Office of the Washington State Auditor
Pat McCarthy

December 14, 2017

Board of Commissioners
Public Utility District No. 1 of Lewis County
Chehalis, Washington

Contracted CPA Firm's Audit Report on Financial Statements

We have reviewed the audit reports issued by a certified public accounting (CPA) firm on Public Utility District No. 1 of Lewis County's financial statements for the fiscal years ended December 31, 2015 and December 31, 2016. The District contracted with the CPA firm for these audits.

Based on this review, we have accepted these reports in lieu of the audit required by RCW 43.09.260. The State Auditor's Office did not audit the accompanying financial statements and, accordingly, we do not express opinions on those financial statements.

This report is being published on the State Auditor's Office website as a matter of public record.

Sincerely,

Pat McCarthy

State Auditor

Olympia, WA

Insurance Building, P.O. Box 40021 • Olympia, Washington 98504-0021 • (360) 902-0370 • Pat.McCarthy@sao.wa.gov

-Report of Independent Auditors and
Financial Statements with Required
Supplementary Information for

Public Utility District No. 1 of Lewis County

December 31, 2016 and 2015

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

CONTENTS

REPORT OF INDEPENDENT AUDITORS

Board of Commissioners
Public Utility District No. 1 of Lewis County
Chehalis, Washington

Report on the Financial Statements
We have audited the accompanying combined and separate financial statements of Public Utility District No. 1 of Lewis County's Electric System and Cowlitz Falls System (the District) which comprise the combined and separate statements of net position as of December 31, 2016, and the related combined and separate statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the combined statement of net position as of December 31, 2015, and the related combined statement of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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.

REPORT OF INDEPENDENT AUDITORS (continued)

Opinions

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 Lewis County's Electric System and Cowlitz Falls System as of December 31, 2016 and 2015 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis preceding the financial statements and the schedule of proportionate share of net pension liability and schedule of employer contributions subsequent to the notes to the financial statements be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the 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 May 30, 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.

Moss Adams LLP

Portland, Oregon
May 30, 2017

This discussion and analysis is designed to provide an overview of Public Utility District No. 1 of Lewis County, Washington (the District) financial activities for the year ended December 31, 2016, with comparable information for 2015 and 2014. This required supplementary information should be read in conjunction with the District's financial statements and notes to financial statements.

The District is a municipal corporation incorporated in 1936 to serve the citizens of Lewis County, Washington. The District is governed by a three-member board of locally elected commissioners, independent of the county government. The District manages and operates two systems: Electric Distribution System (Electric System) and the Cowlitz Falls Hydroelectric Generation Project (Cowlitz Falls System).

Overview of the Financial Statements

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

Effective for fiscal year ended December 31, 2016, the District adopted GASB Statement of Government Accounting Standards No. 72, Fair Value Measurement and Application. This Statement establishes standards for fair value measurements of assets and liabilities. The definition of fair value is the price in an orderly transaction between market participants at the measurement date. No adjustments were needed as a result of adopting this Statement.

Basic Financial Statements

The Statement of Net Position presents the District's net position as the difference between assets and deferred outflows of resources, and liabilities and deferred inflows of resources. The Statement of Net Position provides information about the nature and amount of investments in resources (assets), the consumption of net position in one period that are applicable to future periods (deferred outflows of resources), the obligations to creditors (liabilities), and the acquisition of net position that are applicable to future periods (deferred inflows of resources).

The Statement of Revenues, Expenses, and Changes in Net Position reports the revenues and expenses during the periods indicated and identify operating activity separately from non-operating activity.

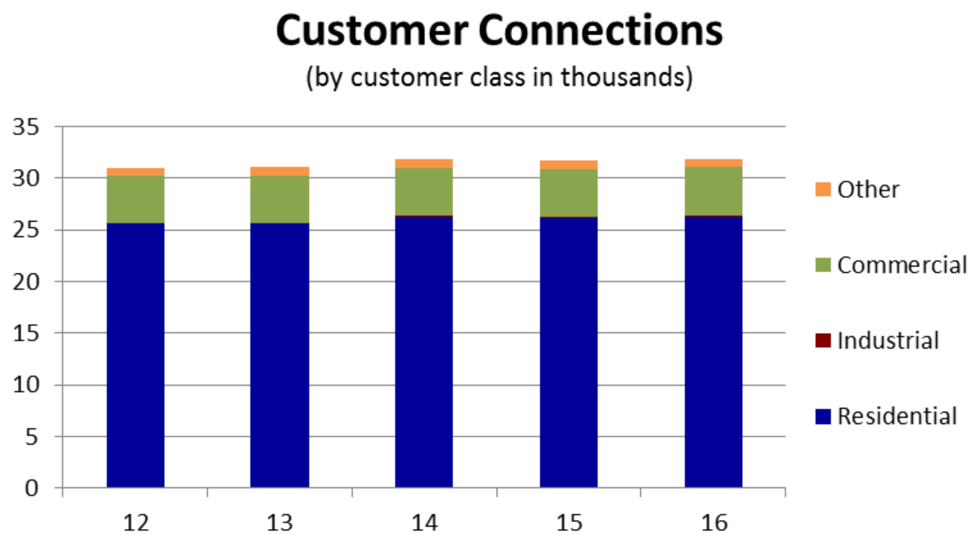
The Statement of Cash Flows provides information about the District's cash flows from operating activities, capital and related financing activities, investing activities, and noncapital financing activities, and presents a reconciliation of net operating income to net cash provided by operating activities.

Notes to the Financial Statements

The notes to the financial statements provide additional information that is essential to a full understanding of the figures provided in the basic financial statements.

ELECTRIC DISTRIBUTION SYSTEM

The Electric System provides electric service throughout Lewis County with the exception of the City of Centralia who is served by the City's Municipal Light and Power Department. Currently, the District serves 31,840 customer connections within approximately 2,530 square miles comprising 2,912 miles of distribution line and services. Power supplies are primarily provided to the District through purchase power contracts with Bonneville Power Administration (BPA). Weather and economic climate are the primary conditions that influence electricity sales. Generally, extreme temperatures increase sales to customers who use electricity for cooling and heating, while moderate temperatures produce moderate sales. Seasonal influences exist from industrial customers that are related to agriculture products peaking during the District's summer months in contrast to residential customers peaking during the winter months from heating. Economic conditions have shown slight, but steady improvements in Lewis County over the past couple of years.



Financial Summary and Analysis

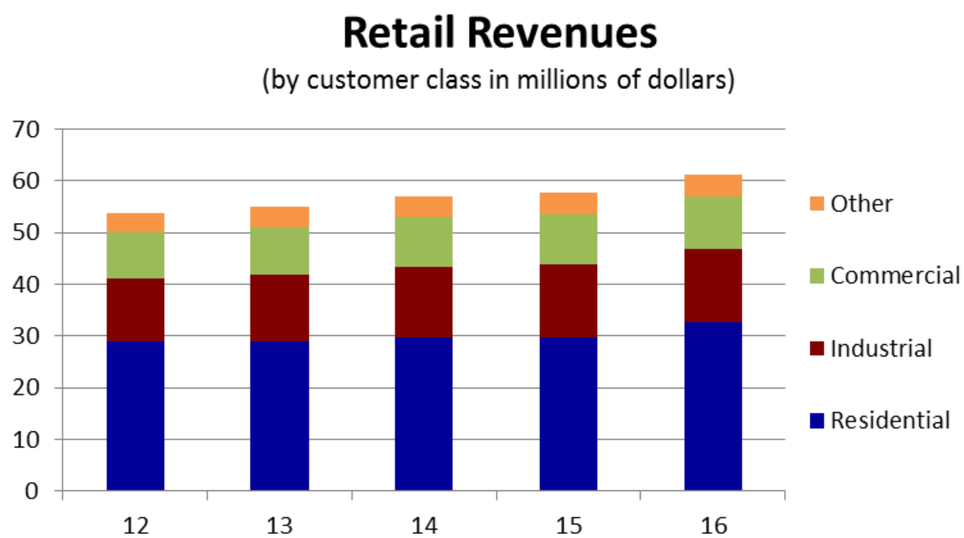
During 2016, the Electric System's net operating loss before other revenues (expenses) and contributed capital was $304,810, which was a change of $1.56 million from 2015. The factors influencing these results in 2016 include:

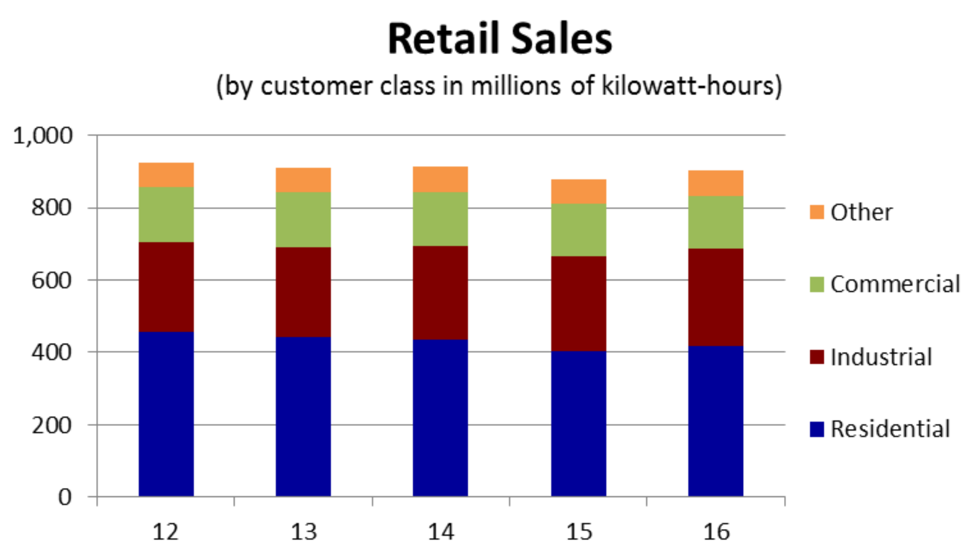
- Total operating revenues increased by $4.63 million or 7.3%.
  - Revenues from sales to customers increased $3.51 million or 6.1% due to the rate increase effective May 2015, and a 2.6% increase in kilowatt hours sold.
  - Revenues from wholesale decreased $258,800 or 6.1% due to low wholesale prices.
  - Other operating revenues increased $5,600 or 0.2%
  - The Board of Commissioners approved the transfer of $92,590 to the rate stabilization account, a decrease of $1.37 million.

- Total operating expenses increased by $3.07 million or 4.7%.
    - Purchase power expense increased by $1.79 million or 4.1% primarily due to increased BPA expenses.
    - Other operating expense increased by $903,200 or 10.1% primarily due to increased wheeling, distribution and administrative expenses.
    - Maintenance expense increased by $57,200 or 1.4% primarily due to increased transmission line maintenance.
    - Depreciation expense increased by $118,100 or 2.8% as a result of capital additions.
    - Taxes increased by $202,400 or 4.8% primarily as a result of higher retail sales.

Selected Financial Data

	(in thousands)		
	2016	2015	2014
			as restated
Operating revenues	$ 67,545	$ 62,917	$ 66,233
Operating expenses	67,850	64,784	65,587
Net operating revenues	(305)	(1,867)	646
Other revenues (expenses) and contributed capital	(50)	(366)	(614)
Change in net position	$ (355)	$ (2,233)	$ 32
Total assets and deferred outflows	$ 171,855	$ 172,297	$ 173,591
Total liabilities and deferred inflows	49,848	49,936	48,996
Net investment in capital assets	120,873	120,332	117,447
Unrestricted net position	(306)	856	5,986
Restricted for debt service	440	172	162
Restricted - other	1,000	1,000	1,000


Retail Revenues
(by customer class in millions of dollars)
70
60
50
40
30
20
10
0
12
13
14
15
16
Other
Commercial
Industrial
Residential


Retail Sales
(by customer class in millions of kilowatt-hours)
1,000
800
600
400
200
0
12
13
14
15
16
Other
Commercial
Industrial
Residential

Capital Asset and Long–Term Debt Activity

As of December 31, 2016, the Electric System had $177.3 million invested in a variety of capital assets in service. This represents an increase of $3.2 million or 1.8% from 2015. As of December 31, 2015, the Electric System had $174.1 million invested in a variety of capital assets in service. This represents an increase of $4.5 million or 2.7% from 2014. Capital construction is provided for through a combination of construction fees and cash flow from revenues, and represents normal additions to the system.

	(in thousands)		
	2016	2015	2014
Intangible and land	$ 4,957	$ 4,953	$ 4,944
Distribution plant	123,743	121,358	118,097
Transmission plant	22,918	22,957	22,536
Hydraulic plant	1,180	1,180	1,180
General plant	24,585	23,639	22,821
Total plant in service	$ 177,383	$ 174,087	$ 169,578

In December 2016, $20.602 million in Electric System Revenue Refunding Bonds were issued to advance refund all of the outstanding Revenue Bonds, Series 2008A. In 2016, revenue bonds outstanding were $25.877 million, which is a decrease of $757,600 or 2.8% from 2015. In 2015, revenue bonds outstanding were $26.635 million, which is a decrease of $1.85 million or 6.5% from 2014.

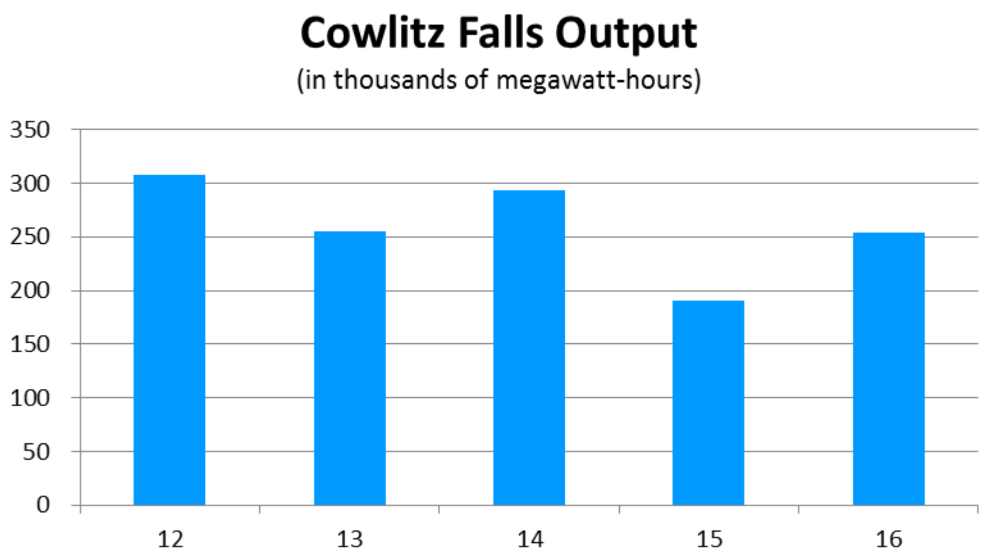
Power Supply

The District signed a 20-year Block and Slice Power Agreement with BPA on December 1, 2008, with the contract taking effect on October 1, 2011. The District also purchases wind power in order to comply with Initiative 937 renewable resources requirements.

COWLITZ FALLS HYDROELECTRIC GENERATION PROJECT

The District operates the Cowlitz Falls Project (System or Project) located on the upper Cowlitz River in eastern Lewis County. The powerhouse contains two Kaplan turbine generating units with net installed capacity of 35 MW each. Average annual generation is estimated at 265 million kilowatt hours.

Project operation depends upon the "run of the river" to produce the maximum amount of electric energy. Generation output in 2016 rebounded to slightly less than average after 2015 was negatively impacted by a low water year and the scheduled two month reservoir drawdown associated with the construction of the North Shore Collector.



Financial Summary and Analysis

Revenues for the Cowlitz Falls Project are recognized on the basis of the Amendatory Power Purchase Contract between the District and BPA. Through this contract, BPA receives all output from the Cowlitz Falls Project in exchange for payment of all operation and maintenance costs and debt service on the Cowlitz Falls Project revenue bonds.

Selected Financial Data

	(in thousands) 2016	2015	2014
Operating revenues	$ 10,801	$ 10,285	$ 10,519
Operating expenses	7,257	6,518	6,678
Net operating revenues	3,544	3,767	3,841
Other expenses	3,544	3,767	3,841
Change in net position	$ -	$ -	$ -
Total assets and deferred outflows	$ 93,138	$ 97,757	$ 100,658
Total liabilities and deferred inflows	93,138	97,757	100,658
Net position	-	-	-

Capital Assets and Long-Term Debt Activity

Capital invested in plant was $158.2 million and plant net of depreciation was $84.4 million in 2016. Total Cowlitz Falls Project plant in service as of December 31, 2016, 2015 and 2014 consisted of the following:

	(in thousands)		
	2016	2015	2014
Production plant	$ 155,392	$ 155,392	$ 155,392
Transmission plant	2,192	2,192	2,175
General plant	623	563	563
Total plant in service	$ 158,207	$ 158,147	$ 158,130

In 2016, revenue bonds outstanding were $78.905 million, which is a decrease of $3.15 million or 3.8% from 2015. In 2015, revenue bonds outstanding were $82.055 million, which is a decrease of $3.0 million or 3.5% from 2014.

Requests for Information

The basic financial statements, notes, and management's discussion and analysis are designed to provide a general overview of the District's finances. Questions concerning any of the information provided in this report should be directed to the District at 321 NW Pacific Ave, Chehalis, WA 98532.

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PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
STATEMENT OF NET POSITION

	Electric System	Cowlitz Falls System	December 31, 2016 Combined	December 31, 2015 Combined
CURRENT ASSETS				
Cash and cash equivalents	$ 7,984,966	$ 2,627,644	$ 10,612,610	$ 12,291,240
Customer and other receivables, net	10,154,438	1,828,314	11,982,752	11,609,435
Inventories	2,727,855	-	2,727,855	3,070,495
Other current assets	188,809	-	188,809	156,548
Current portion of prepaid power and attributes	1,889,538	-	1,889,538	1,889,538
Total current assets	22,945,606	4,455,958	27,401,564	29,017,256
RESTRICTED ASSETS				
Cash and cash equivalents –				
Debt service fund	462,976	-	462,976	285,161
Major catastrophe fund	1,000,000	-	1,000,000	1,000,000
Rate stabilization	4,159,825	-	4,159,825	4,067,235
Total restricted assets	5,622,801	-	5,622,801	5,352,396
UTILITY PLANT				
Utility plant in service	177,383,063	158,207,960	335,591,023	332,235,000
Construction in progress	4,722,014	-	4,722,014	4,431,068
Total utility plant	182,105,077	158,207,960	340,313,037	336,666,068
Less accumulated depreciation	61,231,787	73,771,445	135,003,232	128,616,427
Net utility plant	120,873,290	84,436,515	205,309,805	208,049,641
OTHER ASSETS				
Conservation loans	129,041	-	129,041	129,087
Derivative asset	238,361	-	238,361	403,842
Unamortized prepaid power and attributes	18,895,384	-	18,895,384	20,784,923
Regulatory asset - issuance costs	83,475	660,504	743,979	1,076,478
Total other assets	19,346,261	660,504	20,006,765	22,394,330
DEFERRED OUTFLOWS OF RESOURCES				
Accumulated decrease in fair value of hedging derivatives	245,854	-	245,854	104,432
Pension	1,772,465	196,962	1,969,427	1,221,116
Deferred loss on refunding	1,048,628	3,387,758	4,436,386	3,914,952
Total deferred outflow of resources	3,066,947	3,584,720	6,651,667	5,240,500
Total assets and deferred outflows of resources	$ 171,854,905	$ 93,137,697	$ 264,992,602	$ 270,054,123

See accompanying notes.

