



Office of the Washington State Auditor
Pat McCarthy

Financial Statements Audit Report
Public Utility District No. 1 of Grays
Harbor County

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

Published September 29, 2017

Report No. 1020003





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

September 29, 2017

Board of Commissioners
Public Utility District No. 1 of Grays Harbor County
Aberdeen, Washington

Report on Financial Statements

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

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

Sincerely,

Pat McCarthy
State Auditor
Olympia, WA

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SCHEDULE OF AUDIT FINDINGS AND RESPONSES

Grays Harbor County Public Utility District No. 1 Grays Harbor County January 1, 2016 through December 31, 2016

2016-001 The District's internal controls over accounting and financial reporting were not sufficient to ensure financial statements are accurate and complete.

Background

The Board of Commissioners, state and federal agencies, and the public rely on the information included in financial statements and reports to make decisions. District management has the responsibility to design and implement internal controls that provide reasonable assurance regarding the reliability of financial reporting.

Our audit identified a significant deficiency in internal controls that affects the District's ability to produce reliable financial statements.

Description of Condition

The Governmental Standards Accounting Board issued Statement No. 45 in 2004, which required local governmental employers who provide other postemployment benefits (OPEB) to recognize and display OPEB expenses and related liabilities (assets), note disclosures and RSI in their financial reports. This is a multifaceted standard that is currently being updated which adds to the complexity of these reporting requirements.

The District lacked an effective preparation and review process to ensure the accuracy of the financial statements. Specifically, the District did not accurately report Other Post Employment Benefit (OPEB) balances.

Cause of Condition

The District lacked adequate understanding over their OPEB reporting to ensure balances were accurately presented.

Effect of Condition

Our audit identified an error on the original Statement of Net Position. Specifically, the District reported a Net OPEB Asset of \$12,722,609, which did not exist.

This misstatement caused errors throughout the District's financial statements and overstated their net position.

The District corrected these errors.

Recommendation

We recommend the District ensure:

- Resources are dedicated to training on and research of the correct reporting for OPEB balances.

District's Response

The District implemented GASB Statement No. 45 in 2008, in accordance with the required implementation date (based on the District's revenues). The District had consistently handled entries for the OPEB balance in the same manor for eight years. Upon inquiry from the Auditor's office, the District re-evaluated the original Standard, and corrected entries related to the OPEB balances. The District's OPEB note disclosures in each of the eight years were accurately stated.

The District agrees that it did not handle the application of the accounting principle accurately. The error resulted in a deferred debit balance on the financial statements, which did not affect cash. Corrections have been made and no further corrective action is necessary.

Auditor's Remarks

We appreciate the District's commitment to resolving the issues identified above. We will review the corrective action taken during our next audit. We thank the District for its cooperation and assistance during the audit.

Applicable Laws and Regulations

RCW 43.09.200 Local government accounting—Uniform system of accounting

Budgeting Accounting and Reporting System (BARS) Manual – Accounting, Accounting Principles and General Procedures, Internal Controls

Government Auditing Standards, December 2011 Revision, paragraph 4.23

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in its Codification of Statements on Auditing Standards, section 265.

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

Public Utility District No. 1 of Grays Harbor County January 1, 2016 through December 31, 2016

Board of Commissioners
Public Utility District No. 1 of Grays Harbor County
Aberdeen, Washington

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Public Utility District No. 1 of Grays Harbor County, Washington, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated September 27, 2017. As discussed in Note 15 to the financial statements, during the year ended December 31, 2016, the District implemented Governmental Accounting Standards Board Statement No. 72, *Fair Value Measurement and Application* and Statement No. 79, *Certain External Investment Pools and Pool Participants*.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of District's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of

deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies 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. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Audit Findings and Responses as Finding 2016-001 that we consider to be significant deficiencies.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of the District's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

DISTRICT'S RESPONSE TO FINDINGS

The District's response to the findings identified in our audit is described in the accompanying Schedule of Audit Findings and Responses. The District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

