Olympia, WA

June 27, 2017

# INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

## **Public Utility District No. 1 of Franklin County January 1, 2015 through December 31, 2016**

Board of Commissioners  
Public Utility District No. 1 of Franklin County  
Pasco, Washington

### **REPORT ON THE FINANCIAL STATEMENTS**

We have audited the accompanying financial statements of Public Utility District No. 1 of Franklin County, Washington, as of and for the years ended December 31, 2016 and 2015, 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 opinions 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 opinions.

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Public Utility District No. 1 of Franklin County, as of December 31, 2016 and 2015, 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 2016, the District adopted new accounting guidance, Governmental Accounting Standards Board Statement No. 72, *Fair Value Measurement and Application* and Statement No. 79, *Certain External Investment Pools and Pool Participants*. 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 and pension plan information on pages 41 through 42 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 June 27, 2017 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.

A handwritten signature in black ink, reading "Pat McCarthy". The signature is fluid and cursive, with the first name "Pat" and last name "McCarthy" clearly distinguishable.

Pat McCarthy

State Auditor

Olympia, WA

June 27, 2017



## **FINANCIAL SECTION**

### **Public Utility District No. 1 of Franklin County January 1, 2015 through December 31, 2016**

#### **REQUIRED SUPPLEMENTARY INFORMATION**

Management's Discussion and Analysis – 2016 and 2015

#### **BASIC FINANCIAL STATEMENTS**

Statement of Net Position – 2016 and 2015

Statement of Revenues, Expenses and Changes in Net Position – 2016 and 2015

Statement of Cash Flows – 2016 and 2015

Notes to Financial Statements – 2016 and 2015

#### **REQUIRED SUPPLEMENTARY INFORMATION**

Schedules of Proportionate Share of the Net Pension Liability – 2016

Schedules of Employer Contributions – 2016

## MANAGEMENT'S DISCUSSION AND ANALYSIS

This section provides an overview and analysis of key data presented in the basic financial statements for the years ended December 31, 2016 and 2015, with additional comparative data for 2014. Information within this section should be used in conjunction with the basic financial statements and accompanying notes.

### Overview of the Financial Statements

Public Utility District No. 1 of Franklin County (District) accounts for its financial activities within a single proprietary fund. The District's financial activities are comprised of the purchase, generation, transmission, distribution and sale of electric energy, as well as the sale of wholesale telecommunication services.

In accordance with requirements set forth by the Governmental Accounting Standards Board (GASB), 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 in comparative format for the years ended December 31, 2016 and 2015 are comprised of:

**Comparative Statement of Net Position:** The District presents its statement of net position using the balance sheet format. The Statement reflects the assets, deferred outflows, liabilities, deferred inflows and net position (equity) of the District at year-end. The net position section of the Statement is separated into three categories: net investment in capital assets; restricted net position; and unrestricted net position. In 2015, the District implemented *GASB Statement No. 68 - Accounting and Financial Reporting for Pensions* and *GASB Statement No. 71 - Pension Transition for Contributions Made Subsequent to the Measurement Date* – an Amendment of GASB Statement No. 68, which resulted in an adjustment to net position of \$7.8 million in 2014.

**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. Certain amounts for 2014 were restated to reflect the adoption of GASB Statement No. 68 and GASB Statement No. 71.

**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.

**Restatement of 2014:** The District has restated the net position presented within 2014 financial statements to conform to accounting and reporting requirements as prescribed by GASB Statement No. 68 and GASB Statement No. 71, which the District implemented for 2015. The primary objective of GASB Statement No. 68 is to improve accounting and financial reporting by state and local governments for pensions. Adoption of this statement resulted in an adjustment to net position of \$7.8 million in 2014 as shown in the comparative information below.

**Statement of Net Position (in thousands)**

	2016	2015	2015 to 2016 Change	2014 as restated
Current and Other Assets	\$55,841	\$59,839	-6.68%	\$63,564
Capital Assets and Work in Progress	228,452	215,298	6.11%	205,341
Accumulated Depreciation	(91,026)	(84,280)	8.00%	(77,951)
<b>Total Assets</b>	<b>193,267</b>	<b>190,857</b>	1.26%	<b>190,954</b>
Deferred Outflows of Resources	2,874	2,595	10.75%	1,707
<b>Total Assets and Deferred Outflows</b>	<b>196,141</b>	<b>193,452</b>	1.39%	<b>192,661</b>
Current and Other Liabilities	16,197	17,362	-6.71%	15,306
Long-Term Liabilities	72,235	68,685	5.17%	70,361
<b>Total Liabilities</b>	<b>88,432</b>	<b>86,047</b>	2.77%	<b>85,667</b>
Deferred Inflows of Resources	1,665	3,090	-46.12%	3,630
<b>Total Liabilities and Deferred Inflows</b>	<b>90,097</b>	<b>89,137</b>	1.08%	<b>89,297</b>
Net Investment in Capital Assets	77,791	70,465	10.40%	70,055
Restricted for Debt Service	3,915	3,142	0.00%	3,142
Unrestricted	24,338	30,708	-20.74%	30,167
<b>Total Net Position</b>	<b>\$106,044</b>	<b>\$104,315</b>	1.66%	<b>\$103,364</b>

**Statement of Revenues, Expenses and Changes in Net Position (in thousands)**

	2016	2015	2015 to 2016 Change	2014 as restated
Operating Revenues:				
Retail Energy Sales	\$73,895	\$75,121	-1.63%	\$74,002
Sales for Resale	7,970	9,257	-13.90%	12,052
Other	1,976	2,022	-2.27%	1,634
Total Operating Revenues	83,841	86,400	-2.96%	87,688
Nonoperating Revenues	246	184	33.70%	277
<b>Total Revenues</b>	<b>84,087</b>	<b>86,584</b>	<b>-2.88%</b>	<b>87,965</b>
Operating Expenses:				
Power Supply	57,475	58,300	-1.42%	58,574
Operations, Maintenance & Administrative	13,214	12,601	4.86%	12,641
Taxes & Depreciation	11,718	11,635	0.71%	11,251
Total Operating Expenses	82,407	82,536	-0.16%	82,466
Nonoperating Expenses	2,807	2,885	-2.70%	3,023
<b>Total Expenses</b>	<b>85,214</b>	<b>85,421</b>	<b>-0.24%</b>	<b>85,489</b>
Income (Loss) Before Capital Contributions	(1,127)	1,163	-196.90%	2,476
Capital Contributions	2,856	2,788	2.44%	3,119
Extraordinary Loss		(3,000)		
<b>Change in Net Position</b>	<b>1,729</b>	<b>951</b>	<b>81.81%</b>	<b>5,595</b>
Beginning Net Position	104,315	103,364	0.92%	105,611
Cumulative Effect of Restatement				(\$7,842)
<b>Ending Net Position</b>	<b>\$106,044</b>	<b>\$104,315</b>	1.66%	<b>\$103,364</b>

## Financial Analysis

During 2016, the District maintained a strong overall financial position, with total Net Position increasing 1.66% over 2015. The following narrative is an analysis of the change in net position by major components of income, with a primary focus on changes between 2016 and 2015.

### Operating Revenues

#### 2015 to 2016:

Seasonally mild weather across the region for most of 2016 impacted the District's sales of kilowatt hours to retail energy customers. Retail energy consumption was consistently below expected throughout the majority of the year, with a short period very high consumption at the end of the year due to record cold temperatures and snowfall. This is reflected in the overall \$1.2 million (1.63%) decrease in Retail Energy Sales from 2015 to 2016.

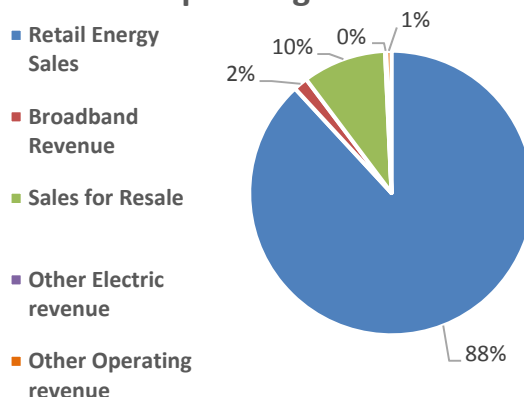
Revenues from wholesale energy (Sales for Resale) decreased 2.27% in 2016. While the average wholesale power prices received for sales of excess megawatt hours increased from 2015, the District sold approximately 19% fewer megawatt hours.

#### 2014 to 2015:

The District experienced a \$1.1 million (1.5%) increase in Retail Energy Sales in 2015. While consumption of kilowatt hours increased slightly, the increase in revenue is largely due to a cumulative increase in the rate charged for electric service. This increase was structured to increase the basic charge for receiving electric service and decrease the amount charged per kilowatt hour of energy usage. Increasing the basic charge positions the District to recover the full cost of providing the infrastructure necessary for a customer to receive electric service. The rate change was approved by the Board of Commissioners on August 25, 2015 and effective September 1, 2015.

Sales for Resale decreased by 23% in 2015 as the result of significantly lower wholesale power prices than the District realized in 2014, average wholesale power prices were \$22 per megawatt hour in 2015 versus \$35 in 2014.