			December 31,	
	Electric System	Cowlitz Falls System	2016 Combined	2015 Combined
CURRENT LIABILITIES				
Accounts payable	$ 828,722	$ 898,460	$ 1,727,182	$ 1,244,623
Accrued liabilities	6,911,123	290,134	7,201,257	7,073,727
Accrued bond interest	23,386	997,978	1,021,364	1,150,096
Accrued OPEB liability	514,126	53,969	568,095	531,507
Operations and maintenance advance	-	2,206,180	2,206,180	3,338,544
Customer deposits	1,593,635	-	1,593,635	1,527,295
Current maturities of long-term debt	5,275,000	3,310,000	8,585,000	5,095,000
Total current liabilities	15,145,992	7,756,721	22,902,713	19,960,792
LONG-TERM DEBT				
Revenue bonds, net of current portion	20,602,385	75,595,000	96,197,385	103,595,000
Unamortized premium	-	8,765,858	8,765,858	10,213,539
Total long-term debt	20,602,385	84,360,858	104,963,243	113,808,539
OTHER LIABILITIES				
Other credits	293,096	8,429	301,525	67,738
Net pension liability	9,000,575	993,783	9,994,358	8,040,499
Derivative liability	245,854	-	245,854	104,432
Total liabilities	45,287,902	93,119,791	138,407,693	141,982,000
DEFERRED INFLOWS OF RESOURCES				
Accumulated increase in fair value of hedging derivatives	238,361	-	238,361	403,842
Pension	162,180	17,906	180,086	1,239,737
Regulatory liability - rate stabilization	4,159,825	-	4,159,825	4,067,235
Total deferred inflows of resources	4,560,366	17,906	4,578,272	5,710,814
NET POSITION				
Net investment in capital assets	120,873,290	153,415	121,026,705	120,167,414
Restricted:				
Debt service	439,590	-	439,590	172,418
Other	1,000,000	-	1,000,000	1,000,000
Unrestricted	(306,243)	(153,415)	(459,658)	1,021,477
Total net position	122,006,637	-	122,006,637	122,361,309
Total net position, liabilities, and deferred inflows of resources	$ 171,854,905	$ 93,137,697	$ 264,992,602	$ 270,054,123

PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

	Electric System	Cowlitz Falls System	Years Ended December 31, 2016 Combined	2015 Combined
OPERATING REVENUES				
Retail sales – electric energy	$ 61,183,659	$ 10,801,049	$ 71,984,708	$ 67,955,444
Wholesale – wind and attributes	3,994,309	-	3,994,309	4,253,116
Transfer from/(to) rate stabilization	(92,590)	-	(92,590)	(1,460,097)
Other operating revenues	2,460,054	-	2,460,054	2,454,418
Total operating revenues	67,545,432	10,801,049	78,346,481	73,202,881
OPERATING EXPENSES				
Power supply	45,084,063	-	45,084,063	43,299,249
Other operating	9,847,279	2,271,336	12,118,615	10,903,300
Maintenance	4,236,239	1,505,405	5,741,644	5,541,098
Depreciation	4,285,598	3,349,548	7,635,146	7,251,163
Taxes	4,397,063	130,862	4,527,925	4,308,119
Total operating expenses	67,850,242	7,257,151	75,107,393	71,302,929
NET OPERATING INCOME (LOSS)	(304,810)	3,543,898	3,239,088	1,899,952
OTHER REVENUES (EXPENSES)				
Interest income	27,094	4,138	31,232	44,359
Interest expense	(1,265,933)	(4,110,038)	(5,375,971)	(5,700,801)
Amortization of debt expense, premium, and loss on refunding	10,217	375,561	385,778	398,021
Revenue from merchandising	163,603	-	163,603	233,628
Expense of contract work	(147,972)	-	(147,972)	(210,558)
Other income	342,604	186,441	529,045	547,323
Total other expenses	(870,387)	(3,543,898)	(4,414,285)	(4,688,028)
NET LOSS	(1,175,197)	-	(1,175,197)	(2,788,076)
Contributed capital	820,525	-	820,525	554,688
CHANGE IN NET POSITION	(354,672)	-	(354,672)	(2,233,388)
NET POSITION, beginning of year	122,361,309	-	122,361,309	124,594,697
NET POSITION, end of year	$ 122,006,637	$ -	$ 122,006,637	$ 122,361,309

See accompanying notes.

PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
STATEMENT OF CASH FLOWS

	Electric System	Cowlitz Falls System	Year Ended December 31, 2016 Combined	2015 Combined
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash received from customers	$ 67,233,941	$ 9,765,789	$ 76,999,730	$ 74,546,599
Cash paid to suppliers	(47,677,728)	(2,108,715)	(49,786,443)	(46,671,784)
Cash paid to employees	(9,074,403)	(1,051,053)	(10,125,456)	(9,930,915)
Cash paid for taxes	(4,397,063)	(139,216)	(4,536,279)	(4,094,779)
Net cash from operating activities	6,084,747	6,466,805	12,551,552	13,849,121
CASH FLOWS FROM INVESTING ACTIVITIES				
Interest and dividends on investments	27,094	4,138	31,232	44,359
Net conservation loan activity	46	-	46	(15,424)
Net other income	358,235	186,441	544,676	570,393
Net cash from investing activities	385,375	190,579	575,954	599,328
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Payments on debt	(1,806,243)	-	(1,806,243)	(1,850,000)
Interest paid on bonds	(1,355,290)	-	(1,355,290)	(1,446,704)
Net cash from noncapital financing activities	(3,161,533)	-	(3,161,533)	(3,296,704)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Utility plant additions, net of cost of removal and salvage proceeds	(4,826,440)	(68,870)	(4,895,310)	(7,894,714)
Contributed capital	820,525	-	820,525	554,688
Principal paid on bonds	-	(3,150,000)	(3,150,000)	(3,000,000)
Interest paid on bonds	-	(4,149,413)	(4,149,413)	(4,299,413)
Net cash from capital and related financing activities	(4,005,915)	(7,368,283)	(11,374,198)	(14,639,439)
CHANGE IN CASH AND CASH EQUIVALENTS	(697,326)	(710,899)	(1,408,225)	(3,487,694)
CASH AND CASH EQUIVALENTS, beginning of year	14,305,093	3,338,543	17,643,636	21,131,330
CASH AND CASH EQUIVALENTS, end of year	$ 13,607,767	$ 2,627,644	$ 16,235,411	$ 17,643,636
CASH FLOWS FROM OPERATING ACTIVITIES				
Net operating revenues	$ (304,810)	$ 3,543,898	$ 3,239,088	$ 1,899,952
Adjustments to reconcile net operating revenues to net cash from operating activities				
Depreciation	4,285,598	3,349,548	7,635,146	7,251,163
Pension related items	(35,826)	(20,487)	(56,313)	998,447
Amortization of prepaid power and attributes	1,889,539	-	1,889,539	1,889,539
Change in assets and liabilities				
Receivables	(470,421)	97,104	(373,317)	(953,162)
Other current assets	(32,261)	-	(32,261)	19,682
Accounts payable and warrants outstanding	(148,839)	631,398	482,559	377,513
Accrued liabilities	123,314	4,216	127,530	198,229
Accrued OPEB liability	33,112	3,476	36,588	22,736
Inventories	342,640	-	342,640	(122,085)
Operations and maintenance advance	-	(1,132,364)	(1,132,364)	791,223
Customer deposits	66,340	-	66,340	45,560
Regulatory liability - rate stabilization	92,590	-	92,590	1,460,097
Deferred credits	243,771	(9,984)	233,787	(29,773)
Net cash from operating activities	$ 6,084,747	$ 6,466,805	$ 12,551,552	$ 13,849,121

See accompanying notes.

Note 1 – Nature of Organization and Operations

Public Utility District No. 1 of Lewis County (the District) is a municipal corporation of the State of Washington and is governed by an elected three member board. The District was organized in 1936, pursuant to a general election in accordance with the Enabling Act, and commenced its operations in 1939. The District has its administrative offices in Chehalis, Washington, which is located in southwestern Washington.

The District manages and operates two systems: Electric Distribution System (Electric System) and the Cowlitz Falls Hydroelectric Generation Project (Cowlitz Falls System or Project). The Electric System provides electric service to substantially all of Lewis County, except for the City of Centralia. The District constructed and, beginning in June 1994, operates the Cowlitz Falls Hydroelectric Dam on the upper Cowlitz River in eastern Lewis County, Washington (see Note 8). The Electric System and Cowlitz Falls System are separate operating systems.

Note 2 – Summary of Significant Accounting Policies

Reporting entity – In evaluating how to define the government, for financial reporting purposes, management has considered the District's financial reporting entity. The financial reporting entity consists of the District and component units. Component units are legally separate organizations for which the District is financially accountable and other organizations for which the District is not accountable but for which the nature and significance of their relationship with the District are such that the exclusion would cause the District's financial statements to be misleading or incomplete. Based upon this criterion, the District has no component units.

Basis of accounting and presentation – The District is considered an enterprise and operates as a proprietary fund. The financial statements of the District have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The District has applied all applicable Governmental Accounting Standards Board (GASB) pronouncements.

The Uniform System of Accounts, as prescribed by the Federal Energy Regulatory Commission (FERC), is the basis for the District's accounting policies. The accounting records of the District are maintained in accordance with methods prescribed by the State Auditor under authority of Chapter 43.09 RCW.

The accompanying financial statements include the individual and combined statements of financial position of the Electric System and Cowlitz Falls System and the results of operations and cash flows for each system.

Concentration of credit risk – The District's financial instruments that are exposed to concentrations of credit risk consist primarily of cash, temporary investments and receivables.

Note 2 – Summary of Significant Accounting Policies (continued)

The District maintains its cash and temporary investments in bank deposit accounts which exceed federally insured limits. However, all deposits are made with state-approved depositories and are protected under the State's Public Deposit Protection Commission (PDPC).

Credit is extended to customers generally without collateral requirements, however, deposits are obtained from certain customers and formal shut-off procedures are in place.

Utility plant – Utility plant assets are stated at cost (see Note 4). Cost includes contracted services, direct labor and materials, interest capitalized during construction, and certain overhead items. For the Electric System, the provision for depreciation is determined by the straight-line method over the estimated useful lives of the assets (as specified by FERC for utility plant) ranging from three to fifty years. The cost of maintenance and repairs is expensed as incurred; renewals, replacements and betterments are capitalized. Capitalization threshold is $1,000. For the Cowlitz Falls Project, depreciation, renewals, and replacements are recognized on the basis of the Amendatory Power Purchase Contract between the District and BPA (see Note 8).

The actual or average cost of property replaced or renewed is removed from utility plant and such cost plus removal cost less salvage is charged to accumulated depreciation.

Cash equivalents – The District considers all highly liquid investments, including restricted cash, with a maturity of three months or less to be cash equivalents.

Restricted cash and investments – Restricted cash and investments consist of Board restricted funds set aside and invested by the District in a major catastrophe fund, rate stabilization account and investments restricted by bond resolution. The major catastrophe fund balance provides the District with emergency funds should the District face a catastrophe, such as a major wind storm or other extraordinary event.

Customer and other receivables – Accounts receivable are recorded when invoices are issued and are written off when they are determined to be uncollectible. The allowance for doubtful accounts is estimated based on the District's historical losses, review of specific problem accounts, the existing economic conditions, and the financial stability of its customers. Generally, the District considers accounts receivable past due after 30 days. The allowance for doubtful accounts for the Electric System was $416,353 and $405,918 at December 31, 2016 and 2015, respectively. No allowance was deemed necessary for the Cowlitz Falls System.

Inventories – Inventories consist primarily of materials and supplies for construction and maintenance of utility plant and are valued at the lower of average cost or market.

Note 2 – Summary of Significant Accounting Policies (continued)

Unamortized bond premiums and loss on refunding – Bond premiums relating to revenue bonds are amortized by the effective interest method over the life of bond issues using a weighted average of the face amount of bonds outstanding. Losses on refunding are amortized over the life of the old or new bonds, whichever is shorter. These amounts are recorded as deferred outflow of resources on the statement of net position.

Regulatory assets – unamortized bond issue costs – Unamortized bond issue costs represent the remaining expense related to various debt issuances. The asset is amortized over the duration of the related debt and recognition of these costs is included in the rate making process.

Deferred inflow of resources – The District has deferred revenues to be recognized in future periods in accordance with regulatory accounting requirements. The Board authorized the transfer of $92,590 and $1,460,097 from operating revenues to the rate stabilization account for 2016 and 2015, respectively. Future withdrawals from the rate stabilization account will be used to mitigate potential rate increases or provide for unexpected expenses.

Unamortized prepaid power and attributes – Consists of prepaid power and attributes amortized using the straight-line method over the life of the 2008 Series bonds (see Note 6 – White Creek Wind Project).

Compensated absences – The District accrues accumulated unpaid personal leave benefits as the obligation is incurred. The accrued liability for unpaid personal leave at December 31, 2016 and 2015 was $1,660,053 and $1,546,244, respectively. Employees covered by PERS I (see Note 5) are entitled to, upon retirement, the use of up to 60 days of unused personal leave for calculation of retirement benefits. PERS actuarially determines the cost for these additional benefits and bills the District for a portion of them on a one-time basis. These additional costs do not materially affect the District's financial statements. Eligible sick leave balances, meeting certain requirements, may either be converted to personal leave according to a schedule or a percent may be cashed out upon retirement.

Operations and maintenance advance – Operations and maintenance advance represents unspent BPA operation and maintenance advances recognized in accordance with the Amendatory Power Purchase Contract with BPA (see Note 8).

Customer deposits – The District requires deposits from certain customers upon request for service. The customer deposits are held to defray potential uncollected accounts and other contingencies. The deposits are refundable under certain circumstances.

Note 2 – Summary of Significant Accounting Policies (continued)

Net position – Net position consists primarily of cumulative net income (loss) collected for the payment of utility plant in advance of net accumulated depreciation recognized on such plant. It is the District's intention to set rates at a level to continue replacing and improving net utility plant. Net position consists of the following components:

- **Net investment in capital assets** – This component of net position consists of capital assets, net of accumulated depreciation, less outstanding balances of any debt borrowings that are attributable to the acquisition, construction or improvement of those assets.
- **Restricted** – This component of net position consists of assets restricted by bond resolutions and assets restricted by Board resolution.
- **Unrestricted** – This component of net position consists of net position that does not meet the definition of "net investment in capital assets" or "restricted."

Revenue recognition – The District recognizes Electric System revenue as earned. Substantially all residential and small commercial customers are billed bimonthly while large commercial and industrial customers are billed monthly. The District utilizes cycle billing and records revenue billed to its customers when the meters are read. In addition, the District recognizes unbilled revenue, revenues from electric power delivered but not yet billed. At December 31, 2016 and 2015, unbilled revenue was $4,395,394 and $3,724,850, respectively and included in customer and other receivables. Revenues for the Cowlitz Falls Project are recognized on the basis of the Amendatory Power Purchase Contract between the District and BPA (see Note 8).

Contributed capital – Consists of cash contributions received from customers for the construction of utility plant.

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

Derivative instruments – The District has adopted GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. Subject to certain exceptions, GASB Statement No. 53 requires every derivative instrument be recorded on the statement of net position as an asset or liability measured at its fair value, and changes in the derivative's fair value be recognized 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."

Note 2 – Summary of Significant Accounting Policies (continued)

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, and do not generally meet the "normal purchases and normal sales" criteria (see Note 7).

Fair value measurement - In February 2015, the GASB issued Statement No. 72, Fair Value Measurement and Application, effective for financial statements for years beginning after June 15, 2015. This statement clarifies the definition of fair value, establishes general principles for measuring fair value, provides additional fair value application guidance, and enhances disclosures about fair value measurements.

In accordance with GASB 72, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price). Fair value is a market-based measurement for a particular asset or liability based on assumptions that market participants would use in pricing the asset or liability.
Note 2 - Summary of Significant Accounting Policies (continued)

Valuation inputs are assumptions that market participants use in pricing an asset or liability. The hierarchy of inputs used to generate the valuation is classified into three different Levels:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities at the measurement date.
- Level 2 inputs include quoted prices for similar assets or liabilities in markets that are active; quoted prices for identical or similar assets or liabilities in markets that are not active; and inputs other than quoted prices that are observable for an asset, either directly or indirectly.
- Level 3 inputs are unobservable inputs from the asset or liability where there is very little market activity and they should be used only when relevant Level 1 and Level 2 inputs are unavailable.

Fair value measurements are performed on a recurring basis. The fair values of swap contracts as of December 31, 2016, were based on the future price curve for the Mid-Columbia Intercontinental Exchange for electricity. The observability of inputs used to perform the measurement results in the swap fair values being categorized as Level 2 on the fair value hierarchy.

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.

Note 3 – Cash Equivalents

The District's investment policies allow for investments in bank certificates of deposit of commercial banks as approved by the State of Washington Public Deposit Protection Commission, or in U.S. Government securities that can be liquidated should it be necessary. Any U.S. Government security purchased shall be purchased through commercial banks qualified as public depositories. All investments shall mature in such amounts and at such times as is anticipated by the District that such moneys will be either reinvested or required to pay District costs. The primary concern of the District shall be the safety of the principal.

The District's deposits and certificates of deposit are entirely covered by Federal Depository Insurance Corporation (FDIC) or held by state-approved depositaries protected under the Commission.

Custodial credit risk is that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. All of the aforementioned cash is held in the District's name by a third–party custodian.

Note 4 – Utility Plant

Capital assets are defined by the District as assets with initial individual cost of more than $1,000 and an estimated useful life in excess of one year.

Utility plant activity for the year ended December 31, 2016 is as follows:

	Balance December 31, 2015	Additions	Retirements	Balance December 31, 2016
ELECTRIC SYSTEM				
Utility plant not being depreciated				
Land	$ 4,831,719	$ 4,508	$ -	$ 4,836,227
Construction in progress	4,431,068	4,256,201	3,965,255	4,722,014
Intangible	121,133	-	-	121,133
Total utility plant not being depreciated	9,383,920	4,260,709	3,965,255	9,679,374
Utility plant being depreciated				
Distribution system	121,357,972	3,602,983	1,218,290	123,742,665
Transmission system	22,957,561	14,667	53,852	22,918,376
Hydraulic system	1,179,530	-	-	1,179,530
General plant	23,639,260	1,048,454	102,582	24,585,132
Total utility plant being depreciated	169,134,323	4,666,104	1,374,724	172,425,703
Less accumulated depreciation for:				
Distribution system	41,139,403	3,238,314	1,515,844	42,861,873
Transmission system	6,635,519	511,260	79,973	7,066,806
Hydraulic system	659,972	20,141	-	680,113
General plant	9,750,901	921,323	49,229	10,622,995
Total accumulated depreciation	58,185,795	4,691,038	1,645,046	61,231,787
Total utility plant being depreciated, net	110,948,528			111,193,916
Total utility plant, net	$ 120,332,448			$ 120,873,290
COWLITZ FALLS SYSTEM GENERATION				
Utility plant not being depreciated				
Land	$ 7,483,000	$ -	$ -	$ 7,483,000
Utility plant being depreciated				
Hydraulic system	148,212,624	-	-	148,212,624
Transmission system	1,889,088	-	-	1,889,088
General plant	563,110	85,360	25,224	623,246
Total plant being depreciated	150,664,822	85,360	25,224	150,724,958
Less accumulated depreciation				
Hydraulic system	70,215,531	3,329,032	-	73,544,563
Transmission system	160,532	9,777	-	170,309
General plant	54,566	2,005	-	56,571
Total accumulated depreciation	70,430,629	3,340,814	-	73,771,443
Total plant being depreciated, net	80,234,193			76,953,515
Total plant, net	$ 87,717,193			$ 84,436,515

Note 4 – Utility Plant (continued)

Utility plant activity for the year ended December 31, 2015 is as follows:

	Balance December 31, 2014	Additions	Retirements	Balance December 31, 2015
ELECTRIC SYSTEM				
Utility plant not being depreciated				
Land	$ 4,822,998	$ 8,721	$ -	$ 4,831,719
Construction in progress	3,124,079	6,278,728	4,971,739	4,431,068
Intangible	121,133	-	-	121,133
Total utility plant not being depreciated	8,068,210	6,287,449	4,971,739	9,383,920
Utility plant being depreciated				
Distribution system	118,096,943	4,015,460	754,431	121,357,972
Transmission system	22,535,950	618,114	196,503	22,957,561
Hydraulic system	1,179,530	-	-	1,179,530
General plant	22,821,548	1,146,807	329,095	23,639,260
Total utility plant being depreciated	164,633,971	5,780,381	1,280,029	169,134,323
Less accumulated depreciation for:				
Distribution system	39,050,038	3,148,164	1,058,799	41,139,403
Transmission system	6,343,540	502,215	210,236	6,635,519
Hydraulic system	639,831	20,141	-	659,972
General plant	9,221,913	858,083	329,095	9,750,901
Total accumulated depreciation	55,255,322	4,528,603	1,598,130	58,185,795
Total utility plant being depreciated, net	109,378,649			110,948,528
Total utility plant, net	$ 117,446,859			$ 120,332,448
COWLITZ FALLS SYSTEM GENERATION				
Utility plant not being depreciated				
Land	$ 7,483,000	$ -	$ -	$ 7,483,000
Utility plant being depreciated				
Hydraulic system	148,212,624	-	-	148,212,624
Transmission system	1,871,394	40,790	23,096	1,889,088
General plant	563,110	-	-	563,110
Total plant being depreciated	150,647,128	40,790	23,096	150,664,822
Less accumulated depreciation				
Hydraulic system	67,151,243	3,064,288	-	70,215,531
Transmission system	150,755	9,777	-	160,532
General plant	52,561	2,005	-	54,566
Total accumulated depreciation	67,354,559	3,076,070	-	70,430,629
Total plant being depreciated, net	83,292,569			80,234,193
Total plant, net	$ 90,775,569			$ 87,717,193

Note 5 – Pension Plans and Other Post-Employment Benefit Plans

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

	Aggregate Pension Amounts	
	2016	2015
Pension liabilities	$ 9,994,358	$ 8,040,499
Deferred outflows of resources	1,969,427	1,221,116
Deferred inflows of resources	180,086	1,239,737
Pension expense	1,265,535	1,132,956

State sponsored pension plans – Substantially all 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.