PURPOSE OF THIS REPORT

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However,

this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

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

Pat McCarthy

State Auditor

Olympia, WA

September 27, 2017

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

Public Utility District No. 1 of Grays Harbor County January 1, 2016 through December 31, 2016

Board of Commissioners
Public Utility District No. 1 of Grays Harbor County
Aberdeen, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of Public Utility District No. 1 of Grays Harbor County, Washington, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed on page 12.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Public Utility District No. 1 of Grays Harbor County, as of December 31, 2016, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Matters of Emphasis

As discussed in Note 15 to the financial statements, in 2016, the District adopted new accounting guidance, Governmental Accounting Standards Board Statement No. 72, *Fair Value Measurement and Application* and Statement No. 79, *Certain External Investment Pools and Pool Participants*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 13 through 15, pension plan information on pages 42 through 45 and information on postemployment benefits other than pensions on page 46 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated September 27, 2017 on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "Pat McCarthy".

Pat McCarthy

State Auditor

Olympia, WA

September 27, 2017

FINANCIAL SECTION

Public Utility District No. 1 of Grays Harbor County January 1, 2016 through December 31, 2016

REQUIRED SUPPLEMENTARY INFORMATION

Management's Discussion and Analysis – 2016

BASIC FINANCIAL STATEMENTS

Statement of Net Position – 2016

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

Statement of Cash Flows – 2016

Notes to Financial Statements – 2016

REQUIRED SUPPLEMENTARY INFORMATION

Schedule of Proportionate Share of Net Pension Liability – PERS 1, PERS 2/3 – 2016

Schedule of Employer Contributions – PERS 1, PERS 2/3 – 2016

Schedule of Other Post-Employment Benefits – 2016

PUBLIC UTILITY DISTRICT No. 1 of GRAYS HARBOR COUNTY
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2016

MANAGEMENT'S DISCUSSION AND ANALYSIS

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

OVERVIEW OF THE FINANCIAL STATEMENTS

Public Utility District No. 1 of Grays Harbor County (District) accounts for its financial activities within a single proprietary fund. The District's financial activities are comprised of purchase, generation, transmission, distribution and sale of electric energy, as well as the sale of wholesale telecommunication services. In accordance with the requirements set forth by the Governmental Account Standards Board, the District's financial statements employ the accrual basis of accounting in recognizing increases and decreases in economic resources. Accrual accounting recognizes all revenues when earned and expenses when incurred during the year, regardless of when cash is received or paid. The basic financial statements are comprised of:

Statement of Net Position: The District presents its statement of net position using the balance sheet format. The Statement reflects assets, liabilities, and net position (equity) of the District at year-end. The net position section of the statements is separated into three categories: net investment in capital assets; restricted net position; and unrestricted net position. The District's accumulated gains and losses in fair value from hedging activities are considered deferred inflows and deferred outflows and have been classified as such on the Statement of Net Position.

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

Statement of Cash Flows: The Statement of Cash Flows provides information about the District's cash receipts and payments for operations, as well as funds provided and used in investing and financing activities.

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

FINANCIAL ANALYSIS

The following analysis focuses on the District's Net Position and Changes in Net Assets during the year. The District's total assets and deferred outflows exceeded the liabilities and deferred inflows by \$93.8 million at the close of calendar year 2016.

Statement of Net Position	2016	2015	2015 to 2016 Change	2014
Current Assets *	\$28,066,215	\$37,616,553	-25.39%	\$54,055,246
Noncurrent Assets *	7,309,126	17,436,633	-58.08%	5,269,144
Capital Assets and Work in Progress	388,224,900	378,145,948	2.67%	361,873,184
Accumulated Depreciation	-153,953,208	-144,046,693	6.88%	-134,164,261
Deferred Outflow of Resources	8,433,872	6,208,527	35.84%	1,047,173
Total Assets and Deferred Outflows	\$278,080,905	\$295,360,968	-5.85%	\$288,080,486
Long-Term Liabilities	161,017,465	159,099,807	1.21%	137,770,230
Other Liabilities	18,819,047	18,311,354	2.77%	14,129,433
Deferred Inflows of Resources	4,433,680	6,732,041	-34.14%	3,965,283
Total Liabilities and Deferred Inflows	184,270,192	184,143,202	0.07%	155,864,946
Net Investment in Capital Assets *	103,501,393	100,889,167	2.59%	100,109,143
Restricted	7,078,535	5,714,911	23.86%	5,144,635
Unrestricted *	-16,769,215	4,613,688	-463.47%	26,961,762
Total Net Position	93,810,713	111,217,766	-15.65%	132,215,540
Total Liabilities & Net Position	\$278,080,905	\$295,360,968	-5.85%	\$288,080,486