#### 2016 Operating Revenues

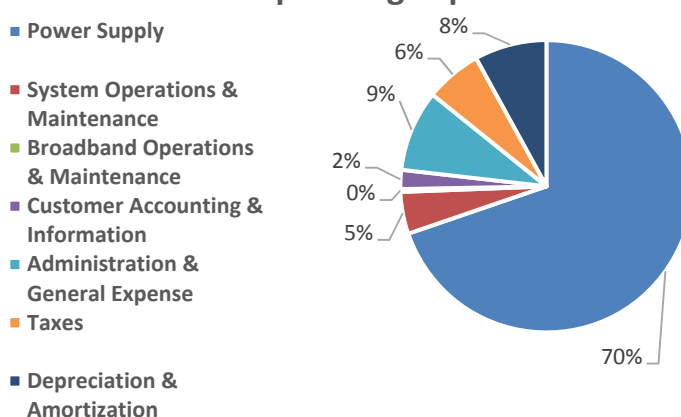


### Operating Expenses

#### 2015 to 2016:

The District experienced a small decrease of approximately \$127,000 (.16%) in Total Operating Expenses in 2016. Power supply and tax expense decreased approximately \$954,000 due to the reduced kilowatt hour sales to retail electric customers discussed previously. This decrease was offset by increases in Operations, Maintenance & Administrative of \$484,000, which is in part due to a reduction of pension expense of approximately \$300,000 experienced in 2015 with the implementation of GASB

#### 2016 Operating Expenses



Statement No. 68. An adjustment of this magnitude was not recorded for 2016.

#### **2014 to 2015:**

Total operating expenses remained steady in 2015, increasing just \$69,914 over 2014. An increase to Depreciation and Amortization of approximately \$362,000 due to addition of capital assets was offset by decreases in Power Supply Expense, Broadband Operations & Maintenance, and Customer Accounting & Information. Power Supply Expense decreased approximately (\$274,000) due to a (\$1.2 million) decrease in power purchased on the open market, offset by increases in the cost of power provided by Bonneville Power Administration of \$1.0 million and purchases of natural gas hedging instruments. The decrease in market purchases was a result of significantly lower wholesale power prices than in 2014.

### **Other Income & Expense**

During 2015, the District adjusted the value of the Pasco Combustion Turbine plant to approximate market value based on markets for similar assets. This resulted in an extraordinary loss to the District of \$3 million. The plant is reported as an Asset Held for Sale on the Statement of Net Position. Further information regarding the revaluation of the Pasco Combustion Turbine plant is presented in Note 4 of the financial statements.

### **Capital Contributions**

Capital Contributions increased approximately \$68,000 in 2016, as the District continued to add new customers in both the residential and commercial business sectors. The District realized approximately \$100,000 in revenues related to serving new customers as well system upgrades for current customers, an increase of 3.6% over 2015. This was offset by a decrease in state grant revenue of \$31,735.

Capital Contributions decreased approximately \$332,000 in 2015 as the District recorded just \$31,735 in state grant revenue versus \$1.2 million in 2014. Contributions related to serving new customers, as well as system upgrades for current customers, increased 25% in 2015 as a result of continued growth within the District's service territory.

### **Summary of Financial Position**

The District's overall financial position improved in 2016, with an increase in net position of almost \$2 million.

District management monitors the effectiveness of its financial operations by measuring results against the financial policy adopted by the District's governing body. This policy directs District management to develop financial plans that position the District for current and future years while being fiscally responsible to the District's ratepayers. The financial policy consists of three key financial performance metrics – minimum cash/investment reserve balance (sufficient to fund 10% of gross power supply costs, 25% of other operating costs, and 25% of planned capital spending); minimum debt service coverage ratio of 1.6; maximum debt/asset ratio of 40%; and funding of a Rate Stabilization Fund at a level sufficient to meet the fiscal needs of the District. The District's performance over the past three years achieved these goals:

	<b>2016 Financial Policy Targets</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
Unrestricted Cash & Investments (in millions)	\$14.3	\$21.5	\$27.7	\$24.0
Minimum Debt Service Coverage	1.6	1.98	2.29	2.53
Maximum Debt/Asset Ratio	40%	33%	32%	34%
Rate Stabilization Fund	\$5.9*	\$5.9	\$5.9	\$5.9

\*Funding level currently established, to be reviewed periodically by the District's governing body.

## Capital Asset and Long-Term Debt Activity

### Capital Assets (in thousands)

	2016	2015	Increase (Decrease)	% Change
Land	\$893	\$893	\$0	0.0%
Electric Plant in Service	223,836	206,943	16,894	8.2%
Construction Work in Progress	3,723	7,462	(3,741)	-50.1%
Total	\$228,452	\$215,298	\$13,153	6.1%

At the end of 2016, the District had \$228 million invested in capital assets. The District purchased a mobile substation and replaced a power transformer in the Franklin Substation during 2016. These projects alone encompassed 18% of the increase in plant placed in service, or approximately \$3 million. The total increase in the District's investment in capital assets for the current year was \$13.1 million, or 6.1%.

Net Capital Asset activity included an increase of approximately \$9.9 million or 4.8% in 2015. Major plant additions during the year included closure of a project to make major improvements to the District's Taylor Flats substation. This project comprised approximately 23% of capital additions for 2015.

More detailed information about the District's capital assets is presented in Note 4 to the financial statements.

### Long Term Debt (in thousands)

	2016	2015	Increase (Decrease)	% Change
Revenue Bonds	\$64,246	\$61,521	\$2,725	4.4%

The District issued a total of \$32.2 million in revenue and refunding bonds in 2016 to fund capital improvements and refund various outstanding bond issues. This issue refunded all but the 2017 maturities of the outstanding 2007 series revenue and refunding bonds, and resulted in a net present value savings to the District of \$2.4 million.

Debt service payments totaled \$5.7 million annually for 2016, 2015 and 2014.

More detailed information regarding the District's long term liabilities is presented in Note 5 to the financial statements.

### Bond Ratings

In 2016, the District affirmed its credit ratings with Standard & Poor's (A) and Moody's Global Ratings Scale (A1).

**STATEMENT OF NET POSITION**  
As of December 31, 2016 and 2015

<b>ASSETS AND DEFERRED OUTFLOWS OF RESOURCES</b>	<b>2016</b>	<b>2015</b>
<b>ASSETS</b>		
Current Assets		
Cash (Note 2)	\$5,235,070	\$5,332,195
Investments (Note 2)		
Restricted Construction Account	3,276,911	
Unrestricted	16,279,039	22,319,797
Accounts Receivable	10,184,417	10,285,139
Inventories	3,704,492	3,524,123
Prepayments	91,676	103,801
Derivative Asset (Note 3)	1,249,771	2,021,766
Asset Held for Sale (Note 4)	5,447,004	5,447,004
Other Current Assets	7,551	13,280
<b>Total Current Assets</b>	<b>45,475,931</b>	<b>49,047,105</b>
Noncurrent Assets		
Other Receivables (Note 1)	6,450,000	7,649,517
Restricted Debt Service Reserve Fund	3,914,649	3,142,483
Utility Plant (Note 4)		
Land	893,104	893,104
Electric Plant in Service	223,836,397	206,942,884
Construction Work in Progress	3,722,684	7,462,430
Accumulated Depreciation	(91,025,824)	(84,279,621)
Net Utility Plant	137,426,361	131,018,797
<b>Total Noncurrent Assets</b>	<b>147,791,010</b>	<b>141,810,797</b>
<b>TOTAL ASSETS</b>	<b>193,266,941</b>	<b>190,857,902</b>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>		
Accumulated decrease in fair value of hedging derivatives	970,795	1,199,361
Deferred loss on refunding	477,162	565,021
Deferred Pension Outflows (Note 6)	1,425,779	830,638
<b>Total Deferred Outflows of Resources</b>	<b>2,873,736</b>	<b>2,595,020</b>
<b>TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES</b>	<b>\$196,140,677</b>	<b>\$193,452,922</b>
<b>LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION</b>		
<b>LIABILITIES</b>		
Current Liabilities		
Accounts Payable	\$6,264,087	\$7,625,562
Customer Deposits	1,413,965	1,387,813
Accrued Taxes Payable	1,849,489	1,915,933
Accrued Interest Payable	753,059	948,323
Other Accrued Liabilities	1,745,611	1,420,481
Revenue Bonds, Current Portion	3,200,000	2,865,000
Derivative Liability (Note 3)	970,795	1,199,361
<b>Total Current Liabilities</b>	<b>16,197,006</b>	<b>17,362,473</b>
Noncurrent Liabilities		
Outstanding Revenue Bonds (Note 5)	61,045,939	58,655,822
Net Pension Liability (Note 6)	8,573,908	7,158,356
Other Credits & Liabilities	2,614,969	2,870,446
<b>Total Noncurrent Liabilities</b>	<b>72,234,816</b>	<b>68,684,624</b>
<b>TOTAL LIABILITIES</b>	<b>88,431,822</b>	<b>86,047,097</b>
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Accumulated increase in fair value of hedging derivatives	1,249,771	2,021,766
Deferred Pension Inflow (Note 6)	157,778	1,068,151
Deferred Gain on Refunding (Note 5)	257,938	
<b>Total Deferred Inflows of Resources</b>	<b>1,665,487</b>	<b>3,089,917</b>
<b>NET POSITION</b>		
Net Investment in Capital Assets	77,790,267	70,465,479
Restricted for Debt Service	3,914,649	3,142,483
Unrestricted	24,338,452	30,707,946
<b>TOTAL NET POSITION</b>	<b>106,043,368</b>	<b>104,315,908</b>
<b>TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION</b>	<b>\$196,140,677</b>	<b>\$193,452,922</b>

The accompanying notes are an integral part of this statement.