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.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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:

	PERS Plan 1 Actual Contribution Rates	
	Employer	Employee
January through December 2016	11.18%	6.00%
July through December 2015	11.18%	6.00%
January through June 2015	9.21%	6.00%

The District's actual contributions to the plan UAAL were $485,516 and $416,345 for the years ended December 31, 2016 and 2015, respectively.

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.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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 and 2015 were as follows:

	PERS Plan 2/3 Actual Contribution Rates	
	Employer 2/3	Employee 2
January through December 2016	11.18%	6.12%
Employee PERS Plan 3		varies
July through December 2015	11.18%	6.12%
January through June 2015	9.21%	4.92%
Employee PERS Plan 3		varies

The District's actual contributions to the plan, excluding the Plan 1 UAAL component, were $634,122 and $534,503 for the years ended December 31, 2016 and 2015, respectively.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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.

- The OSA updated demographic assumptions, consistent with the changes from the *2007-2012 Experience Study Report*, used when valuing the PERS 1 and TERS 1 Basic Minimum COLA.
- The OSA corrected how valuation software calculates a member's entry age under the entry age normal actuarial cost method. Previously, the funding age was rounded, resulting in an entry age one year higher in some cases.
- For purposes of calculating the Plan 2/3 Entry Age Normal Cost contribution rates, the OSA now uses the current blend of Plan 2 and Plan 3 salaries rather than using a long-term membership assumption of two-thirds Plan 2 members and one-third Plan 3 members.
- The OSA changed the way it applies salary limits, as described in the *2007-2012 Experience Study Report*.

Discount rate – The discount rate used to measure the total pension liability for all DRS plans was 7.5 percent.

To determine that rate, an asset sufficiency test included an assumed 7.7 percent long-term discount rate to determine funding liabilities for calculating future contribution rate requirements.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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 and 2015, are summarized in the table below. The inflation component used to create the table is 2.2 percent and represents the WSIB's most recent long-term estimate of broad economic inflation.

Asset Class	Target Allocation	% Long-Term Expected Real Rate of Return Arithmetic	
		2016	2015
Fixed income	20%	1.70%	1.70%
Tangible assets	5%	4.40%	4.40%
Real estate	15%	5.80%	5.80%
Global equity	37%	6.60%	6.60%
Private equity	23%	9.60%	9.60%
	100%		

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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.

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
PERS 1	$ 5,473,725	$ 4,539,122	$ 3,737,839
PERS 2/3	$ 10,044,071	$ 5,455,236	$ (2,839,765)

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, pension expense, and deferred outflows of resources and deferred inflows of resources related to pensions – At June 30, 2016 and 2015, the District reported the following total pension liability:

	2016	2015
PERS 1	$ 4,539,122	$ 4,271,996
PERS 2/3	5,455,236	3,768,503
	$ 9,994,358	$ 8,040,499

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

	Proportionate Share June 30, 2015	Proportionate Share June 30, 2016	Change in Proportion
PERS 1	0.081668%	0.084520%	0.002852%
PERS 2/3	0.105470%	0.108348%	0.002878%

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.*

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

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

Pension expense – For the years ended December 31, 2016 and 2015, the District recognized $1,265,535 and $1,132,956, respectively, of pension expense.

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:

	Deferred Outflows of Resources	Deferred Inflows of Resources
PERS 1		
Differences between expected and actual experience	$ -	$ -
Net difference between projected and actual investment earnings on pension plan investments	114,288	-
Changes of assumptions	-	-
Changes in proportion and differences between contributions and proportionate share of contributions	-	-
Contributions subsequent to the measurement date	242,548	-
Total	$ 356,836	$ -
PERS 2/3		
Differences between expected and actual experience	$ 290,487	$ 180,086
Net difference between projected and actual investment earnings on pension plan investments	667,563	-
Changes of assumptions	56,384	-
Changes in proportion and differences between contributions and proportionate share of contributions	281,370	-
Contributions subsequent to the measurement date	316,787	-
Total	$ 1,612,591	$ 180,086
Combined PERS 1 and PERS 2/3		
Differences between expected and actual experience	$ 290,487	$ 180,086
Net difference between projected and actual investment earnings on pension plan investments	781,851	-
Changes of assumptions	56,384	-
Changes in proportion and differences between contributions and proportionate share of contributions	281,370	
Contributions subsequent to the measurement date	559,335	-
Total	$ 1,969,427	$ 180,086

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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

		PERS 1
Year ended December 31,	2017	$ (28,140)
	2018	(28,140)
	2019	104,961
	2020	65,607

		PERS 2/3
Year ended December 31,	2017	$ 111,546
	2018	111,546
	2019	570,566
	2020	322,060

Deferred compensation plan – The District maintains a deferred compensation plan (Internal Revenue Code Section 457) for all eligible employees. The plan is entirely funded by voluntary employee contributions. The District has entered into a contractual relationship with the State of Washington Deferred Compensation Program placing all plan assets into trust for the exclusive benefit of participants and their beneficiaries.

Post-Retirement Benefits Plan Other than Pensions Plan (OPEB) description – The District provides post-retirement health care benefits for retired employees until age 65. Prior to April 1, 2008, these benefits paid for 97% of the medical premiums of retirees through age 65. Effective April 1, 2008 the District pays 95% of the medical premiums of retirees up to the age of 65. Spouses and dependents of retirees' benefits are not paid under the plan but can access the plan on a self-pay basis. Employees that retire with disability retirement under Washington State PERS may continue their health insurance coverage through the District with the same coverage provisions as other retirees. Currently, 11 retirees and 106 active employees are covered under the plan.

Funding policy – The contribution requirements of plan participants are established by the District and may be amended from time to time. It is the District's intent to expense the actuarially determined OPEB cost annually.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

Annual OPEB cost – The District's annual OPEB cost is calculated based on the annual required contribution of the employer (ARC). The ARC is an amount actuarially determined, based on the entry age normal method, determined in accordance with the guidance of GASB Statement 45.

The ARC represents level funding, that if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial accrued liabilities over a period not to exceed thirty years. The District's estimated contributions for 2016 of $125,513 were less than the current year ARC of $162,101 and therefore, as of December 31, 2016, the District had an OPEB obligation of $568,095. The District's estimated contributions for 2015 of $141,173 were less than the current year ARC of $163,909 and therefore, as of December 31, 2015, the District had an OPEB obligation of $531,507.

Other actuarial assumptions include a rate of return on investments of present and future assets of 3.0%. The health care benefit rate is assumed to increase 9.0% in 2015, and then decreasing to 5.0% annually over 8 years and remaining at 5.0% thereafter. Dental premiums are assumed to increase by 3.0% in all future years.

The District's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2016, 2015 and 2014 were as follows:

Fiscal Year Ending	Annual OPEB Cost	Percentage of Annual OPEB Cost Funded	Net OPEB Obligation
December 31, 2016	$ 162,101	77.4%	$ 568,095
December 31, 2015	163,909	86.1%	531,507
December 31, 2014	166,182	82.8%	508,771

Funding status and funding progress – As of January 1, 2014, the most recent actuarial valuation date, the plan was not funded (0%). The actuarial accrued liability for benefits was $2.2 million, and the actuarial value of assets was zero, resulting in an unfunded actuarial accrued liability (UAAL) of $2.2 million.

The following table presents a schedule of funding progress for the District's OPEB Plan:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Entry Age Normal AAL (b)	UAAL (b – a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b – a) / c)
January 1, 2016	$ -	$ 2,272,420	$ 2,272,420	0%	$ 10,125,456	22%
January 1, 2015	-	2,251,301	2,251,301	0%	9,930,915	25%
January 1, 2014	-	2,227,272	2,227,272	0%	8,857,441	25%

Note 5 – Pension, Deferred Compensation Plan, and Post-Retirement Benefits (continued)

Actuarial valuations on an ongoing plan involve estimates of the value reported and assumptions about the probability of occurrence of events into the future. Examples include assumptions about future employment, composition of employees, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revisions as actual results are compared with past expectations and new estimates are made about the future.

Note 6 – Purchased Power Contracts

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 20-year Block and Slice Power Sale Agreement, which was signed on November 24, 2008, commenced on October 1, 2011, and extends through September 30, 2028. This contract provides federal power in the form of two products: Block and Slice. The monthly Block purchase amounts are fixed hourly values each month, but are shaped somewhat to closer align with the District's monthly power requirements. The non-Slice allocation or Block portion is 0.57954% for fiscal year 2016. The Slice product provides the District 0.96184% of the output of the federal system for fiscal year 2016.

BPA is required by federal law to recover all of its costs through the rates it charges its customers. BPA makes various filings with FERC to confirm that rates are sufficient to cover costs. Under BPA's adopted power and transmission rate provisions, its rates are subject to revision in order to enable BPA to recover its actual costs of service.

Beginning October 1, 2011, BPA changed its rate-making methodology to a tiered rate approach. Each public utility (preference) customer received a High Water Mark (HWM) based on either its 2010 load or average 2007-2008 loads 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. Both Block and Slice and non-Slice (Load Following) customers' HWMs are translated into "Tier 1 Cost Allocators" (TOCAs) which, when multiplied by the estimated costs of the federal system, determine their power costs. The District's TOCA for fiscal year 2017 and 2016 is 1.56427% and 1.54138%, respectively. There is an additional monthly load shaping charge (or credit) for the Block product, determined by the shape of customers' loads compared to the actual shape of the Federal Columbia River Power System (FCRPS). If preference customers want to buy more BPA power beyond their HWM, it will be sold at a BPA Tier 2 rate set to fully recover BPA's cost of securing additional resources to serve that customer's load. The customer also has the option of serving some or all of their above-HWM load with non-federal resources. The District elected not to purchase any Tier 2 products from BPA during the first purchase period, October 2011 through September 2014, or during the second purchase period, October 2014 through September 2019. The District has surplus energy, on average, over this time period.

Note 6 – Purchased Power Contracts (continued)

The rate provisions for the Block product include a Cost Recovery Adjustment Clause (CRAC) and a Dividend Distribution Clause (DDC). Either may be triggered if certain thresholds are met. The CRAC allows BPA to raise rates to collect sufficient funds to pay costs. The 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 Slice true-up mechanism.

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

Energy Northwest – The District is a member of Energy Northwest and a participant in Nuclear Project Nos. 1 and 3 (terminated projects), Columbia Generating Station, the Packwood Lake Hydroelectric Project, and the Nine Canyon Wind Project.

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 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 entered into "Net Billing Agreements" with Energy Northwest and the BPA. Under terms of these agreements, the District purchased a maximum of 1.276% of the capacity of Energy Northwest Nuclear Projects (WNP) 1, 2.274% of WNP 2 (now Columbia Generating Station) and 1.103% of Energy Northwest's 70% ownership share of WNP 3. The District in turn sold this capability to BPA. Under the "Net Billing Agreements," 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, including debt service on revenue bonds issued to finance the projects, whether or not the projects are completed, operable or operating and notwithstanding the suspension, reduction or curtailment of the projects' outputs. WNP 2 commenced commercial operation in December 1984. On November 19, 1984, the District withdrew its membership in Energy Northwest and participated in Energy Northwest Projects as a non-member for nearly 25 years. On April 27, 2009, the District approved a resolution to make application to become a member of Energy Northwest and the Energy Northwest Board approved the District's membership on July 23, 2009.

Note 6 – Purchased Power Contracts (continued)

Packwood Lake Hydroelectric Project – The District is a 14.25% 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 expired in 2010 and the Project has satisfied all of the requirements for relicensing with the Federal Energy Regulatory Commission and is waiting for final issuance. The participants' original Packwood Agreements with Energy Northwest obligated the 12 participants to pay annual costs and receive excess revenues. Energy Northwest recognizes revenues equal to expenses for each period. No net income 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 terms are similar to the original 1962 agreements, wherein the participants are obligated for a percentage of the Project costs. However, seven of the participants, including the District, began taking their share of the energy, and four participants with very small shares assigned theirs to Clallam PUD under separate bilateral contracts.

In addition the District and Energy Northwest have entered into a power transmission service agreement. The agreement, in exchange for providing transmission services to wheel Packwood Power from the Project to the BPA transmission system, provides for the District to receive monthly payments adjusted periodically for actual costs. Revenue amounted to $536,971 and $496,508 for the years ended 2016 and 2015, respectively.

Burton Creek Hydroelectric Project – The Burton Creek Hydroelectric Project is located near the east Lewis County town of Packwood. The project is a 560 KWh small hydro owned and operated by a private party. The District previously purchased the output of the Burton Creek Project under a power purchase agreement executed September 29, 2003, at the price of the District's average BPA priority firm monthly energy and demand rates.

The power purchase agreement extended from year to year unless terminated by either party with six months advance notice. Following the 2011 seasonal shutdown, Burton Creek Hydroelectric failed to resume sale and delivery of power. The District terminated the agreement on July 1, 2012 due to default of the sale and delivery obligation.

Not soon after the District terminated the above agreement, an individual notified the District that he had purchased the distressed FERC license for Burton Creek and had approximately one year to repair the facility and move certain Burton Creek components off Federal land and back onto private property. After the project received Qualifying Facility status, the District contracted to purchase the output of the Burton Creek Project effective October 1, 2013. The contract continues through December 31, 2018, unless otherwise terminated per terms in the agreement. Purchase prices are locked in each fall for the ensuing calendar year based on forward Northwest prices.

Note 6 – Purchased Power Contracts (continued)

Renewable Power Supply – 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. This Act mandates renewable energy and conservation targets for the State's electric utilities with more than 25,000 customers. The District complied with its requirements for the annual renewable energy compliance period ended December 31, 2016 and its two-year conservation compliance period ended December 31, 2016. BPA operated wind projects that are part of the FCRPS, as well as Nine Canyon Wind and White Creek Wind contracts will assist in providing the renewable energy the District will need in order to comply with the Act's energy targets in the future. At this time the District can meet its I-937 yearly compliance targets with these aforementioned plants using the 3-year REC shaping allowed in the Act. After 2020, the District will meet any new higher REC requirements using either tradable RECs or through purchase agreements from renewable resources.

Nine Canyon Wind Project (Phase I and III) – Located near the city of Kennewick, WA, Nine Canyon Wind Project is owned by Energy Northwest. The District has signed a Power Purchase Agreement for 2% of the output of Phase I. The District's 2% share represents approximately 1 MW of capacity and based upon a 30% load factor, approximately 2,600 MWh of energy production annually. The District has also signed a Power Purchase Agreement for 15.7% of the output of Phase III. The District's 15.7% share represents approximately 5 MW of capacity and based upon a 30% load factor, approximately 13,100 MWh of energy production annually.

White Creek Wind Project – On June 20, 2008, the District executed agreements with Klickitat County PUD for the acquisition of a 10% share of the output of the 205 megawatt White Creek Wind Project near Goldendale, Washington for the purchase price of $36.85 million. The White Creek Wind Project agreements include but are not limited to the Energy Marketing Agreement. On June 16, 2008, the District issued bonds to finance a portion of the White Creek Wind Project purchase (see Note 13).

The prepaid power agreements are amortized using the straight line method over the 20 year contract period and had amortization in 2016 and 2015 totaling $1,889,538. The District's 10% share represents approximately 20.5 MW of capacity and based upon a 32% load factor, approximately 57,500 MWh of energy production annually.

Power management – In 2011, the District entered into a power management services agreement with The Energy Authority Inc. (TEA) to provide certain power scheduling, purchasing, sales and related services to assist in the short term management of the District's power supply. Power purchases and sales are managed by the District in accordance with adopted risk management policies.

Note 7 – Derivative Instruments

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

	Changes in Fair Value		Fair Value at December 31, 2016		
	Classification	Amount	Classification	Amount	Notional
Cash Flow Hedges:					
Financial Swap Forward	Deferred Inflow	$ 238,361	Derivative Asset	$ 238,361	MWH
Financial Swap Forward	Deferred Outflow	245,854	Derivative Liability	245,854	MWH

The fair values of the financial swap contracts were based on the futures price curve for the Mid-Columbia Intercontinental Exchange for electricity. The financial swaps were entered into between April 2015 and December 2016, with maturity dates through June 2018.

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:

Surplus Purchased Power Resources – The District hedges projected surpluses in future periods by locking in a forward price. Surplus power is generally sold forward at a fixed-price, either physically or financially, when the probability of surplus is high.

Deficit Power Resources – The District hedges projected power resource deficits in future periods by purchasing power. Power is generally purchased to cover projected deficits at a fixed price, either physically or financially, when the probability of the deficit position is high.

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

- Physical power forward purchases and sales
- Monthly and daily power physical calls and puts
- Power and natural gas fixed for floating swaps
- Monthly financial Asian power call and put options
- Financial daily power put and call options
- Monthly power swaptions

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

Credit risk – The District is a member of TEA. The District adheres to the credit policies and credit limits agreed to by TEA and the District. 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.

Note 7 – Derivative Instruments (continued)

All physical commodity 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. As of December 31, 2016, the District had 10 counterparties. The maximum credit extended to any one counterparty is $1.75 million.

The District entered into master enabling agreements with various counterparties, which enable hedging transactions. Such agreements include the 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 ISDA agreements are used to financially hedge monthly long or short positions to reduce the risk of an underlying physical position by using Risk Management Committee approved financial instruments.

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, 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 Intercontinental Exchange index and all gas transactions are to be settled on the relevant Sumas/Huntingdon index.

Termination risk – As of December 31, 2016, 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 not generally fall under the events of default provisions, unless the non-performing party fails to pay the resulting liquidated damages as they come due.

Note 8 – District Hydroelectric Projects

Cowlitz Falls Project – The Cowlitz Falls Project is located on the upper Cowlitz River in eastern Lewis County, Washington upstream from two existing hydroelectric projects, Mayfield and Mossyrock, owned by the City of Tacoma. The Project includes a concrete gravity dam and powerhouse, a reservoir covering about 610 acres extending approximately 10 miles up the Cowlitz River and 1.5 miles of the Cispus River, and 5.2 miles of overland transmission line to the District's Glenoma Substation.