* Certain prior year amounts have been reclassified to conform to the current year presentation.

PUBLIC UTILITY DISTRICT No. 1 of GRAYS HARBOR COUNTY
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2016

2016 saw a decrease to total assets of \$17.2 million. Current Assets accounted for \$9.5 million of the change, which was due to the following notable transactions: A \$1.5 million increase in the bond reserve fund, transferred from unrestricted cash; a \$2.2 million reduction to derivative assets based on fewer hedged transactions outstanding at the close of the year; and the current year operating loss. Noncurrent assets were reduced by \$10.1 million, primarily due to a prior period adjustment for the post-employment benefit obligation as outlined in Note 16. Deferred outflow of resources increased by \$2.3 million. This change was primarily due to a \$1.6 million increase to the GASB 68 Pension liability, and a \$.7 million increase in the fair value of hedging derivatives.

Capital Assets

2016 saw an overall increase of approximately \$11.4 million in Capital Assets and Work in Progress, which is primarily a result of the improvements to the Transmission and Distribution system as well as closing capital projects that were previously in construction in progress. The following is a summary of the major projects in 2016:

- Over 600 new poles were replaced on the Transmission and Distribution systems as a result of the District pole treatment and testing program.
- New substation transformer.
- High voltage circuit breaker replacement at the Highland Substation.
- Several other projects were completed throughout the service territory as the District strives to increase safety and reliability for its employees and customer owners.

See Note 4 for more information regarding capital asset activity for 2016.

Long-Term Liabilities

In 2016, long-term liabilities increased by \$1.9 million primarily due to increases in Pension and OPEB liabilities. Long term debt was reduced by \$.3 million over the prior year. The District refinanced the balance of the 2006 revenue bonds, with no new proceeds received. See Note 6 for more information regarding debt activity for 2016.

Changes in the District's net assets can be determined by reviewing the following condensed Statement of Revenues, Expenses, and Changes in Net Assets for the year.

Statement of Revenues, Expenses and Changes in Net Position				
	2016	2015	2015 to 2016 Change	2014
Operating Revenues:				
Retail Energy Sales	\$85,181,351	\$80,888,912	5.31%	\$81,801,022
Sales for Resale	17,568,141	20,615,742	-14.78%	22,794,813
Other*	13,680,005	13,925,977	-1.77%	13,027,958
Total Operating Revenue	\$116,429,497	\$115,430,631	0.87%	\$117,623,793
Nonoperating Revenue*	\$369,085	\$2,719,941	-86.43%	\$461,375
Total Revenues	\$116,798,582	\$118,150,572	-1.14%	\$118,085,168
Operating Expenses:				
Power Supply	\$73,770,183	\$70,563,510	4.54%	\$69,742,484
Operations and Maintenance	25,827,439	26,346,748	-1.97%	20,610,547
Conservation	1,526,558	1,520,890	0.37%	1,785,455
Taxes & Depreciation	18,327,871	18,338,251	-0.06%	19,674,767
Total Operating Expenses	\$119,452,051	\$116,769,399	2.30%	\$111,813,253
Nonoperating Expenses	\$3,284,995	\$9,327,991	-64.78%	\$8,058,127
Total Expenses	\$122,737,046	\$126,097,390	-2.66%	\$119,871,380
Change in Net Position	(\$5,938,464)	(\$7,946,818)	-25.27%	(\$1,786,212)
Beginning Net Position	\$111,217,766	\$132,215,540	-15.88%	\$134,001,752
Cumulative Effect of Restatement	0	-13,050,956	-100.00%	0
Prior Period Adjustment (Note 16)	-11,468,589	0	100.00%	250,211
Ending Net Position	\$93,810,713	\$111,217,766	-15.65%	\$132,465,751
* Certain prior year amounts have been reclassified to conform to the current year presentation.				