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**  
**For the Years Ended December 31, 2016 and 2015**

	2016	2015
<b>OPERATING REVENUES</b>		
Retail Energy Sales (Note 1)	\$73,894,581	\$75,121,236
Broadband Revenue	1,358,933	1,457,290
Sales for Resale	7,970,459	9,256,768
Other Electric revenue	132,478	68,229
Other Operating revenue	484,693	496,287
<b>TOTAL OPERATING REVENUES</b>	<b>83,841,144</b>	<b>86,399,810</b>
<b>OPERATING EXPENSES</b>		
Power Supply (Note 9)	57,475,326	58,299,865
System Operations & Maintenance	3,819,269	3,680,766
Broadband Operations & Maintenance	258,317	283,743
Customer Accounting & Information	1,747,416	1,757,472
Administration & General Expense	7,390,042	6,878,866
Taxes	5,138,588	5,268,784
Depreciation & Amortization of Intangible Assets	6,579,684	6,366,029
<b>TOTAL OPERATING EXPENSES</b>	<b>82,408,642</b>	<b>82,535,525</b>
<b>OPERATING INCOME</b>	<b>1,432,502</b>	<b>3,864,285</b>
<b>NONOPERATING REVENUES &amp; EXPENSES</b>		
Interest Income	123,991	76,330
Bond Interest, Debt Premium/Discount Amortization and Issuance Costs	(2,806,788)	(2,884,549)
Other Nonoperating Revenue (Expense)	121,967	107,782
<b>TOTAL NONOPERATING REVENUES &amp; EXPENSES</b>	<b>(2,560,830)</b>	<b>(2,700,437)</b>
<b>INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS AND EXTRAORDINARY LOSS</b>	<b>(1,128,328)</b>	<b>1,163,848</b>
<b>CAPITAL CONTRIBUTIONS</b>	<b>2,855,788</b>	<b>2,787,707</b>
<b>EXTRAORDINARY GAIN (LOSS) (Note 4)</b>		<b>(3,000,000)</b>
<b>CHANGE IN NET POSITION</b>	<b>1,727,460</b>	<b>951,555</b>
<b>NET POSITION, BEGINNING OF YEAR</b>	<b>104,315,908</b>	<b>103,364,353</b>
<b>NET POSITION, END OF YEAR</b>	<b>\$106,043,368</b>	<b>\$104,315,908</b>

*The accompanying notes are an integral part of this statement.*



**STATEMENT OF CASH FLOWS**  
For the Years Ended December 31, 2016 and 2015

	2016	2015 as restated
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Cash received from customers	\$88,965,237	\$89,256,842
Cash paid to suppliers and counterparties	(67,517,199)	(63,303,650)
Cash paid to employees	(8,729,489)	(8,581,910)
Taxes Paid	(4,729,852)	(4,645,371)
Other receipts	262,027	59,834
<b>Net cash provided (used) by operating activities</b>	<b>8,250,724</b>	<b>12,785,745</b>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Acquisition and construction of capital assets	(12,730,607)	(10,199,453)
Interest paid on long-term debt	(2,844,970)	(2,972,850)
Principal paid on long-term debt	(2,865,000)	(2,740,000)
Proceeds from sale of bonds	5,006,665	-
Contributions in aid of construction	2,189,009	3,326,562
Proceeds from disposal of plant	29,990	143,332
<b>Net cash provided (used) by capital and related financing activities</b>	<b>(11,214,913)</b>	<b>(12,442,409)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Investment purchases	(12,005,421)	(8,299,421)
Investment sales and maturities	14,872,485	7,800,000
<b>Net cash provided (used) by investing activities</b>	<b>2,867,064</b>	<b>(499,421)</b>
<b>Net increase (decrease) in cash</b>	<b>(97,125)</b>	<b>(156,085)</b>
<b>Cash balance, beginning of year</b>	<b>5,332,195</b>	<b>5,488,280</b>
<b>Cash balance, end of year</b>	<b>\$5,235,070</b>	<b>\$5,332,195</b>
<b>RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Operating Income	\$1,432,502	\$3,864,285
Adjustments to reconcile operating income to net cash provided (used) by operating activities		
Depreciation and amortization	6,579,684	6,366,029
Gain (Loss) on foreign currency transactions	-	(8,212)
Miscellaneous other revenue and receipts	1,147,478	939,283
Miscellaneous other disbursements and expenses	(114,836)	(1,073,818)
(Increase) decrease in accounts receivable (Net)	700,239	1,446,685
(Increase) decrease in plant supplies	(180,371)	(207,459)
(Increase) decrease prepaid expenses	12,125	2,314
(Increase) decrease in deferred derivative outflow	228,566	(515,453)
(Increase) decrease in other assets	777,725	(729,455)
(Decrease) increase in payables	(1,455,310)	1,381,258
(Decrease) increase in deferred derivative inflow	(771,995)	796,342
(Decrease) increase in other credits	(105,083)	523,946
<b>Net cash provided by operating activities</b>	<b>\$8,250,724</b>	<b>\$12,785,745</b>

**NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES**

During 2016 and 2015, the District received \$581,435 and \$549,270, respectively, in non-cash capital contributions.

During 2016 and 2015, the District received \$104,885 and \$46,429, respectively, in earnings on invested funds.

During 2016, the District issued \$32,175,000 in Revenue and Refunding bonds and retired various outstanding bond issues (see Note 5).

*The accompanying notes are an integral part of this statement.*

# NOTES TO THE FINANCIAL STATEMENTS

DECEMBER 31, 2016 AND 2015

## NOTE 1 - SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

Public Utility District No. 1 of Franklin County (the District) was established in 1938 and purchases, generates, transmits, distributes and sells electric energy. In addition, the District is authorized under state law to provide wholesale telecommunications services. The District's service area is approximately 435 square miles in Franklin County, and includes approximately 80 percent of the County's population. The District's properties include 20 substations, 1,058 miles of transmission and distribution lines, and other buildings, equipment, and related facilities. The District has 102 employees and serves 29,391 active accounts. The District has revenues in excess of \$83 million and total assets of over \$196 million. An elected three-member Board of Commissioners administers the District.

### A. Basis of Accounting and Presentation

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 accounting policies conform to generally accepted accounting principles as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The District has applied all applicable GASB pronouncements including GASB Statement No. 68 – *Accounting and Financial Reporting for Pensions* and GASB Statement No. 71 - *Pension Transition for Contributions made Subsequent to the Measurement Date*, and in 2016, GASB No. 72 – *Fair Value Measurement and Application*, GASB No. 76- *Hierarchy of Generally Accepted Accounting Principles*, and GASB No. 79 – *Certain External Investment Pools and Pool Participants*. The following is a summary of the most significant policies:

### B. Cash and Cash Equivalents

For purposes of the statement of cash flows, cash includes both restricted and unrestricted cash balances. Short-term highly liquid investments are not considered to be cash equivalents (see Note 2). The Rate Stabilization Fund was established in 2009 with a transfer of \$5.9 million. No transfers were made to or from the Rate Stabilization Fund in 2016 or 2015.

### C. Restricted Funds

In accordance with bond resolutions, related agreements and laws, separate restricted accounts have been established. The assets held in these funds are restricted for specific uses including debt service, and are classified as current or non-current assets as appropriate. As of October 2016, the balance of the Rural Economic Development Fund was dissolved and \$262,026.52 was transferred into restricted funds to be used to fund conservation projects in accordance with state law.

### D. Investments

Refer to Note 2 – Deposits and Investments.

### E. Accounts Receivable

The District uses the percentage-of-sales method to record amounts estimated to be uncollectible based on the prior year's write offs. Uncollected accounts over 60 days, except those with special arrangements, are approved monthly for write off by the Board of Commissioners.

### F. Inventories

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

#### G. Derivative Instruments

Refer to Note 3 – Derivative Instruments.

#### H. Other Receivables

Other receivables consist of the Rural Economic Development Fund (REDF) which was created in 2000 pursuant to RCW 82.16.0491. Through 2010, the District contributed \$50,000 per year since inception. Each contribution was offset by a \$25,000 public utility tax credit in each of those years. In 2009, the District appointed Benton Franklin Council of Governments to oversee and direct activities of the fund. As of December 31, 2015 two loans were outstanding. The two outstanding loans were paid off and the fund was dissolved as of October 28, 2016.

In 2013, a long term receivable was established as a result of participation in the BPA prepay program. The outstanding balance of this receivable was \$7,050,000 as of December 31, 2016. Of this amount \$600,000 will be collected within one year and is accordingly classified within current accounts receivable. For more information regarding the BPA prepay program, refer to Note 9.

#### I. Utility Plant and Depreciation

Refer to Note 4 – Capital Assets.

#### J. Other Liabilities and Other Credits:

Changes in Other Liabilities and Other Credits as of December 31, 2016 were as follows:

<b>Other Accrued Liabilities</b>	<b>2015</b>	<b>Increases</b>	<b>Decreases</b>	<b>2016</b>
Compensated Absences – Current	596,635	713,888	(689,870)	620,653
Conservation Credit	512,257	283,808	0	796,065
Extended Sick Leave	31,643	933		32,576
Other Current Liabilities	279,946	70,194	(53,823)	296,317
<b>Total Other Current Liabilities</b>	<b>\$1,420,481</b>	<b>\$1,068,823</b>	<b>(\$743,693)</b>	<b>\$1,745,611</b>

<b>Other Credits &amp; Liabilities – Long Term</b>	<b>2015</b>	<b>Increases</b>	<b>Decreases</b>	<b>2016</b>
Compensated Absences – Long Term	814,406	924,660	(1,018,878)	720,188
BPA Incentive Credit	2,056,039		(161,258)	1,894,781
<b>Total Other Credits &amp; Liabilities</b>	<b>\$2,870,445</b>	<b>\$924,660</b>	<b>(\$1,180,136)</b>	<b>\$2,614,969</b>

Changes in Other Liabilities and Other Credits as of December 31, 2015 were as follows:

<b>Other Accrued Liabilities</b>	<b>2014</b>	<b>Increases</b>	<b>Decreases</b>	<b>2015</b>
Compensated Absences – Current	609,706	691,416	(704,487)	596,635
Conservation Credit	343,967	355,178	(186,888)	512,257
Extended Sick Leave	30,182	1,461		31,643
Other Current Liabilities	275,144	50,776	(45,974)	279,946
<b>Total Other Current Liabilities</b>	<b>\$1,258,999</b>	<b>\$1,098,831</b>	<b>(\$937,349)</b>	<b>\$1,420,481</b>

<b>Other Credits &amp; Liabilities – Long Term</b>	<b>2014</b>	<b>Increases</b>	<b>Decreases</b>	<b>2015</b>
Compensated Absences – Long Term	721,341	897,700	(804,635)	814,406
BPA Incentive Credit	2,217,297		(161,258)	2,056,039
<b>Total Other Credits &amp; Liabilities</b>	<b>\$2,940,652</b>	<b>\$897,700</b>	<b>(\$965,893)</b>	<b>\$2,870,445</b>

The District records unpaid leave for compensated absences as an expense and liability when incurred. Personal leave may accumulate to a maximum of 1,200 hours, and is payable upon separation of service, retirement, or death. Employees hired after April 1, 2011 may accumulate a maximum of 700 hours. The District estimates a minimum of \$620,653 in compensated absences will be paid within one year. As of December 31, 2016 and 2015, \$620,653 and \$596,635 respectively, were included in other accrued liabilities on the statement of net position.