Note 8 – District Hydroelectric Projects (continued)

The powerhouse contains two Kaplan turbine generating units with net installed capacity of 35 MW each at a rated head of 87.5 feet. Average annual energy generation is estimated at 261 million kilowatt hours. Project operation depends upon the “run of the river” to produce the maximum amount of electric energy, instead of extensively regulating the reservoir behind the dam to maximize the Project’s firm or dependable capacity.

In June 1986, the District was granted a license by FERC to proceed with the development and construction of the Cowlitz Falls Project. On May 23, 1991, the District and BPA executed an Amendatory Power Purchase Contract. Construction of the Project began in July 1991 and the Project began commercial operation on June 29, 1994.

Revenues for the Cowlitz Falls System are recognized on the basis of the Amendatory Power Purchase Contract between the District and BPA. Through this contract, BPA receives all output from the Cowlitz Falls Project in exchange for payment of all operation and maintenance costs and debt service on Cowlitz Falls revenue bonds (see Note 12). The District receives monthly operation and maintenance payments from BPA based upon an annual budget of operating and capital project expenditures. Certain operation and maintenance costs are subject to incentive or reimbursement provisions if actual expenses are less or more than certain budgeted amounts. The District did not receive any incentive payments for the years ended December 31, 2016 and 2015. Debt service payments are made by BPA directly to the Bond transfer agent for payment of scheduled bond interest and principal.

The District records the Cowlitz Falls System activity reflecting the cost reimbursement basis of the Amendatory Power Purchase Contract with BPA. As a result, revenues and costs offset one another with no resulting net income or loss. The Cowlitz Falls System consists of essentially two activities, plant construction and related debt service, and operations and maintenance. For related debt service, revenue is recognized primarily for BPA debt service payments. Expenses consist of interest on the outstanding revenue bonds, depreciation, and amortization of bond costs. For operations and maintenance, revenue is recognized primarily for BPA operation and maintenance advances, and interest income on unspent advances. Expenses consist of operation and maintenance costs, including plant renewals and replacements, and taxes.

As part of the contract, the District (Electric System) provides power transmission services to BPA over facilities of both the City of Tacoma (Tacoma) and the District. The terms and conditions for the use of the Tacoma facilities are governed by an agreement between Tacoma and the District. Costs are passed to BPA as part of the District’s contract with BPA. Revenue amounted to $988,143 and $973,226 for the years ended 2016 and 2015, respectively.

Mill Creek Hydroelectric Project – The Mill Creek Hydroelectric Project is located on Mill Creek, a tributary to the Cowlitz River, near Salkum, Washington and the Cowlitz Salmon Hatchery. The project includes a six foot high concrete diversion structure, 1,500 feet of 42 inch concrete cylinder pipe and a concrete block powerhouse downstream. The powerhouse contains two Francis turbine induction generating units with net installed capacity of 300 KW each at an average head of 96 feet.

Note 9 – Conservation Programs

The District has participated in BPA programs over the past several years to more aggressively seek out and acquire energy efficiency savings. On March 3, 2004, the District signed a Purchase of Conservation Agreement with BPA for the purpose of offering conservation under a program known as "Conservation as Part of Augmentation" (ConAug). On July 10, 2006, the District signed a Conservation Acquisition Agreement (CAA) with BPA for purpose of offering conservation to commercial and industrial customers. On September 22, 2009 the District executed the "Energy Conservation Agreement" (ECA) with BPA to continue efforts begun under the ConAug and CAA agreements. The District continues to offer commercial and industrial energy efficiency measures through the ECA program.

In 2009, the District completed a Conservation Potential Assessment (CPA) as part of the requirements under the Energy Independence Act adopted with passage of Initiative 937. The CPA developed 20 year and 10 year conservation plans with a defined target equaling 20% of the corresponding 10 year potential starting in 2010. Every two years the District must update the CPA with new information and establish a new target for the subsequent two year period. The CPA for the 2016-2017 biennium set the energy savings target for this period at 0.63 aMW, or approximately 2,759 MWh for each year. Through conservation programs described above and indirect savings acquired through the activities of NEEA, the District will exceed the 2016-2017 target.

Note 10 – Fiber Optic Activity

The District's fiber optic based communication system consists of approximately 86 miles of overhead ADSS fiber optic cable, primarily following the District's transmission routes. The District is constructing the system to support its Electric System with communication between its offices and various substations located throughout Lewis County.

The District has also leased portions of excess dark fibers to telecommunication companies, BPA, non-profit, and governmental agencies. Expansion of the system may occur where it best meets the District's communication needs.

Note 10 – Fiber Optic Activity (continued)

Selected financial data is reported as follows:

	2016	2015
Telecommunication services		
Operating revenues		
Dark fiber leases	$ 360,049	$ 305,190
Total operating revenues	360,049	305,190
Operating expenses		
Operating expenses	-	1,416
Maintenance expense	2,480	9,904
Depreciation expense	90,198	79,199
Total operating expenses	92,678	90,519
Net operating revenue	$ 267,371	$ 214,671
Capital investment		
Net telecommunication plant	$ 1,423,578	$ 1,456,889

Note 11 – PURMS Self–Insurance Agreement

The District and eighteen other PUD's participate in a joint self-insurance pool in affiliation with Public Utility Risk Management Services (PURMS).

Liability risk pool – PURMS provides liability insurance coverage for its members participating in the Liability Risk Pool (Liability Pool) and to a limited extent for the benefit of their employees under an agreement entitled "PURMS Joint Self-Insurance Agreement" (amended and restated as of November 10, 2011, "SIA"). Under SIA, the Liability Pool had a self-insured retention of $1,000,000 per occurrence, which was the Coverage Limit in effect for 2016, and in effect as of December 31, 2016.

The Liability Pool is funded through assessments of its participating members. Assessments are levied at the beginning of each calendar year to replenish the Liability Pool to its designated risk pool balance, and at any time during the year that either (a) the actual risk pool balance becomes $500,000 less than the designated risk pool balance or (b) the risk pool balance is depleted to the amount of 70% funding level established by the actuarial report for the liability pool. Effective November 3, 2016, the designated risk pool balance was increased to $3,250,000 from $3,000,000.

At all times, PURMS also maintains excess liability insurance for its members in the Liability Pool. For the year 2016, the amount of such excess insurance was $35,000,000.

Note 11 – PURMS Self–Insurance Agreement (continued)

As of December 31, 2016, there were 84 known incidents and/or unresolved liability claims pending against one or more members or former members of PURMS' Liability Pool. The total dollar value of the risk posed by these claims to such members and to the Liability Pool itself is unknown. Accordingly, no provision has been included in the accompanying financial statements.

Property risk pool – PURMS provides property insurance for its members participating in the Property Risk Pool (Property Pool) in accordance with the terms of the SIA (identified above). Under the SIA, from its inception in 1997 to the present, the Property Pool has had a self-insured retention (or Property Coverage Limit) of $250,000 per property loss.

The Property Pool is funded to the amount of its Designated Property Pool Balance, which in 2016 was $750,000. The Property Pool's operations are financed through assessments of its Members in accordance with the terms of the Property General Assessment Formula. A Property Assessment is issued automatically at the beginning of each calendar year to replenish the Property Pool to its Designated Balance. Property Assessment are also issued at any time during the year that the Actual Property Pool Balance drops below $500,000 or is depleted to the amount of the 70% funding level established by the annual actuarial report for the Property Pool.

The Property Pool also provides its members with automatic extended property coverage. This coverage extends property coverage for property losses that exceed the Property Pool's $250,000 property coverage limit if those losses are also subject to increased retentions under the excess property insurance. Under the excess property insurance retentions in effect for 2016, the maximum exposure to the Property Pool from a property loss that exceeded $250,000, and that was subject to an increased retention, was $250,000, less the applicable deductible, or a maximum of $250,000 more than the property coverage limit.

At all times, PURMS also maintains excess property insurance for its members in the Property Risk Pool. For the year 2016, the amount of such excess insurance was $200,000,000.

As of December 31, 2016, there were 14 known incidents and/or unresolved property claims pending against one or more members of PURMS' Property Pool. The total dollar value of the risk posed by these claims to such members and to the Property Pool itself is unknown. Accordingly, no provision has been included in the accompanying financial statements.

Note 12 – Cowlitz Falls Hydroelectric Project Revenue Bonds

In July 2013, the Board issued $87,995,000 in Cowlitz Falls Hydroelectric Project Revenue Refunding Bonds to refund the series 2003 bond issues, with an average interest rate of 4.79%. The balance of the refunding included proceeds from premium on issue of $12,278,112. Underwriting fees and other issuance costs totaled $925,151. The loss on refunding was $5,284,305 and is being charged to operations through the year 2024 using the effective interest method.

Note 12 – Cowlitz Falls Hydroelectric Project Revenue Bonds (continued)

The 2013 Bonds are special limited obligations of the District secured by a lien and charge on the Cowlitz Falls revenues and bond insurance. Pursuant to a Power Purchase Contract and Payment Agreement all Project output has been sold to BPA. BPA is obligated to pay all operation and maintenance costs including debt service on the Bonds, whether or not the Dam is operating or operable (see Note 8).

	2016	2015
2013 Revenue Bonds		
to refund 2003 revenue bonds due April 1, 2032	$ 78,905,000	$ 82,055,000
Less current maturities	3,310,000	3,150,000
Long-term portion of revenue bonds	$ 75,595,000	$ 78,905,000

Scheduled debt service deposits for principal, interest and principal maturities are as follows:

	Sinking Funds			
	Principal	Interest	Total	Principal Maturities
2017	$ 3,310,000	$ 3,991,912	$ 7,301,912	$ 3,310,000
2018	3,475,000	3,826,413	7,301,413	3,475,000
2019	3,650,000	3,652,662	7,302,662	3,650,000
2020	3,830,000	3,470,163	7,300,163	3,830,000
2021	4,020,000	3,278,662	7,298,662	4,020,000
2022 – 2026	23,365,000	13,133,038	36,498,038	23,365,000
2027 – 2031	30,140,000	6,360,188	36,500,188	30,140,000
2032 – 2033	7,115,000	186,769	7,301,769	7,115,000
	$ 78,905,000	$ 37,899,807	$ 116,804,807	$ 78,905,000

Note 13 – Electric System Revenue Bonds, Series 2008

In June 2008, the District issued two series of revenue bonds in the aggregate amount of $36,690,000 to finance capital improvements to the Electric System and acquire the right to energy and other attributes from the White Creek Wind Project (see Note 6). The bonds consist of two series, Series 2008A, in the principal amount of $19,415,000 with an interest rate of 5.00%, and Series 2008B (Taxable) in the principal amount of $17,275,000 with interest rates ranging from 3.64% to 5.32%.

Note 13 – Electric System Revenue Bonds, Series 2008 (continued)

In December 2016, the District issued $20,602,385 of Electric System Revenue Refunding Bonds, Series 2016 with an average interest rate of 2.08% to advance refund $19,415,000 of outstanding Revenue Bonds, Series 2008A with an average interest rate of 5.0%. The proceeds were used to purchase U.S. State and Local Government Series securities that were placed in an irrevocable trust for the purpose of generating resources for all future debt service payments on the Series 2008A bonds. As a result, the Series 2008A bonds are considered to be defeased and the liability for those bonds have been removed from the financial statements. This advance refunding was undertaken to reduce total debt service over the next 11 years by $2,955,390 and resulted in an economic gain of $2,586,188.

These bonds are subject to covenants which specify the order of application of gross revenue requirements and which require the District to: pay costs of maintenance and operations; costs associated with the generation, conservation, transformation, transmission or distributions of power and energy acquired or purchased or constructed by the District; and to make all payments required to be made into the Bond Account. Other covenants also apply. The 2008 Series bonds were issued with a premium of $1,146,751 and had underwriting fees and other issuance costs of $982,888.

Scheduled debt service deposits for principal and interest and principal maturities are as follows:

	Series 2016			
	Principal	Interest	Total	Principal Maturities
2017	$ -	$ 395,200	$ 395,200	$ -
2018	542,220	428,530	970,750	542,220
2019	2,049,072	417,251	2,466,323	2,049,072
2020	2,093,693	374,630	2,468,323	2,093,693
2021	2,134,741	331,082	2,465,823	2,134,741
2022 – 2026	11,367,325	970,293	12,337,618	11,367,325
2027	2,415,334	50,239	2,465,573	2,415,334
	$ 20,602,385	$ 2,967,225	$ 23,569,610	$ 20,602,385

	Series 2008 B			
	Principal	Interest	Total	Principal Maturities
2017	$ 5,275,000	$ 280,630	$ 5,555,630	$ 5,275,000
	$ 5,275,000	$ 280,630	$ 5,555,630	$ 5,275,000

Note 13 – Electric System Revenue Bonds, Series 2008 (continued)

A reconciliation of the Series 2008 bond issuance and the Statement of Net Position is as follows:

Series 2016	$ 20,602,385
Series 2008 B	5,275,000
Total	25,877,385
Less current maturities	(5,275,000)
Long-term portion of revenue Bonds	$ 20,602,385

The District issued $9,499,000 in Revenue Bonds in June 1992 for financing a portion of the District's Capital Improvement Program and conservation efforts. The Program made capital improvements and completed conservation efforts of $13 million over a two year period. On November 29, 1994, the District deposited $9,480,300 in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1992 Series bonds.

These refunded bonds constitute a contingent liability of the District only to the extent that cash and investments presently in the control of the refunding trustees are not sufficient to meet debt service requirements, and are therefore excluded from the financial statements because the likelihood of additional funding requirements is considered remote.

Note 14 – Line of Credit

On October 18, 2011, the District and West Coast Bank (now Columbia Bank) entered into a Loan Commitment for a Revolving Line of Credit (LOC) with an available commitment of $5 million. The District may use the proceeds of any draws on the LOC to fund short-term cash flow needs and shall accrue interest from the date money is drawn at the prime rate defined in the note resolution. The initial term of the Loan Commitment expired on October 18, 2013. The LOC was extended for up to an additional 38 months expiring on December 1, 2016. On December 1, 2016, the LOC was extended for an additional 36 months, expiring December 1, 2019. As of December 31, 2016, the District has not drawn on the LOC.

Note 15 – Endangered Species Listing of Salmon and Steelhead/American Rivers Intent to Sue

The National Marine Fisheries Service (NMFS) has listed the lower Columbia Chinook salmon and steelhead trout as threatened under the Endangered Species Act (ESA). The Cowlitz River is a tributary of the lower Columbia River and the Cowlitz Falls Project operates on the upper Cowlitz River.

On January 14, 2000, American Rivers, Trout Unlimited, Friends of the Cowlitz, CPR Fish and the Cowlitz Indian Tribe filed a Notice of Intent to Sue for Violations of the ESA. The Notice claims the FERC, BPA, and District are violating the ESA by continued operation of the Cowlitz Falls Project. American Rivers indicates that unless BPA and FERC initiated consultation under Section 7 of the ESA with NMFS regarding the impact of the Project on listed species, and unless immediate action is taken to bring the Project into compliance, they will file suit against BPA, FERC, and the District.

As a result of the Cowlitz Falls Project operation and the ESA anadromous fish listings, the District (as the non-Federal representative to FERC) initiated consultation with the FERC and NMFS to evaluate possible ESA impacts of the Project. As part of the consultation the District completed a draft Biological Assessment (BA) of the Cowlitz Falls Project benefits, impacts, and operation in March 2002 and submitted it to the FERC. The FERC accepted the draft BA, finalized it and submitted it to NMFS in July 2002.

In June 2009, the NMFS issued a Biological Opinion (BiOp) for the Project which allows limited “Take” of the threatened species. The BiOp was submitted to the FERC for inclusion as a Project License amendment which includes studies and mitigation measures to reduce impacts to the species at the Project. As of this time the FERC has not acted on the BiOp. In the interim, the District has evaluated and/or implemented many of the reasonable and prudent measures for protection of the species at the Project. On April 9, 2013, NMFS updated the BiOp’s Incidental Take Statement and study schedule.

On June 20, 2014, Tacoma Power, BPA and the District signed the “Northshore Project Easement Agreement” whereby BPA signed over ownership of the Cowlitz Falls Fish Facility (CFFF) and the Stress Relief Ponds (located at the downstream salmon hatchery). The District agreed to provide access and easement areas to Tacoma Power so that a new fish collection facility could be combined with the existing CFFF. Tacoma Power’s goal is to improve fish collection efficiencies to 95%. On August 18, 2014, FERC issued an “Order Approving Non-Project Use of Project Lands” thereby approving the easement to allow Tacoma Power to build the new collector. Tacoma Power broke ground for the collector in June 2015. As of May, 2017, the new Northshore collector is nearly complete. Testing and debugging has begun and the first fish are being collected.

As stated in Note 8, BPA pays all operation and maintenance costs of the Cowlitz Falls Project. As such, the above matters are not expected to impact the District’s financial position.

Note 16 – Subsequent Event

On March 28, 2017, the Board of Commissioners passed Resolution No. 2765 revising certain rate schedules effective April 1, 2017. The basic charge was increased by $0.20 per day and the kilowatt hour charge was increased by 5.5%.

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REPORT OF INDEPENDENT AUDITORS 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*

Board of Commissioners
Public Utility District No. 1 of Lewis County
Chehalis, Washington

We have audited, in accordance with the 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, which comprise the statement of net position as of December 31, 2016, and the related combined and separate statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the combined statement of net position as of December 31, 2015, and the related combined statement of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements of the Public Utility District No. 1 of Lewis County's Electric System and Cowlitz Falls System (the District), which collectively comprise the Public Utility District No. 1 of Lewis County's financial statements, and have issued our report thereon dated May 30, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit, 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 combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity'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.

REPORT OF INDEPENDENT AUDITORS 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* (continued)

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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. 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 District's financial statements are free of material misstatement, we performed tests of its 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 result of that testing, and not to provide an opinion on the effectiveness of the entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Moss Adams LLP

Portland, Oregon
May 30, 2017

REQUIRED SUPPLEMENTARY INFORMATION

PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
SCHEDULE OF PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
AS OF JUNE 30

		PERS Plan 1	
	2016	2015	2014
Proportion of the net pension liability	0.084520%	0.081668%	0.075402%
Proportionate share of the net pension liability	$ 4,539,122	$ 4,271,996	$ 3,798,411
Covered - employee payroll	$ 10,099,339	$ 9,359,473	$ 8,340,287
Employers proportionate share of the net pension liability as percentage of covered-employee payroll	44%	45%	45%
Plan fiduciary net position as a percentage of the total pension liability	54%	59%	61%

		PERS Plan 2/3	
	2016	2015	2014
Proportion of the net pension liability	0.108348%	0.105470%	0.097080%
Proportionate share of the net pension liability	$ 5,455,236	$ 3,768,503	$ 1,962,337
Covered - employee payroll	$ 10,099,339	$ 9,359,473	$ 8,340,287
Employers proportionate share of the net pension liability as percentage of covered-employee payroll	54%	40%	24%
Plan fiduciary net position as a percentage of the total pension liability	85%	89%	93%

Note to Schedule: The ten year information will be provided as it is available.

PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
SCHEDULE OF EMPLOYER CONTRIBUTIONS
AS OF DECEMBER 31

PERS Plan 1

	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
Statutorily or contractually required contribution	$ 485,516	$ 416,345	$ 365,611	$ 258,054	$ 98,363	$ 13,517	$ 14,645	$ 20,458	$ 35,441	$ 31,667
Contributions in relation to the statutorily or contractually determined contribution*	(485,516)	(416,345)	(365,611)	(258,054)	(98,363)	(13,517)	(14,645)	(20,458)	(35,441)	(31,667)
Contribution deficiency (excess)	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
District's covered-employee payroll **	$10,178,525	$ 9,505,771	$ 9,062,013	$ 8,152,293	$ 4,059,155	$ 236,269	$ 284,344	$ 301,573	$ 528,311	$ 579,605
Contributions as a percentage of covered-employee payroll	4.77%	4.38%	4.03%	3.17%	2.42%	5.72%	5.15%	6.78%	6.71%	5.46%

PERS Plan 2/3

	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
Statutorily or contractually required contribution	$ 634,122	$ 534,503	$ 452,689	$ 389,337	$ 466,380	$ 438,966	$ 357,812	$ 445,921	$ 409,089	$ 296,445
Contributions in relation to the statutorily or contractually determined contribution	(634,122)	(534,503)	(452,689)	(389,337)	(466,380)	(438,966)	(357,812)	(445,921)	(409,089)	(296,445)
Contribution deficiency (excess)	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
District's covered-employee payroll **	$10,178,525	$ 9,505,771	$ 9,062,013	$ 8,152,293	$ 7,970,187	$ 7,321,077	$ 6,947,727	$ 6,593,033	$ 5,847,830	$ 5,388,767
Contributions as a percentage of covered-employee payroll	6.23%	5.62%	5.00%	4.78%	5.85%	6.00%	5.15%	6.76%	7.00%	5.50%

* Effective July 2012 a certain portion of contributions from PERS Plan 2/3 is allocated to PERS Plan 1 in order to fund its unfunded actuarial accrued liability (UAAL)
** Payroll on which contributions are based

Report of Independent Auditors and
Financial Statements with Required
Supplementary Information for

Public Utility District No. 1 of Lewis County

December 31, 2015 and 2014

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

CONTENTS

REPORT OF INDEPENDENT AUDITORS

Board of Commissioners
Public Utility District No. 1 of Lewis County
Chehalis, Washington

Report on the Financial Statements

We have audited the accompanying combined and separate financial statements of Public Utility No. 1 of Lewis County's Electric System and Cowlitz Falls System (the District) which comprise the combined and separate statements of net position as of December 31, 2015, and the related combined and separate statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the combined statement of net position as of December 31, 2014, and the related combined statement of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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.

REPORT OF INDEPENDENT AUDITORS (continued)

Opinions

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 Lewis County's Electric System and Cowlitz Falls System as of December 31, 2015 and 2014 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 16 to the financial statements, the District adopted the provisions of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*, and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68,* effective January 1, 2014. The beginning-of-year net position has been restated for this change. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis preceding the financial statements and the schedule of proportionate share of net pension liability and schedule of employer contributions subsequent to the notes to the financial statements be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the 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 May 27, 2016 on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Moss Adams LLP

Portland, Oregon
May 27, 2016

This discussion and analysis is designed to provide an overview of Public Utility District No. 1 of Lewis County, Washington (the District) financial activities for the year ended December 31, 2015, with comparable information for 2014 and 2013. This required supplementary information should be read in conjunction with the District's financial statements and notes to financial statements.

The District is a municipal corporation incorporated in 1936 to serve the citizens of Lewis County, Washington. The District is governed by a three-member board of locally elected commissioners, independent of the county government. The District manages and operates two systems: Electric Distribution System (Electric System) and the Cowlitz Falls Hydroelectric Generation Project (Cowlitz Falls System).

Overview of the Financial Statements

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

Basic Financial Statements

The Statement of Net Position presents the District's net position as the difference between assets and deferred outflows of resources, and liabilities and deferred inflows of resources. The Statement of Net Position provides information about the nature and amount of investments in resources (assets), the consumption of net position in one period that are applicable to future periods (deferred outflows of resources), the obligations to creditors (liabilities), and the acquisition of net position that are applicable to future periods (deferred inflows of resources).

The Statement of Revenues, Expenses, and Changes in Net Position reports the revenues and expenses during the periods indicated and identify operating activity separately from non-operating activity.

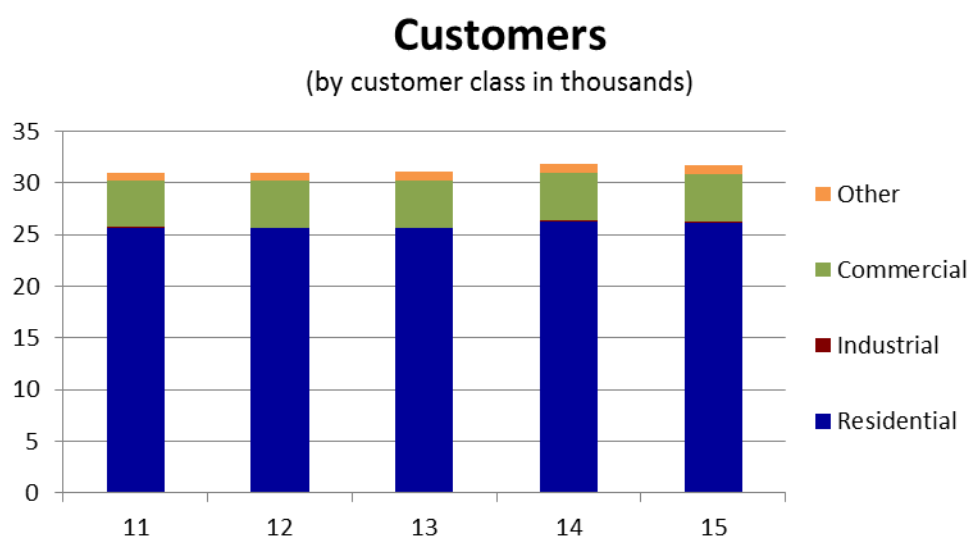
The Statement of Cash Flows provides information about the District's cash flows from operating activities, capital and related financing activities, investing activities, and noncapital financing activities, and presents a reconciliation of net operating income to net cash provided by operating activities.

Notes to the Financial Statements

The notes to the financial statements provide additional information that is essential to a full understanding of the figures provided in the basic financial statements.

ELECTRIC DISTRIBUTION SYSTEM

The Electric System provides electric service throughout Lewis County with the exception of the City of Centralia who is served by the City's Municipal Light and Power Department. Currently, the District serves 31,669 customers within approximately 2,530 square miles comprising 3,416 miles of distribution line and services. Power supplies are primarily provided to the District through purchase power contracts with Bonneville Power Administration (BPA). Weather and economic climate are the primary conditions that influence electricity sales. Generally, extreme temperatures increase sales to customers who use electricity for cooling and heating, while moderate temperatures produce moderate sales. Seasonal influences exist from industrial customers that are related to agriculture products peaking during the District's summer months in contrast to residential customers peaking during the winter months from heating. Economic conditions have improved in Lewis County over the past couple of years and the District's growth has expanded along the Interstate 5 corridor.



Financial Summary and Analysis

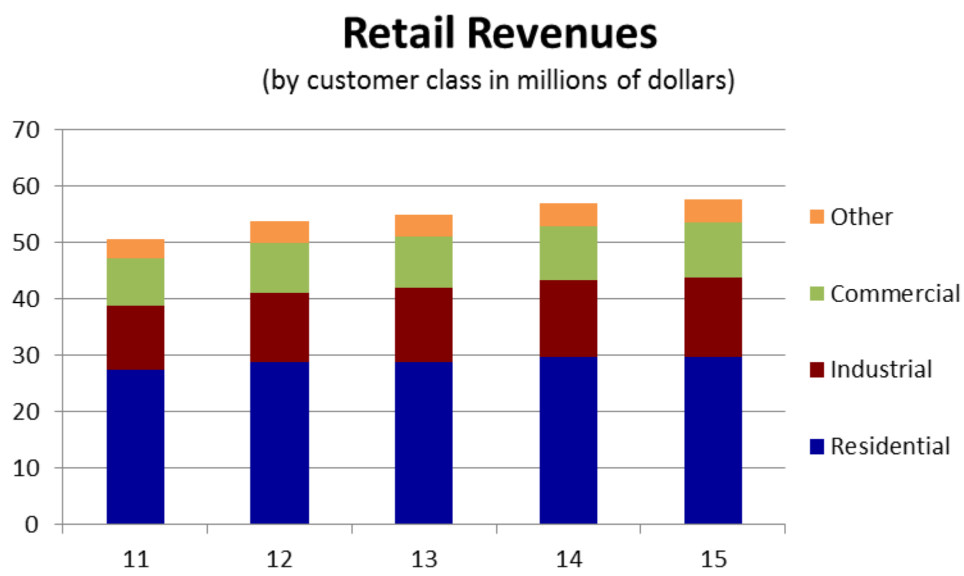
During 2015, the Electric System's net operating loss before other revenues (expenses) and contributed capital was $1.87 million, which was a change of $2.51 million from 2014. The factors influencing these results in 2015 include:

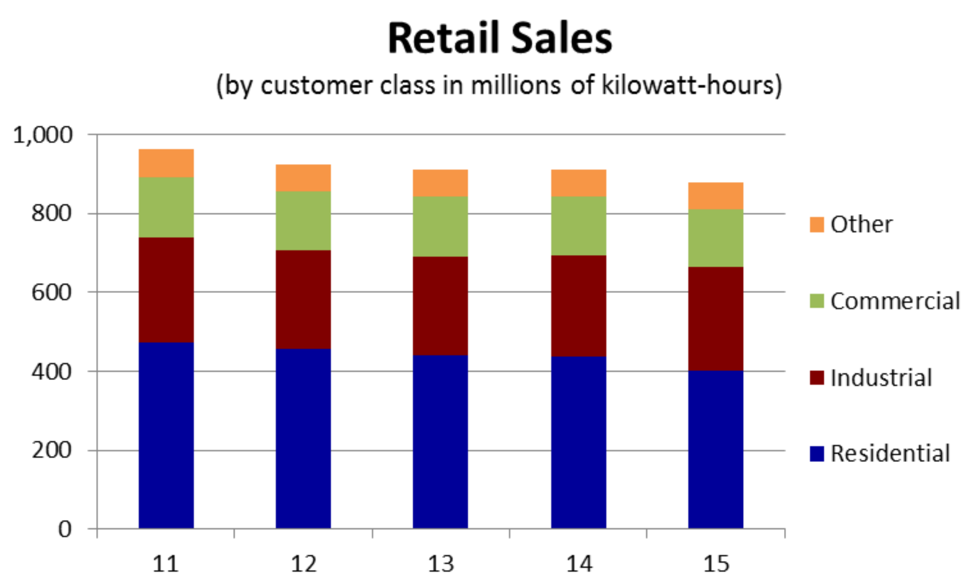
- Total operating revenues decreased by $3.32 million or 5.0%.
  - Revenues from sales to customers increased $645,500 or 1.1% due to the rate increase effective May 2015, offsetting a 3.6% decrease in kilowatt hours sold.
  - Revenues from wholesale decreased $4.08 million or 48.9% due to low wholesale prices and lower volume.
  - Other operating revenues increased $101,000 or 4.3% due to increased wheeling revenues and sales of renewable energy certificates.
  - The Board of Commissioners approved the transfer of $1.46 million to the rate stabilization account, a decrease of $15,000.

- Total operating expenses decreased by $802,600 or 1.2%.
  - Purchase power expense decreased by $1.23 million or 2.8% primarily due to decreased market purchases.
  - Other operating expense increased by $188,700 or 2.2% primarily due to increased wheeling and distribution expenses.
  - Maintenance expense increased by $82,500 or 2.0% primarily due to increased transmission line maintenance.
  - Depreciation expense increased by $96,000 or 2.4% as a result of capital additions.
  - Taxes increased by $62,400 or 1.5% primarily as a result of higher retail sales.

Selected Financial Data

	(in thousands)		
	2015	2014	2013
		as restated	
Operating revenues	$ 62,917	$ 66,233	$ 61,418
Operating expenses	64,784	65,587	62,636
Net operating revenues	(1,867)	646	(1,218)
Other revenues (expenses) and contributed capital	(366)	(614)	(920)
Change in net position	$ (2,233)	$ 32	$ (2,137)
Total assets and deferred outflows	$ 172,297	$ 173,591	$ 174,929
Total liabilities and deferred inflows	49,936	48,996	43,305
Net investment in capital assets	120,332	117,447	116,371
Unrestricted net position	856	5,986	14,100
Restricted for debt service	172	162	152
Restricted - other	1,000	1,000	1,000


Retail Revenues
(by customer class in millions of dollars)
70
60
50
40
30
20
10
0
11
12
13
14
15
Other
Commercial
Industrial
Residential


Retail Sales
(by customer class in millions of kilowatt-hours)
1,000
800
600
400
200
0
11
12
13
14
15
Other
Commercial
Industrial
Residential

Capital Asset and Long–Term Debt Activity

As of December 31, 2015, the Electric System had $174.1 million invested in a variety of capital assets in service. This represents an increase of $4.5 million or 2.7% from 2014. As of December 31, 2014, the Electric Distribution System had $169.5 million invested in a variety of capital assets in service. This represents an increase of $4.5 million or 2.7% from 2013. Capital construction is provided for through a combination of construction fees, cash flow from revenues, and represents normal additions to the system.

	(in thousands)		
	2015	2014	2013
Intangible and land	$ 4,953	$ 4,944	$ 4,944
Distribution plant	121,358	118,097	114,534
Transmission plant	22,957	22,536	22,481
Hydraulic plant	1,180	1,180	1,180
General plant	23,639	22,821	21,908
Total plant in service	$ 174,087	$ 169,578	$ 165,047

In 2015, revenue bonds outstanding were $26.635 million, which is a decrease of $1.85 million or 6.5% from 2014. In 2014, revenue bonds outstanding were $28.485 million, which is a decrease of $1.765 million or 5.8% from 2013.

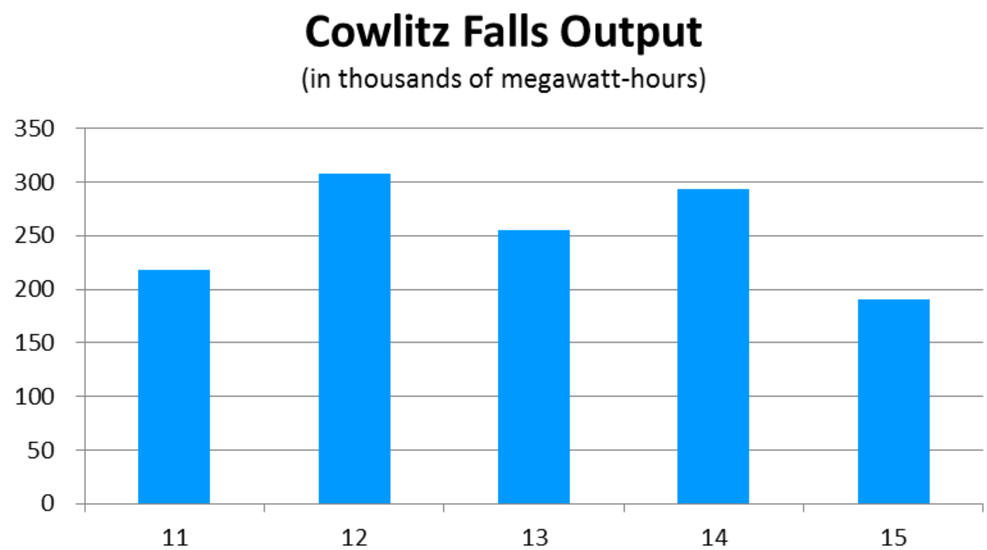
Power Supply

The District signed a 20-year Block and Slice Power Agreement with BPA on December 1, 2008, with the contract taking effect on October 1, 2011. The District also purchases wind power in order to comply with Initiative 937 renewable resources requirements.

COWLITZ FALLS HYDROELECTRIC GENERATION PROJECT

The District operates the Cowlitz Falls Project (System or Project) located on the upper Cowlitz River in eastern Lewis County. The powerhouse contains two Kaplan turbine generating units with net installed capacity of 35 MW each. Average annual generation is estimated at 265 million kilowatt hours.

Project operation depends upon the "run of the river" to produce the maximum amount of electric energy. Generation output in 2015 was negatively impacted by a low water year and the scheduled two month reservoir drawdown associated with the construction of the North Shore Collector.



Financial Summary and Analysis

Revenues for the Cowlitz Falls Project are recognized on the basis of the Amendatory Power Purchase Contract between the District and BPA. Through this contract, BPA receives all output from the Cowlitz Falls Project in exchange for payment of all operation and maintenance costs and debt service on the Cowlitz Falls Project revenue bonds.

Selected Financial Data

	(in thousands)		
	2015	2014	2013
		as restated	
Operating revenues	$ 10,285	$ 10,519	$ 14,302
Operating expenses	6,518	6,678	7,965
Net operating revenues	3,767	3,841	6,337
Other expenses	3,767	3,841	6,337
Change in net position	$ -	$ -	$ -
Total assets and deferred outflows	$ 97,757	$ 100,658	$ 103,904
Total liabilities and deferred inflows	97,757	100,658	103,904
Net position	-	-	-

Capital Assets and Long-Term Debt Activity

Capital invested in plant was $158.1 million and plant net of depreciation was $87.7 million in 2015. Total Cowlitz Falls Project plant in service as of December 31, 2015, 2014 and 2013 consisted of the following:

	(in thousands)		
	2015	2014	2013
Production plant	$ 155,392	$ 155,392	$ 155,392
Transmission plant	2,192	2,175	2,175
General plant	563	563	534
Total plant in service	$ 158,147	$ 158,130	$ 158,101

In July 2013, $87.995 million in Cowlitz Falls Hydroelectric Project Revenue Refunding Bonds were issued to refund the outstanding Revenue Refunding Bonds, Series 2003 maturing on and after October 1, 2014. In 2015, revenue bonds outstanding were $82.055 million, which is a decrease of $3.0 million or 3.5% from 2014. In 2014, revenue bonds outstanding were $85.055 million, which is a decrease of $2.94 million or 3.3% from 2013.

Requests for Information

The basic financial statements, notes, and management's discussion and analysis are designed to provide a general overview of the District's finances. Questions concerning any of the information provided in this report should be directed to the District at 321 NW Pacific Ave, Chehalis, WA 98532.