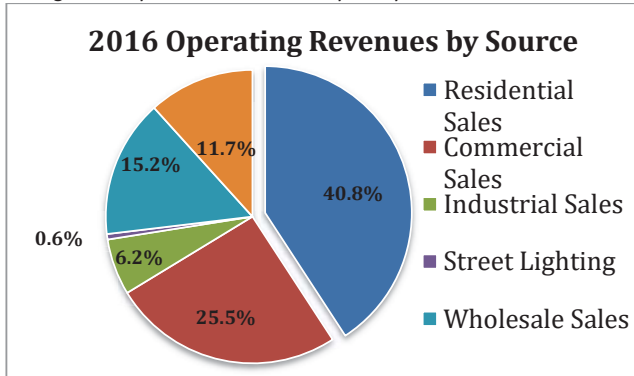
**PUBLIC UTILITY DISTRICT No. 1 of GRAYS HARBOR COUNTY
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2016**

Financial Analysis

During 2016, the District's overall financial position and results of operations decreased from the prior year. The District's net position decreased \$ 5.9 million from Operations. The following narrative is an analysis of the change in net position by major components of income, with a primary focus on changes between 2016 and 2015.

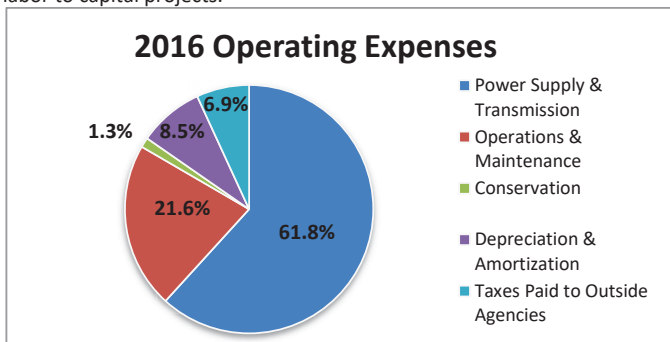
Operating Revenues

In 2016, revenues by source are shown below. Retail sales to customers (residential, commercial, industrial and street lighting) increased by \$4.3 million. This was a result of increased load due to a slightly colder winter than the prior year, and a rate increase. Revenues from Sales for Resale decreased by about \$3 million, as a result of reduced market prices and a below average water year for the Federal Hydro System.



Operating Expenses

Total Operating expenses increased approximately \$ 2.7 million in 2016. Power supply and transmission costs were up \$3.2 million, while operating & maintenance costs were down \$.5 million due to overall cost saving measures and redirection of labor to capital projects.



Non-operating Expenses

Non-operating expenses decreased by approximately \$6.0 million in 2016. This is due in part to completion of the District's clean-up efforts at the former Harbor Paper site in 2015, a reduction of \$3.2 million. Additionally, interest expense was lower in 2016 by \$2.5 million.

REQUESTS FOR INFORMATION

The basic financial statements, notes and management discussion and analysis are designed to provide a general overview of the District's finances. Questions concerning any of the information provided in this report should be directed to Grays Harbor PUD at PO Box 480, Aberdeen, WA 98520, or by calling (360) 532-4220.