Conservation Credit is generally expected to be used within one year. Extended sick leave is sick leave accrued by employees (at 30%) prior to April 1, 1993, adjusted to actual as of December 31, 2016 and 2015. This total is no longer current sick leave; it is used at the employee's option to supplement the District sponsored short-term disability plan. The amount also represents the portion of leave that may be used upon retirement towards health insurance.

#### K. Debt Premium & Discount

Original issue and reacquired bond premiums and discounts relating to revenue bonds are amortized over the lives of the related bonds using the straight-line method. Unamortized premium and discount is included in the amount shown as Outstanding Revenue Bonds within the financial statements. Debt issuance costs are expensed in the period incurred in accordance with GASB Statement No. 65.

#### L. 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 included within Retail Energy Sales in the accompanying financial statements in the amount of \$2.1 million at December 31, 2016 and \$2.7 million at December 31, 2015.

#### 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. Contributed Capital

Capital contributions of \$2,855,788 and \$2,787,707 are reported for 2016 and 2015, respectively, on the statement of revenues, expenses and changes in net position. There were no capital contributions resulting from federal grant awards for either 2016 or 2015.

#### O. Use of Estimates

The preparation of the financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

#### P. Construction Financing

Capital expenditures in 2016 were made using 13.89% from Capital Contributions, 10.54% from Bond Funds, and 75.57% from rate revenue.

#### Q. Purchase Commitments

Refer to Note 9 for contracts with Bonneville Power Administration and others for future power supply.

### **NOTE 2 – DEPOSITS AND INVESTMENTS**

Deposits: The District's deposits and certificates of deposits are entirely covered by federal depository insurance (FDIC and FSLIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC). Deposit accounts are reconciled to the District's accounting records at year end, and the book balance of these accounts does not materially differ from the bank balance.

## Investments:

### *Investments Measured at Amortized Cost*

As of December 31, 2016, the District held the following investments at amortized cost:

Investments	Maturities	Total
State Treasurers Local Government Investment Pool (LGIP)	30 days average	\$23,470,599

As of December 31, 2015, the District held the following investments at amortized cost:

Investments	Maturities	Total
State Treasurers Local Government Investment Pool (LGIP)	35 days average	\$25,462,280

Credit Risk –The District’s investment policy conforms with state law, which restricts investments of public funds to funds to debt securities and obligations of the U.S. Treasury, U.S. Government agencies, and certain other U.S. Government sponsored corporations, certificates of deposit, and other evidences of deposit at financial institutions qualified by the Washington Public Deposit Protection Commission (PDPC), bankers’ acceptances, investment-grade general obligation debt of state and local governments and public authorities, and the Washington State Treasurer’s Local Government Investment Pool (LGIP). The LGIP portfolio meets the requirements set forth in GASB 79 to report the investment at amortized cost. The reported value of the pool is the same as the fair value of the pool shares. There is no formal withdrawal transaction limit, however, the LGIP requests a one day notice for transaction sizes of ten million dollars or more. The LGIP is governed by the State Finance Committee and is administered by the State Treasurer. The District does not have a policy specifically addressing custodial credit risk.

## **NOTE 3 – DERIVATIVE INSTRUMENTS**

The District has adopted GASB Statement No. 53 *Accounting and Financial Reporting for Derivative Instruments*. Subject to certain exceptions, GASB 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 derivatives 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. It is the District’s policy to document and apply as appropriate the normal purchase and normal sales exception 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, natural gas and option contracts that require 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 under GASB Statement No. 53 and therefore are not required to be recorded at fair value in the financial statements. Certain put and call options, and financial swaps for electricity and natural gas, are considered to be derivatives under GASB Statement No. 53, but do not generally meet the “normal purchases and normal sales” criteria.

As of December 31, 2016, the District had the following derivative instruments outstanding:

As of December 31, 2016, the District had the following derivative instruments outstanding:						
	Changes in Fair Value		Fair Value at December 31, 2016		Notional	
	Classification	Amount	Classification	Amount		
Cash Flow Hedges:						
Financial Swap Forward	Deferred Inflow	\$ 462,361	Derivative Asset	\$ 462,361	64,916	MWh
Financial Swap Forward	Deferred Inflow	\$ 787,410	Derivative Asset	\$ 787,410	1,151,400	mmbtu
Financial Swap Forward	Deferred Outflow	\$ (582,511)	Derivative Liability	\$ (582,511)	111,814	MWh
Financial Swap Forward	Deferred Outflow	\$ (373,695)	Derivative Liability	\$ (373,695)	43,200	mmbtu
Put Options	Deferred Outflow	\$ (14,589)	Derivative Liability	\$ (14,589)	10,800	MWh

These derivative instruments were entered into between April 2015 and December 2016 with maturities between January 2017 and September 2018.

As of December 31, 2015, the District had the following derivative instruments outstanding:

As of December 31, 2015, the District had the following derivative instruments outstanding:						
	Changes in Fair Value		Fair Value at December 31,2015		Notional	
	Classification	Amount	Classification	Amount		
Cash Flow Hedges:						
Financial Swap Forward	Deferred Inflow	\$ 1,836,836	Derivative Asset	\$ 1,836,836	334,396	MWh
Financial Swap Forward	Deferred Inflow	\$ 74,074	Derivative Asset	\$ 74,074	23,400	mmbtu
Financial Basis Swap	Deferred Inflow	\$ 110,856	Derivative Asset	\$ 110,856	-	mmbtu
Financial Swap Forward	Deferred Outflow	\$ (1,009,703)	Derivative Liability	\$ (1,009,703)	1,863,600	mmbtu
Financial Swap Forward	Deferred Outflow	\$ (180,874)	Derivative Liability	\$ (180,874)	17,902	MWh
Call Options	Deferred Outflow	\$ (8,784)	Derivative Liability	\$ (8,784)	10,000	MWh

These derivative instruments were entered into between November 2013 and December 2015 with maturities between January 2016 and December 2017.

The fair values of the commodity swap contracts are based on the futures price curve for the Mid-Columbia Intercontinental Exchange for electricity. There are instances when the variance between prices at the Sumas gas trading hub and the Henry gas trading hub are wide, creating an illiquid market. The District has approved using Henry Hub to hedge Frederickson (refer to Note 9) when this occurs, but requires the position to be converted to Sumas by six months to delivery. This reduction of basis risk is achieved through the use of financial basis swaps. The fair value of the options was calculated using the Black-76 options pricing model. The District categorizes its fair value measurements within the fair value hierarchy established by GAAP. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. All of the District's fair market measurements are classified as Level 2.

#### Objective & Strategies:

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. Generally, several strategies are employed to hedge the District's resource portfolio, including:

**Combustion Turbines** – The District purchases gas for future periods to generate electricity when the plant is economically viable on a marginal basis for that period based on parameters set by the Risk Management Committee. If load projections indicate that the District does not require the electricity to serve its customers, an equivalent quantity of power will concurrently be sold or otherwise hedged for the same period.

Surplus Purchased Power Resources – The District hedges projected surpluses in future periods by selling power or by purchasing put options. Surplus power is generally sold forward at a fixed-price, either physically or financially, when the probability of surplus is very high; surplus power is hedged through the purchase of physical or financial put options when the projected surplus is less certain, but nevertheless expected to be available under expected scenarios.

Deficit Power Resources – The District hedges projected power resource deficits in future periods by purchasing power or by purchasing power call options (or if the Frederickson Project (see Note 9) is economically viable for the period, by buying gas or gas call options). Power is generally purchased to cover projected deficits at a fixed price, either physically or financially, when the probability of the deficit position is very high; such deficit positions are hedged through the purchase of physical or financial call options when the projected deficits are less certain, but nevertheless expected under the approved planning conditions.

Derivatives authorized under the Risk Management Policy and employed by the District include:

- Physical power and natural gas forward purchases and sales
- Monthly and daily power and gas physical calls and puts
- Power and natural gas fixed for floating swaps
- Currency swaps relating to managing US/Canadian exchange rate risk resulting from transactions denominated in Canadian dollars
- Quarterly and monthly financial power and gas put and call options
- Financial daily power and gas put and call options
- Quarterly and monthly financial power and natural gas swaptions
- Financial natural gas swing and basis swaps

There is no associated debt for these instruments at December 31, 2016 or 2015.

#### Credit Risk

The District is a client of The Energy Authority, Inc. (TEA). The District adheres to the credit policies and credit limits established by TEA. TEA's policy addresses guidelines for setting credit limits and monitors credit exposure on a real time basis on behalf of the District. TEA's management determines the credit quality of the District's counterparties based upon various credit evaluation factors, including collateral requirements under certain circumstances.