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PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
STATEMENT OF NET POSITION

	Electric System	Cowlitz Falls System	December 31, 2015 Combined	December 31, 2014 Combined *(as restated)*
CURRENT ASSETS				
Cash and cash equivalents	$ 8,952,697	$ 3,338,543	$ 12,291,240	$ 17,241,693
Customer and other receivables, net	9,684,017	1,925,418	11,609,435	10,656,273
Inventories	3,070,495	-	3,070,495	2,948,410
Other current assets	156,548	-	156,548	176,230
Current portion of prepaid power and attributes	1,889,538	-	1,889,538	1,889,538
Total current assets	23,753,295	5,263,961	29,017,256	32,912,144
RESTRICTED ASSETS				
Cash and cash equivalents –				
Debt service fund	285,161	-	285,161	282,499
Major catastrophe fund	1,000,000	-	1,000,000	1,000,000
Rate stabilization	4,067,235	-	4,067,235	2,607,138
Total restricted assets	5,352,396	-	5,352,396	3,889,637
UTILITY PLANT				
Utility plant in service	174,087,176	158,147,824	332,235,000	327,708,232
Construction in progress	4,431,068	-	4,431,068	3,124,079
Total utility plant	178,518,244	158,147,824	336,666,068	330,832,311
Less accumulated depreciation	58,185,796	70,430,631	128,616,427	122,609,883
Net utility plant	120,332,448	87,717,193	208,049,641	208,222,428
OTHER ASSETS				
Conservation loans	129,087	-	129,087	113,663
Derivative asset	403,842	-	403,842	219,565
Unamortized prepaid power and attributes	20,784,923	-	20,784,923	22,674,462
Regulatory asset - issuance costs	342,409	734,069	1,076,478	1,222,172
Total other assets	21,660,261	734,069	22,394,330	24,229,862
DEFERRED OUTFLOWS OF RESOURCES				
Accumulated decrease in fair value of hedging derivatives	104,432	-	104,432	94,037
Pension	1,094,566	126,550	1,221,116	438,801
Deferred loss on refunding	-	3,914,952	3,914,952	4,461,626
Total deferred outflow of resources	1,198,998	4,041,502	5,240,500	4,994,464
Total assets and deferred outflows of resources	$ 172,297,398	$ 97,756,725	$ 270,054,123	$ 274,248,535

 See accompanying notes

	Electric System	Cowlitz Falls System	December 31, 2015 Combined	December 31, 2014 Combined (as restated)
CURRENT LIABILITIES				
Accounts payable	$ 977,561	$ 267,062	$ 1,244,623	$ 867,110
Accrued liabilities	6,787,809	285,918	7,073,727	6,875,498
Accrued bond interest	112,743	1,037,353	1,150,096	1,195,412
Accrued OPEB liability	481,014	50,493	531,507	508,771
Operations and maintenance advance	-	3,338,544	3,338,544	2,547,321
Customer deposits	1,527,295	-	1,527,295	1,481,735
Current maturities of long-term debt	1,945,000	3,150,000	5,095,000	4,850,000
Total current liabilities	11,831,422	8,129,370	19,960,792	18,325,847
LONG-TERM DEBT				
Revenue bonds, net	24,690,000	78,905,000	103,595,000	108,690,000
Unamortized premium	471,360	9,742,179	10,213,539	11,303,927
Total long-term debt	25,161,360	88,647,179	113,808,539	119,993,927
OTHER LIABILITIES				
Other credits	49,325	18,413	67,738	97,511
Net pension liability	7,207,217	833,282	8,040,499	5,760,748
Derivative liability	104,432	-	104,432	94,037
Total liabilities	44,353,756	97,628,244	141,982,000	144,272,070
DEFERRED INFLOWS OF RESOURCES				
Accumulated increase in fair value of hedging derivatives	403,842	-	403,842	219,565
Pension	1,111,256	128,481	1,239,737	2,555,065
Regulatory liability - rate stabilization	4,067,235	-	4,067,235	2,607,138
Total deferred inflows of resources	5,582,333	128,481	5,710,814	5,381,768
NET POSITION				
Net investment in capital assets	120,332,448	(165,034)	120,167,414	116,058,139
Restricted:				
Debt service	172,418	-	172,418	161,940
Other	1,000,000	-	1,000,000	1,000,000
Unrestricted	856,443	165,034	1,021,477	7,374,618
Total net position	122,361,309	-	122,361,309	124,594,697
Total net position, liabilities, and deferred inflows of resources	$ 172,297,398	$ 97,756,725	$ 270,054,123	$ 274,248,535

PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

			Years Ended December 31,	
	Electric System	Cowlitz Falls System	2015 Combined	2014 Combined
OPERATING REVENUES				
Retail sales – electric energy	$ 57,670,014	$ 10,285,430	$ 67,955,444	$ 67,543,840
Wholesale – wind and attributes	4,253,116	-	4,253,116	8,330,843
Transfer from/(to) rate stabilization	(1,460,097)	-	(1,460,097)	(1,475,327)
Other operating revenues	2,454,418	-	2,454,418	2,353,384
Total operating revenues	62,917,451	10,285,430	73,202,881	76,752,740
OPERATING EXPENSES				
Power supply	43,299,249	-	43,299,249	44,531,631
Other operating	8,944,040	1,959,260	10,903,300	10,767,887
Maintenance	4,179,041	1,362,057	5,541,098	5,052,744
Depreciation	4,167,480	3,083,683	7,251,163	7,653,673
Taxes	4,194,600	113,519	4,308,119	4,259,298
Total operating expenses	64,784,410	6,518,519	71,302,929	72,265,233
NET OPERATING INCOME (LOSS)	(1,866,959)	3,766,911	1,899,952	4,487,507
OTHER REVENUES (EXPENSES)				
Interest income	40,131	4,228	44,359	48,551
Interest expense	(1,438,888)	(4,261,913)	(5,700,801)	(5,870,627)
Amortization of debt expense, premium, and loss on refunding	8,581	389,440	398,021	403,947
Revenue from merchandising	233,628	-	233,628	174,649
Expense of contract work	(210,558)	-	(210,558)	(139,273)
Other income	445,989	101,334	547,323	372,707
Total other expenses	(921,117)	(3,766,911)	(4,688,028)	(5,010,046)
NET LOSS	(2,788,076)	-	(2,788,076)	(522,539)
Contributed capital	554,688	-	554,688	554,610
CHANGE IN NET POSITION	(2,233,388)	-	(2,233,388)	32,071
NET POSITION, beginning of year, as originally reported	124,594,697	-	124,594,697	131,623,299
Restatement for change in accounting principal	-	-	-	(7,060,673)
NET POSITION, beginning of year, as restated				124,562,626
NET POSITION, end of year	$ 122,361,309	$ -	$ 122,361,309	$ 124,594,697

 See accompanying notes

	Electric System	Cowlitz Falls System	Year Ended December 31, 2015 Combined	2014 Combined
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash received from customers	$ 63,378,164	$ 11,168,435	$ 74,546,599	$ 78,229,460
Cash paid to suppliers	(45,179,668)	(1,492,116)	(46,671,784)	(50,865,486)
Cash paid to employees	(8,981,493)	(949,422)	(9,930,915)	(8,857,441)
Cash paid for taxes	(4,194,600)	99,821	(4,094,779)	(4,008,331)
Net cash from operating activities	5,022,403	8,826,718	13,849,121	14,498,202
CASH FLOWS FROM INVESTING ACTIVITIES				
Interest and dividends on investments	40,131	4,228	44,359	48,551
Net conservation loan activity	(15,424)	-	(15,424)	(532)
Net other income	469,059	101,334	570,393	408,083
Net cash from investing activities	493,766	105,562	599,328	456,102
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Payments on debt	(1,850,000)	-	(1,850,000)	(1,765,000)
Interest paid on bonds	(1,446,704)	-	(1,446,704)	(1,534,424)
Net cash from noncapital financing activities	(3,296,704)	-	(3,296,704)	(3,299,424)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Utility plant additions, net of cost of removal and salvage proceeds	(7,053,069)	(841,645)	(7,894,714)	(5,161,197)
Contributed capital	554,688	-	554,688	554,610
Principal paid on bonds	-	(3,000,000)	(3,000,000)	(2,940,000)
Interest paid on bonds	-	(4,299,413)	(4,299,413)	(4,358,213)
Net cash from capital and related financing activities	(6,498,381)	(8,141,058)	(14,639,439)	(11,904,800)
CHANGE IN CASH AND CASH EQUIVALENTS	(4,278,916)	791,222	(3,487,694)	(249,920)
CASH AND CASH EQUIVALENTS, beginning of year	18,584,009	2,547,321	21,131,330	21,381,250
CASH AND CASH EQUIVALENTS, end of year	$ 14,305,093	$ 3,338,543	$ 17,643,636	$ 21,131,330
CASH FLOWS FROM OPERATING ACTIVITIES				
Net operating revenues	$ (1,866,959)	$ 3,766,911	$ 1,899,952	$ 4,487,507
Adjustments to reconcile net operating revenues to net cash from operating activities				
Depreciation	4,167,480	3,083,683	7,251,163	7,653,673
Pension related items	163,234	835,213	998,447	-
Amortization of prepaid power and attributes	1,889,539	-	1,889,539	1,889,538
Change in assets and liabilities				
Receivables	(1,044,944)	91,782	(953,162)	61,319
Other current assets	19,682	-	19,682	(16,859)
Accounts payable and warrants outstanding	147,375	230,138	377,513	(718,309)
Accrued liabilities	188,499	9,730	198,229	(384,497)
Accrued OPEB liability	20,576	2,160	22,736	28,587
Inventories	(122,085)	-	(122,085)	64,124
Operations and maintenance advance	-	791,223	791,223	(75,677)
Customer deposits	45,560	-	45,560	15,751
Regulatory liability - rate stabilization	1,460,097	-	1,460,097	1,475,327
Deferred credits	(45,651)	15,878	(29,773)	17,718
Net cash from operating activities	$ 5,022,403	$ 8,826,718	$ 13,849,121	$ 14,498,202

Note 1 – Nature of Organization and Operations

Public Utility District No. 1 of Lewis County (the District) is a municipal corporation of the State of Washington and is governed by an elected three member board. The District was organized in 1936, pursuant to a general election in accordance with the Enabling Act, and commenced its operations in 1939. The District has its administrative offices in Chehalis, Washington, which is located in southwestern Washington.

The District manages and operates two systems: Electric Distribution System (Electric System) and the Cowlitz Falls Hydroelectric Generation Project (Cowlitz Falls System or Project). The Electric System provides electric service to substantially all of Lewis County, except for the City of Centralia. The District constructed and, beginning in June 1994, operates the Cowlitz Falls Hydroelectric Dam on the upper Cowlitz River in eastern Lewis County, Washington (see Note 8). The Electric System and Cowlitz Falls System are separate operating systems.

Note 2 – Summary of Significant Accounting Policies

Reporting entity – In evaluating how to define the government, for financial reporting purposes, management has considered the District's financial reporting entity. The financial reporting entity consists of the District and component units. Component units are legally separate organizations for which the District is financially accountable and other organizations for which the District is not accountable but for which the nature and significance of their relationship with the District are such that the exclusion would cause the District's financial statements to be misleading or incomplete. Based upon this criterion, the District has no component units.

Basis of accounting and presentation – The District is considered an enterprise and operates as a proprietary fund. The financial statements of the District have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The District has applied all applicable Governmental Accounting Standards Board (GASB) pronouncements.

The Uniform System of Accounts, as prescribed by the Federal Energy Regulatory Commission (FERC), is the basis for the District's accounting policies. The accounting records of the District are maintained in accordance with methods prescribed by the State Auditor under authority of Chapter 43.09 RCW.

The accompanying financial statements include the individual and combined statements of financial position of the Electric System and Cowlitz Falls System and the results of operations and cash flows for each system.

Concentration of credit risk – The District's financial instruments that are exposed to concentrations of credit risk consist primarily of cash, temporary investments and receivables.

Note 2 – Summary of Significant Accounting Policies (continued)

The District maintains its cash and temporary investments in bank deposit accounts which exceed federally insured limits. However, all deposits are made with state-approved depositories and are protected under the State's Public Deposit Protection Commission (PDPC).

Credit is extended to customers generally without collateral requirements, however, deposits are obtained from certain customers and formal shut-off procedures are in place.

Utility plant – Utility plant assets are stated at cost (see Note 4). Cost includes contracted services, direct labor and materials, interest capitalized during construction, and certain overhead items. For the Electric System, the provision for depreciation is determined by the straight-line method over the estimated useful lives of the assets (as specified by FERC for utility plant) ranging from three to fifty years. The cost of maintenance and repairs is expensed as incurred; renewals, replacements and betterments are capitalized. Capitalization threshold is $1,000. For the Cowlitz Falls Project, depreciation, renewals, and replacements are recognized on the basis of the Amendatory Power Purchase Contract between the District and BPA (see Note 8).

The actual or average cost of property replaced or renewed is removed from utility plant and such cost plus removal cost less salvage is charged to accumulated depreciation.

Cash equivalents – The District considers all highly liquid investments, including restricted cash, with a maturity of three months or less to be cash equivalents.

Restricted cash and investments – Restricted cash and investments consist of Board restricted funds set aside and invested by the District in a major catastrophe fund, rate stabilization account and investments restricted by bond resolution. The major catastrophe fund balance provides the District with emergency funds should the District face a catastrophe, such as a major wind storm or other extraordinary event.

Customer and other receivables – Accounts receivable are recorded when invoices are issued and are written off when they are determined to be uncollectible. The allowance for doubtful accounts is estimated based on the District's historical losses, review of specific problem accounts, the existing economic conditions, and the financial stability of its customers. Generally, the District considers accounts receivable past due after 30 days. The allowance for doubtful accounts for the Electric System was $405,918 and $501,282 at December 31, 2015 and 2014, respectively. No allowance was deemed necessary for the Cowlitz Falls System.

Inventories – Inventories consist primarily of materials and supplies for construction and maintenance of utility plant and are valued at the lower of average cost or market.

Unamortized bond premiums and loss on refunding – Bond premiums relating to revenue bonds are amortized by the effective interest method over the life of bond issues using a weighted average of the face amount of bonds outstanding. Losses on refunding are amortized over the life of the old or new bonds, whichever is shorter.

Note 2 – Summary of Significant Accounting Policies (continued)

Regulatory assets – unamortized bond issue costs – Unamortized bond issue costs represent the remaining expense related to various debt issuances. The asset is amortized over the duration of the related debt and recognition of these costs is included in the rate making process.

Deferred inflow of resources – The District has deferred revenues to be recognized in future periods in accordance with regulatory accounting requirements. The Board authorized the transfer of $1,460,097 and $1,475,327 from operating revenues to the rate stabilization account for 2015 and 2014, respectively. Future withdrawals from the rate stabilization account will be used to mitigate potential rate increases or provide for unexpected expenses.

Unamortized prepaid power and attributes – Consists of prepaid power and attributes amortized using the straight-line method over the life of the 2008 Series bonds (see Note 6 – White Creek Wind Project).

Compensated absences – The District accrues accumulated unpaid personal leave benefits as the obligation is incurred. The accrued liability for unpaid personal leave at December 31, 2015 and 2014 was $1,546,244 and $1,475,715, respectively. Employees covered by PERS I (see Note 5) are entitled to, upon retirement, the use of up to 60 days of unused personal leave for calculation of retirement benefits. PERS actuarially determines the cost for these additional benefits and bills the District for a portion of them on a one-time basis. These additional costs do not materially affect the District's financial statements. Eligible sick leave balances, meeting certain requirements, may either be converted to personal leave according to a schedule or a percent may be cashed out upon retirement.

Operations and maintenance advance – Operations and maintenance advance represents unspent BPA operation and maintenance advances recognized in accordance with the Amendatory Power Purchase Contract with BPA (see Note 8).

Customer deposits – The District requires deposits from certain customers upon request for service. The customer deposits are held to defray potential uncollected accounts and other contingencies. The deposits are refundable under certain circumstances.

Net position – Net position consists primarily of cumulative net income (loss) collected for the payment of utility plant in advance of net accumulated depreciation recognized on such plant. It is the District's intention to set rates at a level to continue replacing and improving net utility plant. Net position consists of the following components:

- **Net investment in capital assets** – This component of net position consists of capital assets, net of accumulated depreciation, less outstanding balances of any debt borrowings that are attributable to the acquisition, construction or improvement of those assets.
- **Restricted** – This component of net position consists of assets restricted by bond resolutions and assets restricted by Board resolution.
- **Unrestricted** – This component of net position consists of net position that does not meet the definition of "net investment in capital assets" or "restricted."

Note 2 – Summary of Significant Accounting Policies (continued)

Revenue recognition – The District recognizes Electric System revenue as earned. Substantially all residential and small commercial customers are billed bimonthly while large commercial and industrial customers are billed monthly. The District utilizes cycle billing and records revenue billed to its customers when the meters are read. In addition, the District recognizes unbilled revenue, revenues from electric power delivered but not yet billed. At December 31, 2015 and 2014, unbilled revenue was approximately $3,724,850 and $3,423,038 respectively and included in customer and other receivables. Revenues for the Cowlitz Falls Project are recognized on the basis of the Amendatory Power Purchase Contract between the District and BPA (see Note 8).

Contributed capital – Consists of cash contributions received from customers for the construction of utility plant.

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

Derivative instruments – The District has adopted GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. Subject to certain exceptions, GASB Statement No. 53 requires every derivative instrument be recorded on the statement of net position as an asset or liability measured at its fair value, and changes in the derivative's fair value be recognized 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, and do not generally meet the "normal purchases and normal sales" criteria (see Note 7).

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.

Note 3 – Cash Equivalents

The District's investment policies allow for investments in bank certificates of deposit of commercial banks as approved by the State of Washington Public Deposit Protection Commission, or in U.S. Government securities that can be liquidated should it be necessary. Any U.S. Government security purchased shall be purchased through commercial banks qualified as public depositories. All investments shall mature in such amounts and at such times as is anticipated by the District that such moneys will be either reinvested or required to pay District costs. The primary concern of the District shall be the safety of the principal.

The District's deposits and certificates of deposit are entirely covered by Federal Depository Insurance Corporation (FDIC) or held by state-approved depositaries protected under the Commission.

Custodial credit risk is that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. All of the aforementioned cash is held in the District's name by a third–party custodian.

Note 4 – Utility Plant

Capital assets are defined by the District as assets with initial individual cost of more than $1,000 and an estimated useful life in excess of one year.

Utility plant activity for the year ended December 31, 2015 is as follows:

	Balance December 31, 2014	Additions	Retirements	Balance December 31, 2015
ELECTRIC SYSTEM				
Utility plant not being depreciated				
Land	$ 4,822,998	$ 8,721	$ -	$ 4,831,719
Construction in progress	3,124,079	6,278,728	4,971,739	4,431,068
Intangible	121,133	-	-	121,133
Total utility plant not being depreciated	8,068,210	6,287,449	4,971,739	9,383,920
Utility plant being depreciated				
Distribution system	118,096,943	4,015,460	754,431	121,357,972
Transmission system	22,535,950	618,114	196,503	22,957,561
Hydraulic system	1,179,530	-	-	1,179,530
General plant	22,821,548	1,146,807	329,095	23,639,260
Total utility plant being depreciated	164,633,971	5,780,381	1,280,029	169,134,323
Less accumulated depreciation for:				
Distribution system	39,050,038	3,148,164	1,058,799	41,139,403
Transmission system	6,343,540	502,215	210,236	6,635,519
Hydraulic system	639,831	20,141	-	659,972
General plant	9,221,913	858,083	329,095	9,750,901
Total accumulated depreciation	55,255,322	4,528,603	1,598,130	58,185,795
Total utility plant being depreciated, net	109,378,649			110,948,528
Total utility plant, net	$ 117,446,859			$ 120,332,448
COWLITZ FALLS SYSTEM GENERATION				
Utility plant not being depreciated				
Land	$ 7,483,000	$ -	$ -	$ 7,483,000
Utility plant being depreciated				
Hydraulic system	148,212,624	-	-	148,212,624
Transmission system	1,871,394	40,790	23,096	1,889,088
General plant	563,110	-	-	563,110
Total plant being depreciated	150,647,128	40,790	23,096	150,664,822
Less accumulated depreciation				
Hydraulic system	67,151,243	3,064,288	-	70,215,531
Transmission system	150,755	9,777	-	160,532
General plant	52,561	2,005	-	54,566
Total accumulated depreciation	67,354,559	3,076,070	-	70,430,629
Total plant being depreciated, net	83,292,569			80,234,193
Total plant, net	$ 90,775,569			$ 87,717,193

Note 4 – Utility Plant (continued)

Utility plant activity for the year ended December 31, 2014 is as follows:

	Balance December 31, 2013	Additions	Retirements	Balance December 31, 2014
ELECTRIC SYSTEM				
Utility plant not being depreciated				
Land	$ 4,822,998	$ -	$ -	$ 4,822,998
Construction in progress	3,461,722	4,343,984	4,681,627	3,124,079
Intangible	121,133	-	-	121,133
Total utility plant not being depreciated	8,405,853	4,343,984	4,681,627	8,068,210
Utility plant being depreciated				
Distribution system	114,534,397	4,549,286	986,740	118,096,943
Transmission system	22,480,803	152,653	97,506	22,535,950
Hydraulic system	1,179,530	-	-	1,179,530
General plant	21,907,848	913,700	-	22,821,548
Total utility plant being depreciated	160,102,578	5,615,639	1,084,246	164,633,971
Less accumulated depreciation for:				
Distribution system	37,209,025	3,069,827	1,228,814	39,050,038
Transmission system	5,864,166	500,682	21,308	6,343,540
Hydraulic system	619,690	20,141	-	639,831
General plant	8,444,271	777,642	-	9,221,913
Total accumulated depreciation	52,137,152	4,368,292	1,250,122	55,255,322
Total utility plant being depreciated, net	107,965,426			109,378,649
Total utility plant, net	$ 116,371,279			$ 117,446,859
COWLITZ FALLS SYSTEM GENERATION				
Utility plant not being depreciated				
Land	$ 7,483,000	$ -	$ -	$ 7,483,000
Utility plant being depreciated				
Hydraulic system	148,212,624	-	-	148,212,624
Transmission system	1,871,394	-	-	1,871,394
General plant	534,169	28,941	-	563,110
Total plant being depreciated	150,618,187	28,941	-	150,647,128
Less accumulated depreciation				
Hydraulic system	63,566,026	3,585,217	-	67,151,243
Transmission system	140,978	9,777	-	150,755
General plant	50,556	2,005	-	52,561
Total accumulated depreciation	63,757,560	3,596,999	-	67,354,559
Total plant being depreciated, net	86,860,627			83,292,569
Total plant, net	$ 94,343,627			$ 90,775,569

Note 5 – Pension Plans and Other Post-Employment Benefit Plans

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

	Aggregate Pension Amounts	
	2015	2014
Pension liabilities	$ 8,040,499	$ 5,760,748
Deferred outflows of resources	1,221,116	438,801
Deferred inflows of resources	1,239,737	2,555,065
Pension expense/expenditures	1,132,956	743,859

State sponsored pension plans – Substantially all 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.