Sincerely,

Kathryn Skolrood
Finance Director/CFO

PUBLIC UTILITY DISTRICT NO. 1 OF GRAYS HARBOR COUNTY
STATEMENT OF NET POSITION
DECEMBER 31, 2016

ASSETS

Current Assets:

Cash and Cash Equivalents (Note 2)	
Cash & Working Funds	\$ 7,275,052
Investments	1,689
Accounts Receivable (Net)	11,727,052
Notes and Other Receivables	1,672,439
Inventory	3,326,795
Prepayments	580,356
Derivative Asset (See Note 3)	2,629,576
Other Current Assets	853,256
Total Current Assets	<u>\$ 28,066,215</u>

Noncurrent Assets:

Restricted Bond Reserve	\$ 4,210,707
Medical Trust	2,867,828
Rural Economic Development Fund	19,111
Other Noncurrent Assets (Note 1(f))	211,480

Capital Assets:

Plant	381,390,300
Construction in Progress	6,834,600
Less Accumulated Depreciation	<u>(153,953,208)</u>
Net Capital Assets (Note 4)	<u>234,271,692</u>
Total Noncurrent Assets	<u>\$ 241,580,818</u>

Deferred Outflow Of Resources

Deferred Amount on Refunding Debt	\$ 2,550,267
Accumulated Decrease in PERS Liability from GASB 68	3,023,194
Accumulated Decrease in Fair Value of Hedging Derivatives	<u>2,860,411</u>
Total Deferred Outflow of Resources	<u>8,433,872</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 278,080,905</u>

LIABILITIES

Current Liabilities:

Accounts Payable	\$ 7,663,678
Accrued Taxes	2,406,474
Customer Deposits	1,598,224
Long-Term Debt, due within one year (Note 6)	2,637,240
Derivative Liability (See Note 3)	2,860,411
Compensated Absences-Current portion (Note 1(j))	1,609,785
Other Current, Accrued and Deferred Liabilities	43,235
Total Current Liabilities	<u>\$ 18,819,047</u>

Noncurrent Liabilities:

Compensated Absences (Note 1(j))	\$ 463,141
Accrued OPEB (See Note 8)	12,722,609
Accrued PERS Pension Liability	15,773,767
Long-Term Debt (Note 6)	131,954,508
Other Long-Term Debt (Note 6)	103,440
Total Noncurrent Liabilities	<u>161,017,465</u>
Total Liabilities	<u>\$ 179,836,512</u>

Deferred Inflow of Resources

Deferred Amount on Refunding Debt	\$ 1,455,058
Accumulated Increase in PERS Pension due to GASB 68	349,046
Accumulated Increase in Fair Value of Hedging Derivatives	<u>2,629,576</u>
Total Deferred Inflow of Resources	<u>4,433,680</u>
Total Liabilities and Deferred Inflow of Resources	<u>\$ 184,270,192</u>

NET POSITION

Net Investment in Capital Assets	\$ 103,501,393
Restricted	7,078,535
Unrestricted	<u>(16,769,215)</u>
Total Net Position	<u>\$ 93,810,713</u>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS

PUBLIC UTILITY DISTRICT NO. 1 OF GRAYS HARBOR COUNTY
STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEAR ENDED DECEMBER 31, 2016

	<u>2016</u>
OPERATING REVENUES	
Residential Sales	\$ 47,481,478
Commercial Sales	29,711,386
Industrial Sales	7,265,300
Street Lighting	723,187
Wholesale Sales	17,568,141
Other Operating Revenue	13,680,005
Total Operating Revenues	<u>\$ 116,429,497</u>
 OPERATING & MAINTENANCE EXPENSES	
Power Supply	\$ 66,530,603
Transmission	7,239,580
Operating	17,023,454
Maintenance	8,803,985
Conservation	1,526,558
Depreciation and Amortization	10,131,840
Taxes and Tax Equivalents	8,196,031
Total Operating & Maintenance Expenses	<u>\$ 119,452,051</u>
 OPERATING INCOME (LOSS)	 \$ (3,022,554)
 NONOPERATING REVENUE AND (EXPENSES)	
Interest and Dividend Income	\$ 52,096
Net Decrease in the Fair Value of Investments	(14,927)
Interest and Amortization on Long Term Debt	(3,581,683)
Capital Debt Service Subsidy from the Federal Government	296,688
Other Nonoperating Revenues	331,916
Total Nonoperating Revenue (Expenses)	<u>\$ (2,915,910)</u>
 CHANGE IN NET POSITION	 <u>\$ (5,938,464)</u>
 TOTAL NET POSITION, January 1	 \$ 111,217,766
Prior Period Adjustment (Note 16)	<u>(11,468,589)</u>
 TOTAL NET POSITION, December 31	 <u><u>\$ 93,810,713</u></u>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS

PUBLIC UTILITY DISTRICT No. 1 of GRAYS HARBOR COUNTY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2016
(Page 1 of 2)

Cash Flows from Operating Activities

Cash Received from Customers	\$ 116,429,498
Payments for Purchased Power	(66,530,603)
Payments for Operating, Maintenance and Conservation	(20,446,108)
Cash Payments to Employees	(12,912,714)
Taxes Paid	(8,196,031)
Customer Deposits Received, Net	50,022
Net Cash Provided (Used) by Operating Activities	<u>\$ 8,394,064</u>

Cash Flows from Noncapital Financing Activities

Interest paid on available line of credit	\$ (40,667)
Cash received from State Grants	329,601
Net Cash Provided (Used) by Noncapital Financing Activities	<u>\$ 288,934</u>

Cash Flows from Capital and Related Financing Activities

Repayments of Note	\$ (17,240)
Bond Principal Payments	(2,535,000)
Interest paid on Long-Term Borrowing	(3,729,924)
Capital Debt Service Subsidy from the Federal Government	296,688
Increase to Bond Reserve	(1,516,634)
Deferred Gain on 2016 Refunding	1,470,704
Acquisition and Construction of Assets	(10,899,026)
Net Cash Provided (Used) by Capital & Related Financing Activities	<u>\$ (16,930,432)</u>

Cash Flows from Investing Activities

Investments Redeemed	\$ 2,000,000
Investments Purchased	(2,341,502)
Interest Received on Investments	52,097
Net Cash Provided (Used) by Investing Activities	<u>\$ (289,405)</u>

Net (Decrease) Increase in Cash and Cash Equivalents \$ (8,536,839)

Cash and Cash Equivalents, Beginning of Year \$ 15,813,580

Cash and Cash Equivalents, End of Year \$ 7,276,741

Noncash Investing, Capital, and Financing Activities

The District had a net decrease in the fair value of investment of \$14,927 at December 31, 2016.

The deferred inflows and outflows relating to GASB 68 had no effect on cash flows for 2016. The pension deferred outflow was \$3,023,194 and the pension deferred inflow was \$349,046 as of December 31, 2016.

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2106
(Page 2 of 2)

**Reconciliation of Operating Income (Loss) to Net Cash Provided
(Used) by Operating Activities:**

Operating Income (Loss)	\$	(3,022,554)
Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:		
Depreciation and Amortization		10,131,840
Net GASB 68 Adjustments		406,753
State Dept. of Revenue tax refund for prior years tax paid		(229,827)
Changes in Operating Assets and Liabilities		
Special Funds and Other	\$	160,955
Customer Accounts Receivable		(878,667)
Other Receivables		(143,770)
Inventories		(16,251)
Prepayments		(111,986)
Warrants, Notes, A/P and Construction Payables		526,834
Customer Deposits		50,022
Accrued Taxes		154,531
Miscellaneous Deferred, Accrued and Other Liabilities		112,164
Post retirement benefit obligation	\$	1,254,020
Total Changes in Operating Assets and Liabilities	\$	1,107,852
Total Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:	\$	11,416,618
Net Cash Provided (Used) by Operating Activities	\$	8,394,064

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 1 - SUMMARY OF OPERATIONS & SIGNIFICANT ACCOUNTING POLICIES

Public Utility District No. 1 of Grays Harbor County (the District) is a municipal corporation, governed by an elected three-member board, authorized under Title 54 RCW.

As required by generally accepted accounting principles, management has considered all potential component units in defining the reporting entity and has no component units.