All physical electricity transactions (for hourly and/or daily) for the District are traded by TEA as principle (on behalf of the District) and rely on TEA's credit limits. All forward physical/financial commodity transactions are entered into only with counterparties approved by the District's Risk Management Committee for creditworthiness; credit limits based on market conditions and available qualified counterparties are established and reviewed annually by the Risk Management Committee. As of December 31, 2016, the District had 47 counterparties with credit ratings ranging from "not rated" to AA, or secured by guarantors with BBB to AA credit ratings. As of December 31, 2015, the District had 50 counterparties. The maximum credit extended to any single counterparty is \$3 million.

The District entered into master enabling agreements with various counterparties, which enable hedging transactions. Such agreements include the Western Systems Power Pool (WSPP) form of agreement for physical power transactions, various forms of enabling agreements for physical gas transactions and International Swap Dealers Association Agreements (ISDA) 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 agreement to diffuse a portion of the risk.

Transactions under the physical enabling agreements are used to deal with long and short physical positions under the direction of the Risk Management Committee and pursuant to the risk management policy. Transactions under the ISDA agreements are used to financially hedge long or short positions so that the agreements also permit the District to hedge the risk of an underlying physical position by using call options, or put options.

The aggregate fair value of hedging derivative instruments in asset positions was \$1,249,771 and \$2,021,766 as of December 31, 2016 and 2015, respectively. The District transacts with various counterparties throughout the year, and as of December 31, 2016 three counterparties comprised 94% of the net exposure to credit risk, with credit ratings ranging from Not Rated/Baa2 to A. As of December 31, 2015, four counterparties comprised 97% of the net exposure to credit risk, with credit ratings ranging from Baa1/BBB to A3.

#### Basis 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. At December 31, 2016 and 2015, there are no derivative transactions outstanding that carry basis risk. As applicable, all power related transactions are to be settled on the relevant Mid-Columbia index and all gas transactions are to be settled on the relevant Sumas/Huntingdon index or be converted to the Sumas/Huntingdon index within six months of delivery. The District has ready access to electric transmission and natural gas transportation capacity at those respective trading points.

#### Termination Risk

As of December 31, 2016 and 2015, no termination events have occurred and there are no outstanding transactions with material termination risk. None of the outstanding transactions have early termination provisions except in the event of default by either counterparty. Events of default are generally related to (i) failure to make payments when due, (ii) failure to provide and maintain suitable credit assurances as required, (iii) bankruptcy or other evidence of insolvency, or (iv) failure to perform under any material provision of the agreement. Failure to provide or receive energy or natural gas under physical commodity transactions does generally not fall under the events of default provisions, unless the non-performing party fails to pay the resulting liquidated damages as they come due.

There is no rollover, interest rate, foreign currency, or market access risk for these derivative products as of December 31, 2016 and 2015.

#### **NOTE 4 – CAPITAL ASSETS**

Major expenses for utility plant and major repairs that increase useful lives are capitalized. The District's capitalization threshold is \$5,000 for non-infrastructure capital. All costs related to infrastructure are capitalized. Maintenance, repairs and minor renewals are accounted for as expenses when incurred.

Utility plant in service and other capital assets are recorded at cost where the historical cost is known. Where historical cost is not known, assets are recorded at estimated cost. Contributions by developers and customers are recorded at contract price or cost as contributions in aid of construction. The District records depreciation on assets acquired by contributions.



Utility Plant Activity for the year ended December 31, 2016 was as follows:

Utility Plant	Balance, 12/31/2015	Increase	Decrease	Balance, 12/31/2016
Assets not subject to depreciation:				
Land	\$893,104			\$893,104
Construction Work in Progress	7,462,430	13,103,162	(16,842,908)	3,722,684
Assets subject to depreciation or amortization:				
Intangible	1,269,291	104,074		1,373,365
Broadband	16,751,057	1,760,743	(33,636)	18,478,164
Transmission	6,384,664	279,001	(8,338)	6,655,327
Distribution	159,543,082	13,906,821	(117,034)	173,332,869
General Plant	22,994,790	1,017,373	(15,491)	23,996,672
Subtotal	215,298,418	30,171,174	(17,017,407)	228,452,185
Less Accumulated Depreciation & Amortization:				
Intangible	(340,165)	(163,334)		(503,499)
Broadband	(8,986,569)	(1,139,707)	5,883	(10,120,393)
Transmission	(2,747,814)	(154,989)		(2,902,803)
Distribution	(58,356,294)	(4,627,902)	65,071	(62,919,125)
General Plant	(13,848,779)	(731,225)		(14,580,004)
Total Accumulated Depreciation & Amortization	(84,279,621)	(6,817,157)	70,954	(91,025,824)
<b>Net Utility Plant</b>	<b>\$131,018,797</b>	<b>\$23,354,017</b>	<b>(\$16,946,453)</b>	<b>\$137,426,361</b>

Utility Plant Activity for the year ended December 31, 2015 was as follows:

Utility Plant	Balance, 12/31/2014	Increase	Decrease	Balance, 12/31/2015
Assets not subject to depreciation:				
Land	\$893,104			\$893,104
Construction Work in Progress	6,705,840	11,322,770	(10,566,180)	7,462,430
Assets subject to depreciation or amortization:				
Intangible	1,288,202	80,162	(99,073)	1,269,291
Broadband	15,891,728	860,037	(708)	16,751,057
Transmission	5,912,793	474,847	(2,976)	6,384,664
Distribution	152,055,152	7,637,957	(150,027)	159,543,082
General Plant	22,594,764	801,742	(401,716)	22,994,790
Subtotal	205,341,583	21,177,515	(11,220,680)	215,298,418
Less Accumulated Depreciation & Amortization:				
Intangible	(182,475)	(157,690)		(340,165)
Broadband	(7,921,695)	(1,064,946)	72	(8,986,569)
Transmission	(2,599,963)	(147,882)	31	(2,747,814)
Distribution	(53,980,570)	(4,476,824)	101,100	(58,356,294)
General Plant	(13,266,183)	(821,876)	239,280	(13,848,779)
Total Accumulated Depreciation & Amortization	(77,950,886)	(6,669,218)	340,483	(84,279,621)
<b>Net Utility Plant</b>	<b>\$127,390,697</b>	<b>\$14,508,297</b>	<b>(\$10,880,197)</b>	<b>\$131,018,797</b>

Capital assets are depreciated using the straight-line method over the following estimated useful lives for major asset classes:

Broadband	5-15 years
Transmission	33-50 years
Distribution	15-50 years
General Plant	5-40 years
Production	20 years

Intangible assets are amortized over their estimated useful life at the time of purchase, if the asset meets the criteria for amortization. Initial depreciation on utility plant is recorded in the month subsequent to purchase or project completion.

Preliminary costs incurred for proposed projects are deferred pending construction of the facility. Costs relating to projects ultimately constructed are transferred to utility plant. Charges that relate to abandoned projects are expensed.

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 the 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 2016.

#### Asset Held for Sale

During 2010, the District's Pasco Combustion Turbine plant became temporarily inoperable. In 2013, certain repairs were conducted to make the plant operable and available for sale. As of December 31, 2015, District management determined that the fair value of the plant is approximately \$5.4 million based on markets for similar assets. This adjustment resulted in an extraordinary loss of \$3 million for 2015 that is presented within the Statement of Revenues, Expenses and changes in Net Position. Refer to Note 9 for additional information.

The District has active construction projects as of December 31, 2016 in the amount of \$3,722,684. The District does not require future financing to complete these projects.

#### **NOTE 5 – LONG TERM DEBT**

During the year ended December 31, 2016, the following changes occurred in long term debt:

Issue	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
2007 Electric Revenue & Refunding Bonds – interest rates ranging 4.0% - 5.0%, maturing in 2032	50,715,000		(\$30,335,000)	\$2,670,000	\$2,670,000
2013A Electric Revenue & Refunding Bonds - interest rates ranging 2.0% - 5.0%, maturing in 2031	18,370,000		(160,000)	17,930,000	170,000
2013B Electric Revenue & Refunding Bonds - interest rates ranging 1.0% - 4.2%, maturing in 2023	9,155,000		(165,000)	8,670,000	165,000
2016A Electric Revenue & Refunding Bonds - interest rates ranging 3.1% - 5.0%, maturing in 2041		16,870,000		16,870,000	
2016B Electric Revenue & Refunding Bonds - interest rates ranging 1.0% - 2.2%, maturing in 2022		15,305,000		15,305,000	195,000
Subtotal	59,930,000		(30,660,000)	61,445,000	3,200,000
Plus: Unamortized premium	1,968,012	2,862,129	(1,790,574)	3,039,567	
Less: Unamortized discount	(377,190)	(31,818)	170,380	(238,628)	
<b>Total Long-Term Liabilities</b>	<b>\$61,520,822</b>		<b>(\$32,280,194)</b>	<b>\$64,245,939</b>	<b>\$3,200,000</b>

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
2007 Electric Revenue & Refunding Bonds – interest rates ranging 4.0% - 5.0%, maturing in 2032	50,715,000	\$35,425,000	(\$2,420,000)	\$33,005,000	\$2,540,000
2013A Electric Revenue & Refunding Bonds - interest rates ranging 2.0% - 5.0%, maturing in 2031	18,370,000	18,250,000	(160,000)	18,090,000	160,000
2013B Electric Revenue & Refunding Bonds - interest rates ranging 1.0% - 4.2%, maturing in 2023	9,155,000	8,995,000	(160,000)	8,835,000	165,000
Subtotal		62,670,000	(2,740,000)	59,930,000	2,865,000
Plus: Unamortized premium		2,080,708	(112,696)	1,968,012	
Less: Unamortized discount		(396,184)	18,994	(377,190)	
<b>Total Long-Term Liabilities</b>		<b>\$64,354,524</b>	<b>(\$2,833,702)</b>	<b>\$61,520,822</b>	<b>\$2,865,000</b>