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.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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

Contributions – The PERS Plan 1 member contribution rate is established by State statute at 6 percent. The employer contribution rate is developed by the Office of the State Actuary and includes an administrative expense component that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates. The PERS Plan 1 required contribution rates (expressed as a percentage of covered payroll) for 2015 were as follows:

	PERS Plan 1 Actual Contribution Rates	
	Employer	Employee*
January through June 2015	9.21%	6.00%
July through December 2015	11.18%	6.00%
January through December 2014	9.21%	6.00%

* For employees participating in JBM, the contribution rate was 12.26%

The District's actual contributions to the plan UAAL were $416,345 and $365,611 for the years ended December 31, 2015 and 2014, respectively.

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.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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 2015 were as follows:

	PERS Plan 2/3 Actual Contribution Rates	
	Employer 2/3	Employee 2*
January through June 2015	9.21%	4.92%
July through December 2015	11.18%	6.12%
Employee PERS Plan 3		varies
January through December 2014	9.21%	4.92%
Employee PERS Plan 3		varies

* For employees participating in JBM, the contribution rate was 15.30%

The District's actual contributions to the plan, excluding the Plan 1 UAAL component, were $534,503 and $452,689 for the years ended December 31, 2015 and 2014, respectively.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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

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

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

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

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

- The OSA updated demographic assumptions, consistent with the changes from the *2007-2012 Experience Study Report*, used when valuing the PERS 1 and TERS 1 Basic Minimum COLA.
- The OSA corrected how valuation software calculates a member's entry age under the entry age normal actuarial cost method. Previously, the funding age was rounded, resulting in an entry age one year higher in some cases.
- For purposes of calculating the Plan 2/3 Entry Age Normal Cost contribution rates, the OSA now uses the current blend of Plan 2 and Plan 3 salaries rather than using a long-term membership assumption of two-thirds Plan 2 members and one-third Plan 3 members.
- The OSA changed the way it applies salary limits, as described in the *2007-2012 Experience Study Report*.

Discount rate – The discount rate used to measure the total pension liability for all DRS plans was 7.5 percent.

To determine that rate, an asset sufficiency test included an assumed 7.7 percent long-term discount rate to determine funding liabilities for calculating future contribution rate requirements. (All plans use 7.7 percent except LEOFF 2, which has assumed 7.5 percent). Consistent with the long-term expected rate of return, a 7.5 percent future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue being made at

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

contractually required rates (including PERS 2/3, PSERS 2, SERS 2/3, and TRS 2/3 employers, whose rates include a component for the PERS 1, and TRS 1 plan liabilities). Based on these assumptions, the pension plans' fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.5 percent was used to determine the total liability.

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

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

Asset Class	Target Allocation	% Long-Term Expected Real Rate of Return Arithmetic	
		2015	2014
Fixed income	20%	1.70%	0.80%
Tangible assets	5%	4.40%	4.10%
Real estate	15%	5.80%	5.30%
Global equity	37%	6.60%	6.05%
Private equity	23%	9.60%	9.05%
	100%		

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

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
PERS 1	$ 5,201,166	$ 4,271,996	$ 3,472,995
PERS 2/3	$ 11,019,299	$ 3,768,503	$ (1,783,159)

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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, pension expense, and deferred outflows of resources and deferred inflows of resources related to pensions – At June 30, 2015 and 2014, the District reported the following total pension liability:

	2015	2014
PERS 1	$ 4,271,996	$ 3,798,411
PERS 2/3	3,768,503	1,962,337
	$ 8,040,499	$ 5,760,748

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

	Proportionate Share June 30, 2014	Proportionate Share June 30, 2015	Change in Proportion
PERS 1	0.075402%	0.081668%	0.006266%
PERS 2/3	0.097080%	0.105470%	0.008390%

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.*

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

Pension expense – For the years ended December 31, 2015 and 2014, the District recognized $1,132,956 and $743,859, respectively, of pension expense.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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

	Deferred Outflows of Resources	Deferred Inflows of Resources
PERS 1		
Differences between expected and actual experience	$ -	$ -
Net difference between projected and actual investment earnings on pension plan investments	-	233,725
Changes of assumptions	-	-
Changes in proportion and differences between contributions and proportionate share of contributions	-	-
Contributions subsequent to the measurement date	308,148	-
Total	$ 308,148	$ 233,725
PERS 2/3		
Differences between expected and actual experience	$ 400,593	$ -
Net difference between projected and actual investment earnings on pension plan investments	-	1,006,012
Changes of assumptions	6,072	-
Changes in proportion and differences between contributions and proportionate share of contributions	269,961	-
Contributions subsequent to the measurement date	236,342	-
Total	$ 912,968	$ 1,006,012
Combined PERS 1 and PERS 2/3		
Differences between expected and actual experience	$ 400,593	$ -
Net difference between projected and actual investment earnings on pension plan investments	-	1,239,737
Changes of assumptions	6,072	-
Changes in proportion and differences between contributions and proportionate share of contributions	269,961	-
Contributions subsequent to the measurement date	544,490	-
Total	$ 1,221,116	$ 1,239,737

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

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

		PERS 1
Year ended December 31,	2016	$ 90,584
	2017	90,584
	2018	90,584
	2019	(38,027)

		PERS 2/3
Year ended December 31,	2016	193,736
	2017	193,736
	2018	193,736
	2019	(251,822)

As of December 31, 2014, pension related deferred outflows of resources of $438,801 were due to employer contributions subsequent to the measurement date, and deferred inflows of resources of $2,555,065 were due to net differences between projected and actual investment earnings on pension plan investments.

Deferred compensation plan – The District maintains a deferred compensation plan (Internal Revenue Code Section 457) for all eligible employees. The plan is entirely funded by voluntary employee contributions. The District has entered into a contractual relationship with the State of Washington Deferred Compensation Program placing all plan assets into trust for the exclusive benefit of participants and their beneficiaries.

Post-Retirement Benefits Plan Other than Pensions Plan (OPEB) description – The District provides post-retirement health care benefits for retired employees until age 65. Prior to April 1, 2008, these benefits paid for 97% of the medical premiums of retirees through age 65. Effective April 1, 2008 the District pays 95% of the medical premiums of retirees up to the age of 65. Spouses and dependents of retirees' benefits are not paid under the plan but can access the plan on a self-pay basis. Employees that retire with disability retirement under Washington State PERS may continue their health insurance coverage through the District with the same coverage provisions as other retirees. Currently, 11 retirees and 106 active employees are covered under the plan.

Funding policy – The contribution requirements of plan participants are established by the District and may be amended from time to time. It is the District's intent to expense the actuarially determined OPEB cost annually.

Note 5 – Pension Plans and Other Post-Employment Benefit Plans (continued)

Annual OPEB cost – The District's annual OPEB cost is calculated based on the annual required contribution of the employer (ARC). The ARC is an amount actuarially determined, based on the entry age normal method, determined in accordance with the guidance of GASB Statement 45.

The ARC represents level funding, that if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial accrued liabilities over a period not to exceed thirty years. The District's estimated contributions for 2015 of $141,173 were less than the current year ARC of $163,909 and therefore, as of December 31, 2015, the District had an OPEB obligation of $531,507. The District's estimated contributions for 2014 of $137,595 were less than the annual ARC of $166,182 and therefore, as of December 31, 2014, the District had an OPEB obligation of $508,771.

Other actuarial assumptions include a rate of return on investments of present and future assets of 3.0%. The health care benefit rate is assumed to increase 9.0% in 2015, and then decreasing to 5.0% annually over 8 years and remaining at 5.0% thereafter. Dental premiums are assumed to increase by 3.0% in all future years.

The District's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2015, 2014 and 2013 were as follows:

Fiscal Year Ending	Annual OPEB Cost	Percentage of Annual OPEB Cost Funded	Net OPEB Obligation
December 31, 2015	$ 163,909	86.1%	$ 531,507
December 31, 2014	166,182	82.8%	508,771
December 31, 2013	223,365	61.8%	480,184

Funding status and funding progress – As of January 1, 2014, the most recent actuarial valuation date, the plan was not funded (0%). The actuarial accrued liability for benefits was $2.2 million, and the actuarial value of assets was zero, resulting in an unfunded actuarial accrued liability (UAAL) of $2.2 million.

The following table presents a schedule of funding progress for the District's OPEB Plan:

Actuarial Valuation Date	Actuarial Value of Assets	Entry Age Normal AAL (b)	UAAL (b – a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b – a) / c)
January 1, 2015	$ -	$ 2,251,301	$ 2,251,301	0%	$ 9,930,915	25%
January 1, 2014	-	2,227,272	2,227,272	0%	8,857,441	25%
January 1, 2013	-	2,895,484	2,895,484	0%	8,314,762	35%

Note 5 – Pension, Deferred Compensation Plan, and Post-Retirement Benefits (continued)

Actuarial valuations on an ongoing plan involve estimates of the value reported and assumptions about the probability of occurrence of events into the future. Examples include assumptions about future employment, composition of employees, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revisions as actual results are compared with past expectations and new estimates are made about the future.

Note 6 – Purchased Power Contracts

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 20-year Block and Slice Power Sale Agreement, which was signed on November 24, 2008, commenced on October 1, 2011, and extends through September 30, 2028. This contract provides federal power in the form of two products: Block and Slice. The monthly Block purchase amounts are fixed hourly values each month, but are shaped somewhat to closer align with the District's monthly power requirements/ The non-Slice allocation or Block portion is 0.57041% for fiscal year 2015. The Slice product provides the District 0.96216% of the output of the federal system for fiscal year 2015.

BPA is required by federal law to recover all of its costs through the rates it charges its customers. BPA makes various filings with FERC to confirm that rates are sufficient to cover costs. Under BPA's adopted power and transmission rate provisions, its rates are subject to revision in order to enable BPA to recover its actual costs of service.

Beginning October 1, 2011, BPA changed its rate-making methodology to a tiered rate approach. Each public utility (preference) customer received a High Water Mark (HWM) based on either its 2010 load or average 2007-2008 loads 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. Both Block and Slice and non-Slice (Load Following) customers' HWMs are translated into "Tier 1 Cost Allocators" (TOCAs) which, when multiplied by the estimated costs of the federal system, determine their power costs. The District's TOCA for fiscal year 2016 and 2015 is 1.54138 and 1.53257%, respectively. There is an additional monthly load shaping charge (or credit) for the Block product, determined by the shape of customers' loads compared to the actual shape of the Federal Columbia River Power System (FCRPS). If preference customers want to buy more BPA power beyond their HWM, it will be sold at a BPA Tier 2 rate set to fully recover BPA's cost of securing additional resources to serve that customer's load. The customer also has the option of serving some or all of their above-HWM load *with n*on-federal resources. The District elected not to purchase any Tier 2 products from BPA during the first purchase period, October 2011 through September 2014, or during the second purchase period, October 2014 through September 2019. The District has surplus energy, on average, over this time period.

Note 6 – Purchased Power Contracts (continued)

The rate provisions for the Block product include a Cost Recovery Adjustment Clause (CRAC) and a Dividend Distribution Clause (DDC). Either may be triggered if certain thresholds are met. The CRAC allows BPA to raise rates to collect sufficient funds to pay costs. The 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 Slice true-up mechanism.

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

Energy Northwest – The District is a member of Energy Northwest and a participant in Nuclear Project Nos. 1 and 3 (terminated projects), Columbia Generating Station, the Packwood Lake Hydroelectric Project, and the Nine Canyon Wind Project.

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 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 entered into "Net Billing Agreements" with Energy Northwest and the BPA. Under terms of these agreements, the District purchased a maximum of 1.276% of the capacity of Energy Northwest Nuclear Projects (WNP) 1, 2.274% of WNP 2 (now Columbia Generating Station) and 1.103% of Energy Northwest's 70% ownership share of WNP 3. The District in turn sold this capability to BPA. Under the "Net Billing Agreements," 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, including debt service on revenue bonds issued to finance the projects, whether or not the projects are completed, operable or operating and notwithstanding the suspension, reduction or curtailment of the projects' outputs. WNP 2 commenced commercial operation in December 1984. On November 19, 1984, the District withdrew its membership in Energy Northwest and participated in Energy Northwest Projects as a non-member for nearly 25 years. On April 27, 2009, the District approved a resolution to make application to become a member of the Energy Northwest and Energy Northwest Board approved the District's membership on July 23, 2009.

Note 6 – Purchased Power Contracts (continued)

Packwood Lake Hydroelectric Project – The District is a 14.25% 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. The participants' original Packwood Agreements with Energy Northwest obligated the 12 participants to pay annual costs and receive excess revenues. Energy Northwest recognizes revenues equal to expenses for each period. No net income 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 terms are similar to the original 1962 agreements, wherein the participants are obligated for a percentage of the Project costs. However, seven of the participants, including the District, began taking their share of the energy, and four participants with very small shares assigned theirs to Clallam PUD under separate bilateral contracts.

In addition the District and Energy Northwest have entered into a power transmission service agreement. The agreement, in exchange for providing transmission services to wheel Packwood Power from the Project to the BPA transmission system, provides for the District to receive monthly payments adjusted periodically for actual costs. Revenue amounted to $496,508 for the years ended 2015 and 2014, respectively.

Burton Creek Hydroelectric Project – The Burton Creek Hydroelectric Project is located near the east Lewis County town of Packwood. The project is a 560 KWh small hydro owned and operated by a private party. The District previously purchased the output of the Burton Creek Project under a power purchase agreement executed September 29, 2003, at the price of the District's average BPA priority firm monthly energy and demand rates.

The power purchase agreement extended from year to year unless terminated by either party with six months advance notice. Following the 2011 seasonal shutdown, Burton Creek Hydroelectric failed to resume sale and delivery of power. The District terminated the agreement on July 1, 2012 due to default of the sale and delivery obligation.

Not soon after the District terminated the above agreement, an individual notified the District that he had purchased the distressed FERC license for Burton Creek and had approximately one year to repair the facility and move certain Burton Creek components off Federal land and back onto private property. After the project received Qualifying Facility status, the District contracted to purchase the output of the Burton Creek Project effective October 1, 2013. The contract continues through December 31, 2018, unless otherwise terminated per terms in the agreement. Purchase prices are locked in each fall for the ensuing calendar year based on forward Northwest prices.

Note 6 – Purchased Power Contracts (continued)

Renewable Power Supply – 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. This Act mandates renewable energy and conservation targets for the State's electric utilities with more than 25,000 customers. The District complied with its requirements for the annual renewable energy compliance period ended December 31, 2015 and its two-year conservation compliance period ended December 31, 2015. BPA operated wind projects that are part of the FCRPS, as well as Nine Canyon Wind and White Creek Wind contracts will assist in providing the renewable energy the District will need in order to comply with the Act's energy targets in the future. At this time the District can meet its I-937 yearly compliance targets with these aforementioned plants using the 3-year REC shaping allowed in the Act. After 2020, the District will meet any new higher REC requirements using either tradable RECs or through purchase agreements from renewable resources.

Nine Canyon Wind Project (Phase I and III) – Located near the city of Kennewick, WA, Nine Canyon Wind Project is owned by Energy Northwest. The District has signed a Power Purchase Agreement for 2% of the output of Phase I. The District's 2% share represents approximately 1 MW of capacity and based upon a 30% load factor, approximately 2,600 MWh of energy production annually. The District has also signed a Power Purchase Agreement for 15.7% of the output of Phase III. The District's 15.7% share represents approximately 5 MW of capacity and based upon a 30% load factor, approximately 13,100 MWh of energy production annually.

White Creek Wind Project – On June 20, 2008, the District executed agreements with Klickitat County PUD for the acquisition of a 10% share of the output of the 205 megawatt White Creek Wind Project near Goldendale, Washington for the purchase price of $36.85 million. The White Creek Wind Project agreements include but are not limited to the Energy Marketing Agreement. On June 16, 2008, the District issued bonds to finance a portion of the White Creek Wind Project purchase (see Note 13).

The prepaid power agreements are amortized using the straight line method over the 20 year contract period and had amortization in 2015 and 2014 totaling $1,889,538. The District's 10% share represents approximately 20.5 MW of capacity and based upon a 32% load factor, approximately 57,500 MWh of energy production annually.

Power management – In 2011, the District entered into a power management services agreement with The Energy Authority Inc. (TEA) to provide certain power scheduling, purchasing, sales and related services to assist in the short term management of the District's power supply. Power purchases and sales are managed by the District in accordance with adopted risk management policies.

Note 7 – Derivative Instruments

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

	Changes in Fair Value		Fair Value at December 31, 2015		
	Classification	Amount	Classification	Amount	Notional
Cash Flow Hedges:					
Financial Swap Forward	Deferred Inflow	$ 403,842	Derivative Asset	$ 403,842	MWH
Financial Swap Forward	Deferred Outflow	104,432	Derivative Liability	104,432	MWH

The fair values of the financial swap contracts were based on the futures price curve for the Mid-Columbia Intercontinental Exchange for electricity. The financial swaps were entered into between November 2013 and December 2015, with maturity dates through June 2017.

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:

<u>Surplus Purchased Power Resources</u> – The District hedges projected surpluses in future periods by locking in a forward price. Surplus power is generally sold forward at a fixed-price, either physically or financially, when the probability of surplus is high.

<u>Deficit Power Resources</u> – The District hedges projected power resource deficits in future periods by purchasing power. Power is generally purchased to cover projected deficits at a fixed price, either physically or financially, when the probability of the deficit position is high.

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

- Physical power forward purchases and sales
- Monthly and daily power physical calls and puts
- Power and natural gas fixed for floating swaps
- Monthly financial Asian power call and put options
- Financial daily power put and call options
- Monthly power swaptions

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

Credit risk – The District is a member of The Energy Authority, Inc. (TEA). The District adheres to the credit policies and credit limits agreed to by TEA and the District. 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.

Note 7 – Derivative Instruments (continued)

All physical commodity 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. As of December 31, 2015, the District had 11 counterparties. The maximum credit extended to any one counterparty is $1.75 million.

The District entered into master enabling agreements with various counterparties, which enable hedging transactions. Such agreements include the 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 ISDA agreements are used to financially hedge monthly long or short positions to reduce the risk of an underlying physical position by using Risk Management Committee approved financial instruments.

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, 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 Intercontinental Exchange index and all gas transactions are to be settled on the relevant Sumas/Huntingdon index.

Termination risk – As of December 31, 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 not generally fall under the events of default provisions, unless the non-performing party fails to pay the resulting liquidated damages as they come due.

Note 8 – District Hydroelectric Projects

Cowlitz Falls Project – The Cowlitz Falls Project is located on the upper Cowlitz River in eastern Lewis County, Washington upstream from two existing hydroelectric projects, Mayfield and Mossyrock, owned by the City of Tacoma. The Project includes a concrete gravity dam and powerhouse, a reservoir covering about 610 acres extending approximately 10 miles up the Cowlitz River and 1.5 miles of the Cispus River, and 5.2 miles of overland transmission line to the District's Glenoma Substation.