Future Debt Service on these bonds is as follows:

Year	Principal	Interest	Total
2017	\$ 3,200,000	\$ 2,355,992	\$ 5,555,992
2018	3,260,000	2,306,275	5,566,275
2019	3,320,000	2,254,581	5,574,581
2020	3,365,000	2,194,813	5,559,813
2021	3,445,000	2,128,193	5,573,193
2022-2026	12,805,000	9,277,270	22,082,270
2027-2031	14,510,000	6,251,906	20,761,906
2032-2036	11,695,000	2,979,456	14,674,456
2037-2041	5,845,000	484,793	6,329,793
<b>Total</b>	<b>\$ 61,445,000</b>	<b>\$ 30,233,279</b>	<b>\$ 91,678,279</b>

In March 2007, the District issued Electric Revenue and Refunding Bonds, Series 2007 in the amount of \$ 50,715,000. The Bonds were issued to finance improvements to the electric utility system and to refund certain Outstanding Electric Revenue and Refunding Bonds; to acquire a surety policy to fund the Reserve Account; and to pay costs of issuance of the Bonds. The District cash defeased \$2,744,547 portions of Electric Revenue Refunding Bonds, Series 1996 and 2002. This advance refunding was undertaken to reduce debt service payments over the next ten years by \$1,908,645 and recognize total present value savings of \$2,122,687. The transaction resulted in an economic loss of \$796,785.

During 2013 the District issued Series 2013A Electric Revenue and Refunding bonds in the amount of \$18,370,000 and Series 2013B (Taxable) in the amount of \$9,155,000 for the purpose of financing certain capital improvements to the District's electric system and refund the 2001, 2002 and 2003 outstanding bonds, as well as certain maturities of the 2007 bonds. The refunding portion of the bond proceeds was placed in an irrevocable trust for future debt service on the refunded bonds. At December 31, 2013, the 2001, 2002 and 2003 bonds were considered defeased and are no longer reflected in the District's financial statements. The refunding resulted in net present value cash flow savings of (\$1,071,453) and an economic loss from refunding of \$770,025. Bond proceeds were also used to establish the debt service reserve fund in the amount of \$3,142,483 as required by the bond resolutions.

In October 2016, the District issued Electric Revenue and Refunding Bonds Series 2016A and 2016B (taxable) in the amounts of \$16,870,000 and \$15,305,000, respectively. The bonds were issued for the purpose of refunding the portion of the 2007 series bonds maturing after September 1, 2017 and to fund future improvement to the electric utility system in the amount of \$5 million. The refunding proceeds were placed in an irrevocable trust for future debt service on the refunded bonds and as of December 31, 2016 are no longer report within the District's Financial Statements. The transaction resulted in a net present value cash flow savings to the District of \$2.4 million over the life of the refunded bonds and an economic gain of \$257,938. The refunding resulted in an increase to the District's Debt Service Reserve Fund of \$772,166. As of December 31, 2016, \$3,276,911 of unspent bond proceeds remained in the bond construction fund.

As of December 31, 2016 and 2015, there was \$3,914,649 and \$3,142,483 respectively in restricted assets related to bonded debt of the District. This represents the debt service reserve fund as required by the bond resolutions. There are a number of other limitations and restrictions contained in the various bond resolutions. The District is in compliance with all significant limitations and restrictions, including those regarding federal arbitrage.

#### Line of Credit

The District's renewable \$3 million line of credit with Bank of the West expired October 31, 2016. This line of credit was not renewed. In October 2016, the District entered into a non-revolving line of credit to support standby letters of credit with Umpqua Bank in the amount of \$3 million. The District does not anticipate utilizing this line of credit in 2017.

#### **NOTE 6 – PENSION PLANS**

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

<b>Aggregate Pension Amounts – All Plans</b>	<b>2016</b>	<b>2015</b>
Pension liabilities	\$8,573,908	\$7,158,356
Pension assets	\$0	\$0
Deferred outflows of resources	\$1,425,779	\$830,638
Deferred inflows of resources	\$157,778	\$1,068,151
Pension expense/expenditures	\$863,394	\$414,312

#### **State Sponsored Pension Plans**

Substantially all of the District's 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](http://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 2016 were as follows:

<b>PERS Plan 1</b>		
<b>Actual Contribution Rates:</b>	<b>Employer</b>	<b>Employee</b>
PERS Plan 1	6.23%	6.00%
PERS Plan 1 UAAL	4.77%	6.00%
Administrative Fee	0.18%	
<b>Total</b>	<b>11.18%</b>	<b>6.00%</b>

**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.

### Contributions

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 2016 were as follows:

PERS Plan 2/3		
Actual Contribution Rates:	Employer 2/3	Employee 2
PERS Plan 2/3	6.23%	6.12%
PERS Plan 1 UAAL	4.77%	
Administrative Fee	0.18%	
Employee PERS Plan 3		varies
<b>Total</b>	<b>11.18%</b>	<b>6.12%</b>

The District's actual PERS plan contributions were \$435,891 to PERS Plan 1 and \$517,463 to PERS Plan 2/3 for the year ended December 31, 2016.

### **Actuarial Assumptions**

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2016 with a valuation date of June 30, 2015. 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 2015 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2016. Plan liabilities were rolled forward from June 30, 2015, to June 30, 2016, 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.

- For all systems, except LEOFF Plan 2, the assumed valuation interest rate was lowered from 7.8% to 7.7%. Assumed administrative factors were updated.

- Valuation software was corrected on how the nonduty disability benefits for LEOFF Plan 2 active members is calculated
- New LEOFF Plan 2 benefit definitions were added within the OSA valuation software to model legislation signed into law during the 2015 legislative session.

### 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, 2016, 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%
	<b>100%</b>	

### 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.

2016:

	1% Decrease (6.5%)	Current Rate (7.5%)	1% Increase (8.5%)
PERS 1 (.076313%)	4,942,219	4,098,368	3,372,181
PERS 2/3 (.088890%)	8,240,276	4,475,541	(2,329,778)

2015:

	1% Decrease (6.5%)	Current Rate (7.5%)	1% Increase (8.5%)
PERS 1 (.076313%)	4,834,586	3,970,904	3,228,216
PERS 2/3 (.088890%)	9,320,277	3,187,453	(1,508,221)

### 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, 2016, the District reported a total pension liability of \$8,573,908 for its proportionate share of the net pension liabilities as follows:

	Liability (or Asset)
PERS 1	\$4,098,368
PERS 2/3	\$4,475,540

At June 30, 2015, the District reported a total pension liability of \$7,158,357 for its proportionate share of the net pension liabilities as follows:

	Liability (or Asset)
PERS 1	\$3,970,904
PERS 2/3	\$3,187,453

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

	Proportionate Share 6/30/15	Proportionate Share 6/30/16	Change in Proportion
PERS 1	0.075912%	0.076313%	0.000401%
PERS 2/3	0.089208%	0.088890%	-0.000318%

	Proportionate Share 6/30/14	Proportionate Share 6/30/15	Change in Proportion
PERS 1	0.079646%	0.075912%	-0.003734%
PERS 2/3	0.088809%	0.089208%	0.000399%



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 except LEOFF 1.

The collective net pension liability (asset) was measured as of June 30, 2016, and the actuarial valuation date on which the total pension liability (asset) is based was as of June 30, 2015, with update procedures used to roll forward the total pension liability to the measurement date.

### Pension Expense

For the year ended December 31, 2016 and 2015, the District recognized pension expense as follows:

2016	Pension Expense
PERS 1	\$239,709
PERS 2/3	\$610,555
TOTAL	\$850,264

2015	Pension Expense
PERS 1	\$210,774
PERS 2/3	\$203,538
TOTAL	\$414,312

### Deferred Outflows of Resources and Deferred Inflows of Resources

At December 31, 2016, 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	Deferred Inflows of Resources
Differences between expected and actual experience		
Net difference between projected and actual investment earnings on pension plan investments	\$ 103,190	
Changes of assumptions		
Changes in proportion and differences between contributions and proportionate share of contributions		
Contributions subsequent to the measurement date	\$ 219,941	
<b>TOTAL</b>	<b>\$ 323,131</b>	<b>\$ -</b>

PERS 2/3	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 238,319	\$ (147,745)
Net difference between projected and actual investment earnings on pension plan investments	\$ 547,678	
Changes of assumptions	\$ 46,258	
Changes in proportion and differences between contributions and proportionate share of contributions	\$ 9,062	\$ (10,034)
Contributions subsequent to the measurement date	\$ 261,331	
<b>TOTAL</b>	<b>\$ 1,102,648</b>	<b>\$ (157,779)</b>

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

<b>PERS 1</b>	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Differences between expected and actual experience		
Net difference between projected and actual investment earnings on pension plan investments		\$ 217,252
Changes of assumptions		
Changes in proportion and differences between contributions and proportionate share of contributions		
Contributions subsequent to the measurement date	\$ 216,813	
<b>TOTAL</b>	<b>\$ 216,813</b>	<b>\$ 217,252</b>

<b>PERS 2/3</b>	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Differences between expected and actual experience	\$ 338,827	
Net difference between projected and actual investment earnings on pension plan investments		\$ 850,899
Changes of assumptions	\$ 5,136	
Changes in proportion and differences between contributions and proportionate share of contributions	\$ 12,838	
Contributions subsequent to the measurement date	\$ 257,024	
<b>TOTAL</b>	<b>\$ 613,825</b>	<b>\$ 850,899</b>

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, 2017. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

<b>Year ended December 31</b>	<b>PERS 1</b>
2017	(25,408)
2018	(25,408)
2019	94,769
2020	59,237
2021	
Thereafter	
<b>TOTAL</b>	<b>\$ 103,190</b>
<b>Year ended December 31</b>	<b>PERS 2/3</b>
2017	3,732
2018	3,732
2019	417,135
2020	258,939
2021	
Thereafter	
<b>TOTAL</b>	<b>\$ 683,538</b>

## **NOTE 7 – DEFERRED COMPENSATION AND HEALTH BENEFIT PLANS**

### **Deferred Compensation Plans**

The District offers its employees deferred compensation plans created in accordance with Internal Revenue Code Sections 457 and 401(a) permitting employees to defer a portion of their salary until future years. The District match is locked at a maximum rate of 2%. The deferred compensation is not available to employees until separation from service through termination, retirement, death or unforeseeable emergency. The plan assets are held in trust for the exclusive benefit of plan participants and beneficiaries. The District made matching contributions of \$148,162 and \$153,388 in 2016 and 2015, respectively. Employees made contributions of \$515,593 and \$529,621 to the 457 and 401(a) plans in 2016 and 2015, respectively.

### **Health Benefit Plans**

Effective January 1, 2016, employees who elect to participate in a District provided wellness program receive a \$150 per month contribution into their health reimbursement agreement (HRA). In addition, the District makes annual contributions to employee HRA accounts for those employees who enroll in the District's consumer directed health plan (CDHP). The plan assets are held in trust for the exclusive benefit of plan participants and beneficiaries.

## **NOTE 8- OTHER POSTEMPLOYMENT BENEFITS (OPEB)**

The District offers a postemployment benefit plan to pay a portion of medical insurance premiums for certain retirees between the ages of 60 through 64. The plan was established as part of the Collective Bargaining Agreement and is offered to all employee types. The plan may be amended as part of the bargaining process. The plan is administered by the District and does not issue a stand-alone report. To be eligible to receive plan benefits, an employee must have worked in a PERS-eligible position while actively employed, must retire between August 1, 2005 and July 31, 2018, must enroll in retiree medical insurance or COBRA from the Central Washington Public Utilities Unified Insurance Trust within the enrollment period following retirement and must remain continuously enrolled in medical insurance from the Trust.

Employees who retired during the initial plan year between August 1, 2005 and July 31, 2006 have monthly contributions equal to the lesser of actual medical premiums or ten dollars for each year of PERS-eligible service at the District paid toward their medical insurance premium during the time they are between the ages of 60 through 64 for each month they remain enrolled in medical insurance from the Trust. For employees who retired between August 1, 2006 and July 31, 2007 the monthly contributions are equal to the lesser of actual medical premiums or nine dollars for each year of PERS-eligible service. For employees who retire between August 1, 2007 and July 31, 2011 the monthly contributions will be equal to the lesser of actual medical premiums or eight dollars for each year of PERS-eligible service. For each successive year ending July 31, the dollar amount per month for each year of service will be reduced by one dollar until the benefit reaches zero on August 1, 2018.

The District performs an annual review of the plan relative to GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The plan was discontinued during 2015.

The District has made the following OPEB medical insurance premium contributions:

Year	Contributions
2006	\$3,420
2007	\$6,528
2008	\$4,352
2009	\$8,294
2010	\$3,096
2011	\$3,072
2012	\$3,014
2013	\$2,356
2014	\$6,540
2015	\$ 720

## **NOTE 9- POWER SUPPLY**

### **Bonneville Power Administration (BPA)**

The District obtains power from BPA under a long-term power purchase agreement. BPA supplies the District's power under a Block and Slice Power Sale Agreement, which extends from October 1, 2011 through September 30, 2028. The Block product provides power in monthly amounts ranging between 50 average megawatts (aMW) to 81 aMW. Monthly Block purchase amounts are fixed, but are shaped to the District's monthly power requirements. The Slice product provides the District 0.78% of the output of the federal system. The District's share of the Slice product is expected to be 75 aMW, but may vary considerably based on water conditions within the Northwest. Depending upon hydroelectric generating conditions and market prices, the District expects to procure between 95% and 100% of its total energy resources from BPA on an average annual basis.

Beginning October 1, 2011, BPA changed its rate-making methodology to a tiered rate approach. Each preference customer received a High Water Mark (HWM) based on its 2010 load that defined its right to buy power at a Tier 1 rate. The Tier 1 rate is based on the cost of the existing federal system. HWMs are translated into "Tier 1 Cost Allocators" (TOCAs) which, when multiplied by the estimated costs of the federal system, determine their power costs. There is an additional monthly load shaping charge (or credit) for Block and Load Following products, determined by the shape of customers' loads when compared to the shape of the federal system.

If preference customers want to buy more BPA power beyond their HWM, it will be sold at a Tier 2 rate set to fully recover BPA's cost of security additional resources to serve this load. They also have the option of serving some or all of their above-HWM load with non-federal resources. At this time the District has no plans to buy Tier 2 power from BPA.

BPA is required by federal law to recover all of its costs through the rates it charges its customers. The rate provisions for the Block product include a cost recovery adjustment clause (CRAC). The CRAC allows BPA to raise rates to collect sufficient funds to pay costs. A dividend distribution clause (DDC) results in dollars being returned to customers, in the form of future power rate decreases, if excess dollars are collected.

Pursuant to the Slice product rate provisions, the District is subject to additional charges or credits from BPA if BPA's actual costs deviate from budgeted amounts. The Slice product is not subject to the CRAC or DDC; but rather, the District pays its share of cost increases or receives its share of cost decreases through an annual true-up mechanism. The District's share of the true-up was approximately (\$68,233) and (\$1,184,136) in 2016 and 2015, respectively.

After determining that it had over collected from its public customers in providing payments to IOU's for residential exchange benefits in FY 2002-2006, BPA decided to credit the District to reimburse for these over collections. After that decision was challenged by the IOUs and others, parties finally settled the residential exchange issue in 2011. Under the terms of the agreement, the District's credit of approximately \$1 million per year will extend through FY 2018.

Beginning in April 2013, the District receives a monthly \$50,000 credit on its power bill for participation in the BPA Prepay Program. This program allowed customers to purchase blocks of prepaid credits for the future delivery of power in order to help BPA fund improvements to its infrastructure. The District purchased one block of prepay credits in the amount of \$6.8 million for the period April 2013 through September 2028. Total monthly credits received by the District will be \$9.3 million, and will result in a net present value savings of approximately \$1.1 million.

The District also entered into a contract with BPA for transmission service effective May 31, 1997, which provides adequate transmission capacity to meet the District's annual system peak load. The transmission contract extends through September 30, 2031.

### **Frederickson Project**

The District has an agreement with Frederickson Power, L.P. for the purchase of 30 MW of contract capacity from the Frederickson combined-cycle natural gas-fired combustion turbine project station near Tacoma, Washington. The agreement expires September 1, 2022. The District is able to economically dispatch the plant each day based on spot market power and gas prices. Power costs include a capacity charge and fixed and variable operation and

maintenance charges indexed to performance and escalation factors. The District is responsible for supplying natural gas to Frederickson Power, L.P. at Huntingdon, British Columbia on days that the plant is generating power. Natural gas is supplied to the Frederickson Project via the Northwest Pipeline. A proportionate share of the cost of this transportation is passed-through to the District each month.

#### Pasco Combustion Turbine Generating Station

The District and Grays Harbor PUD jointly constructed a four-unit, 44 megawatt (MW), simple-cycle gas-turbine generating station located in the District's service area. Commercial operation commenced in August 2002. The PUDs jointly own certain common facilities and individually own specific facilities (i.e., the turbines and SCR outfitted exhaust systems). In 2013, the District expended funds to repair the Pasco Combustion Turbine Generating Station to make it saleable. It was not intended to be placed back into service and was accordingly reclassified in 2013 as an asset held for sale. Grays Harbor PUD made a similar determination in early 2014. The PUDs are in the process of seeking a buyer for the facility. Refer to Note 4 – Capital Assets.

#### Energy Northwest

Energy Northwest is a municipal corporation and a joint operating agency of the State of Washington. It has the authority to acquire, construct and operate works, plants, and facilities for the generation and transmission of electric power and energy. The membership of Energy Northwest consists of twenty-three public utility districts, including the District, and five cities, all located in the State of Washington. The District is a participant in Nuclear Project Nos. 1 and 3, Columbia Generating Station, the Packwood Lake Hydroelectric Project and the Nine Canyon Wind Project. Columbia Generating Station, the Packwood Lake Hydroelectric Project and the Nine Canyon Wind Project are operating; Project Nos. 1 and 3 have been terminated.

The District, Energy Northwest and BPA have entered into separate "net billing agreements" with respect to Energy Northwest's Project No. 1, Columbia Generating Station and 70% ownership share of Project No. 3. Under terms of these agreements, the District has purchased from Energy Northwest and, in turn, assigned to BPA a maximum of capability of each project. BPA is unconditionally obligated to pay the District and the District is unconditionally obligated to pay Energy Northwest, the pro rata share of the total annual costs of each project, whether or not the projects are completed, operable or operating and notwithstanding the suspension, reduction or curtailment of the projects' output. The District's respective shares may be increased by not more than 25% upon default of other public agency participants.

- Packwood Lake Hydroelectric Project

The District is a 10.5% participant in Energy Northwest's 27 MW Packwood Project (the "Project"), located in the Cascade Mountains south of Mount Rainier. The Project's fifty-year license has expired and the Project has satisfied all of the requirements for relicensing with the Federal Energy Regulatory Commission and is waiting for final issuance. Energy Northwest recognizes revenues equal to expenses for each period. No net revenue or loss is recognized, and no equity is accumulated. Accordingly, no investment for the joint venture is reflected on the District's statement of net position. The participants entered into new Power Sales Contracts with Energy Northwest effective October 1, 2011. The participants' Agreements obligate the 12 participants to pay annual costs and receive excess revenues. The District uses their share of the energy to serve customer load.