Note 8 – District Hydroelectric Projects (continued)

The powerhouse contains two Kaplan turbine generating units with net installed capacity of 35 MW each at a rated head of 87.5 feet. Average annual energy generation is estimated at 261 million kilowatt hours. Project operation depends upon the "run of the river" to produce the maximum amount of electric energy, instead of extensively regulating the reservoir behind the dam to maximize the Project's firm or dependable capacity.

In June 1986, the District was granted a license by FERC to proceed with the development and construction of the Cowlitz Falls Project. On May 23, 1991 the District and BPA executed an Amendatory Power Purchase Contract. Construction of the Project began in July 1991 and the Project began commercial operation on June 29, 1994.

Revenues for the Cowlitz Falls System are recognized on the basis of the Amendatory Power Purchase Contract between the District and BPA. Through this contract, BPA receives all output from the Cowlitz Falls Project in exchange for payment of all operation and maintenance costs and debt service on Cowlitz Falls revenue bonds (see Note 12). The District receives monthly operation and maintenance payments from BPA based upon an annual budget of operating and capital project expenditures. Certain operation and maintenance costs are subject to incentive or reimbursement provisions if actual expenses are less or more than certain budgeted amounts. The District did not receive any incentive payments for the years ended December 31, 2015 and 2014. Debt service payments are made by BPA directly to the Bond transfer agent for payment of scheduled bond interest and principal.

The District records the Cowlitz Falls System activity reflecting the cost reimbursement basis of the Amendatory Power Purchase Contract with BPA. As a result, revenues and costs offset one another with no resulting net income or loss. The Cowlitz Falls System consists of essentially two activities, plant construction and related debt service, and operations and maintenance. For related debt service, revenue is recognized primarily for BPA debt service payments. Expenses consist of interest on the outstanding revenue bonds, depreciation, and amortization of bond costs. For operations and maintenance, revenue is recognized primarily for BPA operation and maintenance advances, and interest income on unspent advances. Expenses consist of operation and maintenance costs, including plant renewals and replacements, and taxes.

As part of the contract, the District (Electric System) provides power transmission services to BPA over facilities of both the City of Tacoma (Tacoma) and the District. The terms and conditions for the use of the Tacoma facilities are governed by an agreement between Tacoma and the District. Costs are passed to BPA as part of the District's contract with BPA. Revenue amounted to $973,226 and $940,975 for the years ended 2015 and 2014, respectively.

Mill Creek Hydroelectric Project – The Mill Creek Hydroelectric Project is located on Mill Creek, a tributary to the Cowlitz River, near Salkum, Washington and the Cowlitz Salmon Hatchery. The project includes a six foot high concrete diversion structure, 1,500 feet of 42 inch concrete cylinder pipe and a concrete block powerhouse downstream. The powerhouse contains two Francis turbine induction generating units with net installed capacity of 300 KW each at an average head of 96 feet.

Note 9 – Conservation Programs

The District has participated in BPA programs over the past several years to more aggressively seek out and acquire energy efficiency savings. On March 3, 2004, the District signed a Purchase of Conservation Agreement with BPA for the purpose of offering conservation under a program known as "Conservation as Part of Augmentation" (ConAug). On July 10, 2006, the District signed a Conservation Acquisition Agreement (CAA) with BPA for purpose of offering conservation to commercial and industrial customers. On September 22, 2009 the District executed the "Energy Conservation Agreement" (ECA) with BPA to continue efforts begun under the ConAug and CAA agreements. The District continues to offer commercial and industrial energy efficiency measures through the ECA program.

In 2009, the District completed a Conservation Potential Assessment (CPA) as part of the requirements under the Energy Independence Act adopted with passage of Initiative 937. The CPA developed 20 year and 10 year conservation plans with a defined target equaling 20% of the corresponding 10 year potential starting in 2010. Every two years the District must update the CPA with new information and establish a new target for the subsequent two year period. The CPA for the 2014-2015 biennium set the energy savings target for this period at 1.32 aMW, or approximately 5,782 MWh for each year. Through conservation programs described above and indirect savings acquired through the activities of NEEA, the District was able to exceed the 2014-2015 target.

Note 10 – Fiber Optic Activity

The District's fiber optic based communication system consists of approximately 60 miles of overhead ADSS fiber optic cable, primarily following the District's transmission routes. The District is constructing the system to support its Electric System with communication between its offices and various substations located throughout Lewis County.

The District has also leased portions of excess dark fibers to telecommunication companies, BPA, non-profit, and governmental agencies. Expansion of the system may occur where it best meets the District's communication needs.

Note 10 – Fiber Optic Activity (continued)

Selected financial data is reported as follows:

	2015	2014
Telecommunication services		
Operating revenues		
Dark fiber leases	$ 305,190	$ 294,988
Total operating revenues	305,190	294,988
Operating expenses		
Operating expenses	1,416	414
Maintenance expense	9,904	6,081
Depreciation expense	79,199	78,266
Total operating expenses	90,519	84,761
Net operating revenue	$ 214,671	$ 210,227
Capital investment		
Net telecommunication plant	$ 1,456,889	$ 1,286,576

Note 11 – PURMS Self–Insurance Agreement

The District and eighteen other PUD's participate in a joint self-insurance pool in affiliation with Public Utility Risk Management Services (PURMS).

Liability risk pool – PURMS provides liability insurance coverage for its members participating in the Liability Risk Pool (Liability Pool) and to a limited extent for the benefit of their employees under an agreement entitled "PURMS Joint Self-Insurance Agreement" (amended and restated as of November 10, 2011, "SIA"). Under SIA, the Liability Pool had a self-insured retention of $1,000,000 per occurrence, which was the Coverage Limit in effect for 2015, and in effect as of December 31, 2015.

The Liability Pool is funded through assessments of its participating members. Assessments are levied at the beginning of each calendar year to replenish the Liability Pool to its designated risk pool balance, and at any time during the year that either (a) the actual risk pool balance becomes $500,000 less than the designated risk pool balance or (b) the risk pool balance is depleted to the amount of 70% funding level established by the actuarial report for the liability pool. For calendar year 2015, the designated risk pool balance was $3,000,000.

At all times, PURMS also maintains excess liability insurance for its members in the Liability Pool. For the year 2015, the amount of such excess insurance was $35,000,000.

Note 11 – PURMS Self–Insurance Agreement (continued)

As of December 31, 2015, there were 14 known incidents and/or unresolved liability claims pending against one or more members or former members of PURMS' Liability Pool. The total dollar value of the risk posed by these claims to such members and to the Liability Pool itself is unknown. Accordingly, no provision has been included in the accompanying financial statements.

Property risk pool – PURMS provides property insurance for its members participating in the Property Risk Pool (Property Pool) in accordance with the terms of the SIA (identified above). Under the SIA, from its inception in 1997 to the present, the Property Pool has had a self-insured retention (or Property Coverage Limit) of $250,000 per property loss.

The Property Pool is funded to the amount of its Designated Property Pool Balance, which in 2015 was $750,000. The Property Pool's operations are financed through assessments of its Members in accordance with the terms of the Property General Assessment Formula. A Property Assessment is issued automatically at the beginning of each calendar year to replenish the Property Pool to its Designated Balance. Property Assessment are also issued at any time during the year that the Actual Property Pool Balance drops below $500,000 or is depleted to the amount of the 70% funding level established by the annual actuarial report for the Property Pool.

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

At all times, PURMS also maintains excess property insurance for its members in the Property Risk Pool. For the year 2015, the amount of such excess insurance was $200,000,000.

Note 12 – Cowlitz Falls Hydroelectric Project Revenue Bonds

In July 2013, the Board issued $87,995,000 in Cowlitz Falls Hydroelectric Project Revenue Refunding Bonds to refund the series 2003 bond issues, with an average interest rate of 4.79%. The balance of the refunding included proceeds from premium on issue of $12,278,112. Underwriting fees and other issuance costs totaled $925,151. The loss on refunding was $5,284,305 and is being charged to operations through the year 2024 using the effective interest method.

Note 12 – Cowlitz Falls Hydroelectric Project Revenue Bonds (continued)

The 2013 Bonds are special limited obligations of the District secured by a lien and charge on the Cowlitz Falls revenues and bond insurance. Pursuant to a Power Purchase Contract and Payment Agreement all Project output has been sold to BPA. BPA is obligated to pay all operation and maintenance costs including debt service on the Bonds, whether or not the Dam is operating or operable (see Note 8).

	2015	2014
2013 Revenue Bonds to refund 2003 revenue bonds due April 1, 2032	$ 82,055,000	$ 85,055,000
Less current maturities	3,150,000	3,000,000
Long-term portion of revenue bonds	$ 78,905,000	$ 82,055,000

Scheduled debt service deposits for principal, interest and principal maturities are as follows:

	Sinking Funds			
	Principal	Interest	Total	Principal Maturities
2016	$ 3,150,000	$ 4,149,413	$ 7,299,413	$ 3,150,000
2017	3,310,000	3,991,912	7,301,912	3,310,000
2018	3,475,000	3,826,413	7,301,413	3,475,000
2019	3,650,000	3,652,662	7,302,662	3,650,000
2020	3,830,000	3,470,163	7,300,163	3,830,000
2021 – 2025	22,230,000	14,268,425	36,498,425	22,230,000
2026 – 2030	28,635,000	7,863,525	36,498,525	28,635,000
2031 – 2032	13,775,000	826,707	14,601,707	13,775,000
	$ 82,055,000	$ 42,049,220	$ 124,104,220	$ 82,055,000

Note 13 – Electric System Revenue Bonds, Series 2008

In June, 2008 the District issued two series of revenue bonds in the aggregate amount of $36,690,000 to finance capital improvements to the Electric System and acquire the right to energy and other attributes from the White Creek Wind Project (see Note 6). The bonds consist of two series, Series 2008A, in the principal amount of $19,415,000 with an interest rate of 5.00%, and Series 2008B (Taxable) in the principal amount of $17,275,000 with interest rates ranging from 3.64% to 5.32%.

Note 13 – Electric System Revenue Bonds, Series 2008 (continued)

These bonds are subject to covenants which specify the order of application of gross revenue requirements and which require the District to: pay costs of maintenance and operations; costs associated with the generation, conservation, transformation, transmission or distributions of power and energy acquired or purchased or constructed by the District; and to make all payments required to be made into the Bond Account. Other covenants also apply. The 2008 Series bonds were issued with a premium of $1,146,751 and had underwriting fees and other issuance costs of $982,888, both of which are amortized on the effective interest method over the life of the bonds.

Scheduled debt service deposits for principal and interest and principal maturities are as follows:

	Series 2008 A			
	Principal	Interest	Total	Principal Maturities
2016	$ -	$ 970,750	$ 970,750	$ -
2017	-	970,750	970,750	-
2018	-	970,750	970,750	-
2019	1,760,000	970,750	970,750	1,760,000
2020	1,850,000	882,750	2,732,750	1,850,000
2021 – 2025	10,725,000	2,931,000	13,656,000	10,725,000
2026 – 2027	5,080,000	384,000	5,464,000	5,080,000
	$ 19,415,000	$ 8,080,750	$ 25,735,750	$ 19,415,000

	Series 2008 B			
	Principal	Interest	Total	Principal Maturities
2016	$ 1,945,000	$ 382,159	$ 2,327,159	$ 1,945,000
2017	5,275,000	280,630	5,555,630	5,275,000
	$ 7,220,000	$ 662,789	$ 7,882,789	$ 7,220,000

Note 13 – Electric System Revenue Bonds, Series 2008 (continued)

A reconciliation of the Series 2008 bond issuance and the Statement of Net Position is as follows:

Series 2008 A	$ 19,415,000
Series 2008 B	7,220,000
Total	26,635,000
Less current maturities	(1,945,000)
Long-term portion of 2008 Series Bonds	$ 24,690,000

The District issued $9,499,000 in Revenue Bonds in June 1992 for financing a portion of the District's Capital Improvement Program and conservation efforts. The Program made capital improvements and completed conservation efforts of $13 million over a two year period. On November 29, 1994, the District deposited $9,480,300 in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1992 Series bonds.

These refunded bonds constitute a contingent liability of the District only to the extent that cash and investments presently in the control of the refunding trustees are not sufficient to meet debt service requirements, and are therefore excluded from the financial statements because the likelihood of additional funding requirements is considered remote.

Note 14 – Line of Credit

On October 18, 2011, the District and West Coast Bank (now Columbia Bank) entered into a Loan Commitment for a Revolving Line of Credit (LOC) with an available commitment of $5 million bearing an interest rate of 3.25%. The District may either draw on the LOC or request that Columbia Bank issue a letter of credit. The District may use the proceeds of any draws on the LOC to fund short-term cash flow needs caused by variable power supply costs. The initial term of the Loan Commitment expired on October 18, 2013. The LOC was extended for up to an additional 38 months expiring on December 1, 2016. As of December 31, 2015, the District has not drawn on the LOC nor requested the issuance of any letters of credit.

Note 15 – Endangered Species Listing of Salmon and Steelhead/American Rivers Intent to Sue

The National Marine Fisheries Service (NMFS) has listed the lower Columbia Chinook salmon and steelhead trout as threatened under the Endangered Species Act (ESA). The Cowlitz River is a tributary of the lower Columbia River and the Cowlitz Falls Project operates on the upper Cowlitz River.

On January 14, 2000, American Rivers, Trout Unlimited, Friends of the Cowlitz, CPR Fish and the Cowlitz Indian Tribe filed a Notice of Intent to Sue for Violations of the ESA. The Notice claims the FERC, BPA, and District are violating the ESA by continued operation of the Cowlitz Falls Project. American Rivers indicates that unless BPA and FERC initiated consultation under Section 7 of the ESA with NMFS regarding the impact of the Project on listed species, and unless immediate action is taken to bring the Project into compliance, they will file suit against BPA, FERC, and the District.

As a result of the Cowlitz Falls Project operation and the ESA anadromous fish listings, the District (as the non-Federal representative to FERC) initiated consultation with the FERC and NMFS to evaluate possible ESA impacts of the Project. As part of the consultation the District completed a draft Biological Assessment (BA) of the Cowlitz Falls Project benefits, impacts, and operation in March 2002 and submitted it to the FERC. The FERC accepted the draft BA, finalized it and submitted it to NMFS in July 2002.

In June 2009, the NMFS issued a Biological Opinion (BiOp) for the Project which allows limited "Take" of the threatened species. The BiOp was submitted to the FERC for inclusion as a Project License amendment which includes studies and mitigation measures to reduce impacts to the species at the Project. As of this time the FERC has not acted on the BiOp. In the interim, the District has evaluated and/or implemented many of the reasonable and prudent measures for protection of the species at the Project. On April 9, 2013, NMFS updated the BiOp's Incidental Take Statement and study schedule.

On June 20, 2014, Tacoma Power, BPA and the District signed the "Northshore Project Easement Agreement" whereby BPA signed over ownership of the Cowlitz Falls Fish Facility (CFFF) and the Stress Relief Ponds (located at the downstream salmon hatchery). The District agreed to provide access and easement areas to Tacoma Power so that a new fish collection facility could be combined with the existing CFFF. Tacoma Power's goal is to improve fish collection efficiencies to 95%. On August 18, 2014, FERC issued an "Order Approving Non-Project Use of Project Lands" thereby approving the easement to allow Tacoma Power to build the new collector. Tacoma Power broke ground for the collector in June 2015.

As stated in Note 8, BPA pays all operation and maintenance costs of the Cowlitz Falls Project. As such, the above matters are not expected to impact the District's financial position.

Note 16 – Change in Accounting Principle

With the implementation of GASB Statements No. 68 and 71, the District restated its 2014 financial statements. In accordance with these statements, the District now recognizes liabilities, deferred outflows and inflows of resources relating to pension obligations. As a result, the District decreased its beginning net position as of January 1, 2014 by $7,060,673. The impact on the Statement of Net Position as of December 31, 2014 is as follows:

	2014 Restated	2014 As Originally Reported	Increase (Decrease)
Statement of Net Position			
Accumulated depreciation	$ 123,426,222	$ 122,609,883	$ 816,339
Pension deferred outflow	438,801	-	438,801
Pension liability	5,760,748	-	5,760,748
Pension deferred inflow	2,555,065	-	2,555,065
Unrestricted net position	7,374,618	14,435,291	(7,060,673)

REPORT OF INDEPENDENT AUDITORS 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*

Board of Commissioners
Public Utility District No. 1 of Lewis County
Chehalis, Washington

We have audited, in accordance with the 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, which comprise the statement of net position as of December 31, 2015, and the related combined and separate statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the combined statement of net position as of December 31, 2014, and the related combined statement of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements of the Public Utility District No. 1 of Lewis County's Electric System and Cowlitz Falls System (the District), which collectively comprise the Public Utility District No. 1 of Lewis County's financial statements, and have issued our report thereon dated May 27, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit, 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 combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity'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.

REPORT OF INDEPENDENT AUDITORS 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* (continued)

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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether District's financial statements are free of material misstatement, we performed tests of its 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 result of that testing, and not to provide an opinion on the effectiveness of the entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Moss Adams LLP

Portland, Oregon
May 27, 2016

REQUIRED SUPPLEMENTARY INFORMATION

PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
SCHEDULE OF PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
AS OF JUNE 30, 2015

	PERS Plan 1	
	2015	2014
Proportion of the net pension liability	0.081668%	0.075402%
Proportionate share of the net pension liability	$ 4,271,996	$ 3,798,411
Covered - employee payroll	$ -	$ -
Employers proportionate share of the net pension liability as percentage of covered-employee payroll	0%	0%
Plan fiduciary net position as a percentage of the total pension liability	59%	61%

	PERS Plan 2/3	
	2015	2014
Proportion of the net pension liability	0.105470%	0.097080%
Proportionate share of the net pension liability	$ 3,768,503	$ 1,962,337
Covered - employee payroll	$ 9,505,771	$ 9,062,013
Employers proportionate share of the net pension liability as percentage of covered-employee payroll	40%	22%
Plan fiduciary net position as a percentage of the total pension liability	89%	93%

Note to Schedule: The ten year information wil be provided as it is avaiable.

PUBLIC UTILITY DISTRICT NO. 1 OF LEWIS COUNTY
SCHEDULE OF CONTRIBUTIONS
AS OF DECEMBER 31, 2015

PERS Plan 1

	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006
Statutorily or contractually required contribution	$ 416,345	$ 365,611	$ 258,054	$ 98,363	$ 13,517	$ 14,645	$ 20,458	$ 35,441	$ 31,667	$ 21,590
Contributions in relation to the statutorily or contractually determined contribution*	(416,345)	(365,611)	(258,054)	(98,363)	(13,517)	(14,645)	(20,458)	(35,441)	(31,667)	(21,590)
Contribution deficiency (excess)	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Covered-employee payroll	$ -	$ -	$ -	$ 62,119	$ 236,269	$ 284,344	$ 301,573	$ 528,311	$ 579,605	$ 766,297
Contributions as a percentage of covered-employee payroll	N/A	N/A	N/A	158.35%	5.72%	5.15%	6.78%	6.71%	5.46%	2.82%

PERS Plan 2/3

	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006
Statutorily or contractually required contribution	$ 534,503	$ 452,689	$ 389,337	$ 466,380	$ 438,966	$ 357,812	$ 445,921	$ 409,089	$ 296,445	$ 143,776
Contributions in relation to the statutorily or contractually determined contribution	(534,503)	(452,689)	(389,337)	(466,380)	(438,966)	(357,812)	(445,921)	(409,089)	(296,445)	(143,776)
Contribution deficiency (excess)	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Covered-employee payroll	$ 9,505,771	$ 9,062,013	$ 8,152,293	$ 7,970,187	$ 7,321,077	$ 6,947,727	$ 6,593,033	$ 5,847,830	$ 5,388,767	$ 5,027,644
Contributions as a percentage of covered-employee payroll	5.62%	5.00%	4.78%	5.85%	6.00%	5.15%	6.76%	7.00%	5.50%	2.86%

* Effective July 2012 a certain portion of contributions from PERS Plan 2/3 is allocated to PERS Plan 1 in order to fund its unfunded acturial accrued liability (UAAL)