- Nine Canyon Wind Project

The Nine Canyon Wind Project is another Energy Northwest generation project. It is located in the Horse Heaven Hills area southwest of Kennewick. The District has a contract for 2.01 MW of Phase I capacity and 8 MW of Phase III capacity. Nine Canyon has a capacity factor of 29% and the District receives approximately 2.88 aMW.

#### White Creek Wind Project

The District entered into a 20-year Purchase Agreement with LL&P Wind Energy, Inc., a wholly-owned subsidiary of Lakeview. The District purchases all of the energy and associated environmental attributes produced from 10 MW of the White Creek Wind Project's (White Creek) capacity. White Creek has a capacity factor of 30% and the District receives approximately 3 aMW. During the first contract year (2008) the price of energy delivered to the District was \$51.97 per MWH; the price will increase by 2% annually during the term of the contract. The environmental

attributes included in that price includes any and all credits, benefits, emissions reductions, offset and allowances attributable to the White Creek as a renewable energy resource.

#### Esquatzel Hydroelectric Project

The District contracted with Green Energy Today, LLC in 2011 to acquire the output from a small conduit hydroelectric project in Pasco, Washington, known as the Esquatzel Project. The Esquatzel Project generates approximately .7 aMW of electricity annually from return water flowing out of an agricultural canal that drains into the Columbia River. Water is diverted from the canal into a penstock and through a turbine with a generating capacity of 1 MW. The Esquatzel Project generally generates electricity year-round. The District's agreement with Green Energy Today, LLC is for a 20-year term, with a first right of refusal for two additional 10-year periods.

#### **Energy Independence Act (I-937)**

The citizens of Washington State passed Initiative 937 in November, 2006, now codified in the Revised Code of Washington Chapter 19.285 as the Energy Independence Act (the "Act"), which mandates renewable energy and conservation targets for the State's utilities with more than 25,000 customers. As of December 31, 2016 the District crossed this customer threshold. The Esquatzel, Nine Canyon and White Creek contracts will provide some of the renewable energy the District will need to comply with the Act's targets in the future.

The Esquatzel Project is a distributed generation resource. The Act defines distributed generation as an eligible renewable resource with a generating capacity of not more than 5 MW. As such, each MWH generated by the Esquatzel Project will count double toward the District's requirements under the Act.

#### Conservation / Energy Services

Conservation funding is available from BPA under the Energy Efficiency Incentive ("EEI") program in two year blocks. The District's EEI budget is \$2,495,294 and the District also budgets for self-funded conservation projects. The District expended \$0 and \$413,148 on utility funded conservation in 2016 and 2015 respectively. Under EEI, utilities request reimbursement from BPA after conservation dollars have been spent on eligible projects. EEI funds rebate incentives for residential energy efficiency upgrades including: weatherization, heat pumps, compact fluorescent lamps, and Energy Star appliances. The District also provides incentives for industrial, irrigation and commercial accounts for cost-effective energy savings.

#### **NOTE 10 - RISK MANAGEMENT**

The District maintains the following insurance coverage:

Coverage	Limit
Buildings and Personal Property	\$95,194,990
General Liability	\$2,000,000
Electromagnetic Field Liability	\$500,000
Umbrella Liability	\$15,000,000
Directors, Officers & Mgrs. Liability	\$10,000,000
Employee Theft Liability	\$4,000,000
Computer Fraud/Funds Transfer	\$2,000,000
Network & Data Protection	\$1,000,000

The District has not paid insurance settlements in excess of coverage in any of the past three years.

**NOTE 11 – PARTICIPATION IN NORTHWEST OPEN ACCESS NETWORK, INC. d.b.a. NOANET**

The District, along with eight 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 BPA, throughout Washington. The network began commercial operation in January 2001.

Each member of NoaNet has entered into a Repayment Agreement to guarantee the debt of NoaNet. This agreement was established and authorized by official resolutions adopted by the District's governing board. Under the Repayment Agreement, 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. The management of NoaNet anticipates meeting debt obligations through continuing profitable operations. There were no member assessments in 2015 or in 2014. The District's guarantee is based on its 6.39% interest. This guarantee was intact until the bonds were no longer outstanding as of December 2016.

As of December 31, 2013, NoaNet had two outstanding lines of credit guaranteed by the members. NoaNet may assess its Members for their percentage share of principal and interest on the Notes to the extent that NoaNet does not have sufficient funds to pay the Notes. However, NoaNet met its payment obligations on the lines of credit. During December 2014, NoaNet obtained a \$13,000,000 line of credit and transferred the balances of previous lines of credit to this new note. Furthermore, this new line of credit is not guaranteed by members, therefore the District does not have any guarantee obligation as of December 31, 2014 with regards to NoaNet's line of credit. In accordance with GASB No. 70 *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, the District has determined that based on qualitative factors and historical data, it is not likely that the District will be required to make a payment on the guarantees of NoaNet's bonded debt or lines of credit. Accordingly, no liability has been recorded by the District.

The following is a summary of the District's guarantees as of December 31, 2016 and 2015:

Date	District %		2016		2015	
			Amount Outstanding	District Guarantee	Amount Outstanding	District Guarantee
2001	6.39%	Bonds	\$0	\$0	\$2,790,000	\$178,281
	Total		\$0	\$0	\$2,790,000	\$178,281

NoaNet recorded a decrease in net position (unaudited) of \$4,555,622 and a decrease of \$5,390,113 for 2016 and 2015, respectively. In accordance with generally accepted accounting principles as well as a position statement issued by the Washington State Auditor concerning the appropriate accounting treatment for NoaNet, a proportionate share of these gain/losses has not been recorded by the District.

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

**NOTE 12 – TELECOMMUNICATIONS SERVICES**

The District installed and continues to build out a fiber optic backbone system in its service area to provide wholesale telecommunication services and for internal use by the electric system. The District has connected its fiber optic system to NoaNet's fiber optic communications system. Broadband coverage is also being extended through the development of a wireless network to deliver high-speed Internet service.

The following is a summary of Broadband activities for 2016 and 2015:

Broadband	2016	2015
Operating Revenues:		
Drop Fees	\$83,554	\$313,474
Fiber Transport charges	808,056	829,562
WiFi Transport	8,000	2,280
Collocation Rental	95,030	88,870
Miscellaneous Broadband Services	213,217	44,421
BTOP Program Income	151,076	178,683
Total Operating Revenues	1,358,933	1,457,290
Operating Expenses:		
Labor and Benefits	166,439	256,868
Supplies	2,379	9,751
Professional Services	21,648	24,167
Other Charges	72,112	57,516
Hardware and Fiber Maintenance	65,693	26,530
Depreciation	1,139,707	1,064,946
Total Operating Expenses	\$1,467,978	\$1,439,778
Capital Investment:		
Current	1,760,743	860,037
Cumulative (since 2000)	\$18,512,999	\$16,752,256

*The above are included in summarized amounts within the District's financial statements*

#### **NOTE 13 – SUBSEQUENT EVENTS**

Effective May 1, 2017 the District will implement an overall rate increase of 4.1%.



Required Supplementary Information

Schedules of Proportionate Share of the Net Pension Liability

As of June 30, 2016

Last 10 Fiscal Years\*

PERS Plan 1	2014	2015	2016
District's proportion of the net pension liability (asset)	0.079646%	0.075912%	0.076313%
District's proportionate share of the net pension liability	\$4,012,205	\$3,970,904	\$4,098,368
District's covered employee payroll	\$8,110,199	\$8,269,969	\$8,640,630
District's proportionate share of the net pension liability as a percentage of covered employee payroll	49.47%	48.02%	47.43%
Plan fiduciary net position as a percentage of the total pension liability	61.19%	59.10%	57.03%

PERS Plan 2 & 3	2014	2015	2016
District's proportion of the net pension liability (asset)	0.079646%	0.075912%	0.088890%
District's proportionate share of the net pension liability	\$1,795,150	\$3,187,453	\$4,475,541
District's covered employee payroll	\$8,110,199	\$8,269,969	\$8,640,630
District's proportionate share of the net pension liability as a percentage of covered employee payroll	22.13%	38.54%	51.80%
Plan fiduciary net position as a percentage of the total pension liability	93.29%	89.20%	57.03%

Notes:

\*These schedules are to be built prospectively until they contain ten years of data.

Required Supplementary Information

Schedules of Employer Contributions

As of December 31, 2016

Last 10 Fiscal Years\*

PERS 1	2015	2016
Statutorily or contractually required contributions	\$392,546	\$435,891
Contributions in relation to the statutorily or contractually required contributions	(392,546)	(435,891)
Contribution deficiency (excess)	0	0
Covered employer payroll	\$8,516,494	\$8,666,873
Contributions as a percentage of covered employee payroll	4.61%	5.03%

PERS 2 & 3	2015	2016
Statutorily or contractually required contributions	\$457,619	\$517,463
Contributions in relation to the statutorily or contractually required contributions	(457,619)	(517,463)
Contribution deficiency (excess)	0	0
Covered employer payroll	\$8,516,494	\$8,666,873
Contributions as a percentage of covered employee payroll	5.37%	5.97%

Notes:

\*These schedules are to be built prospectively until they contain ten years of data.

## 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	
Public Records requests	<a href="mailto:PublicRecords@sao.wa.gov">PublicRecords@sao.wa.gov</a>
Main telephone	(360) 902-0370
Toll-free Citizen Hotline	(866) 902-3900
Website	<a href="http://www.sao.wa.gov">www.sao.wa.gov</a>