The accounting policies of the District conform to generally accepted accounting principles applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The District has applied all applicable GASB pronouncements including GASB 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, as well as all applicable Financial Accounting Standards Board (FASB) statements and interpretations, except for those that conflict with or contradict GASB pronouncements. The following is a summary of the more significant policies:

a) Basis of Accounting and Presentation

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

b) Cash and Cash Equivalents

For the purposes of the statement of cash flows, the District considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. Balances in the Local Government Investment Pool (LGIP) are considered cash equivalents as they can be converted into cash within one business day.

c) Accounting Estimates

The preparation of financial statements in conformity with Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. Estimates may be included in the disclosure of contingent assets and liabilities at the date of the financial statements, and in the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

d) Utility Plant and Depreciation

Utility plant is recorded at the original cost which includes both direct costs of acquisition or construction and indirect costs. The District's capitalization threshold is \$5,000. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and improvements is capitalized. Property, plant and equipment are depreciated using the straight-line method over the following estimated useful lives:

Buildings & Improvements	50 years
Generation Plant	20 years
Electric Plant – Transmission	30-40 years
Electric Plant – Distribution	28-40 years
Transportation Equipment	7-10 years
General Plant & Equipment	5-25 years
Telecommunications	20 years

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 1 - SUMMARY OF OPERATIONS & SIGNIFICANT ACCOUNTING POLICIES (cont.)

d) Utility Plant and Depreciation (cont.)

Preliminary survey and investigation costs incurred for proposed projects are deferred pending a final decision to develop the project. Costs relating to projects ultimately constructed are reclassified to utility plant. If the projects are abandoned, the costs are expensed.

e) Investments

(See Note 2)

f) Noncurrent Assets

In accordance with bond resolutions and other agreements, separate funds have been established for restricted or limited-use funds. The assets held in these funds are limited as to their use, including debt service, employee medical expenses and other reserve requirements. Noncurrent assets include the following:

Description of Asset	2016 Amount	Restricted Net Position
Bond Fund	\$ 4,210,707	\$ 4,210,707
Medical Insurance Trust	2,867,828	2,867,828
Rural Economic Development Fund (REDF)	19,111	
<u>Other Noncurrent Assets:</u>		
Premiera Advance Deposit	\$ 88,000	
Electric license	4,004	
Other Investments	120,533	
Preliminary Survey & Investigation (Note 1(d))	(1,056)	
Total Other Noncurrent Assets	<u>\$ 211,480</u>	
Total Restricted/Limited Use		<u>\$ 7,078,535</u>

The District holds in trust all employee and employer medical insurance premiums. The trust pays actual medical claims and administrative costs associated with claims management. The trust also maintains stop-loss insurance, which is administered by the District's Health and Welfare Committee. A portion of the Medical Trust is restricted to cover incurred but not reported (IBNR) claims. The plan administrator normally maintains these funds; however the District is able to hold these funds in trust. In the event the District changed plan administrators these funds would be used to close out claims during the transition.

g) Receivables and Provision for Doubtful Accounts

Electric meters read but unbilled are reflected in the utility's accounts receivable.

Bad debt expenses, and the accumulated provision for uncollectible accounts, are charged monthly for an amount that provides for estimated losses on accounts receivable that may become uncollectible. Actual losses are then charged against the provision as they are identified.

h) Inventories

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

i) Construction in Progress (CIP)

(See Note 4)

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 1 - SUMMARY OF OPERATIONS & SIGNIFICANT ACCOUNTING POLICIES (cont.)

j) Personal Leave Plan

The District provides its employees with a single leave, Personal Time Off plan (PTO), in lieu of separate programs for vacation and illness benefits. Employees accrue PTO based upon their length of service. Moreover, employees with a sick leave balance under the terms of the former plan were able to transfer the balance into a Supplemental Leave Bank (SLB). No additional hours may be posted to the SLB, though time off for illness may be charged against the SLB rather than PTO.

Employees hired subsequent to the adoption of PTO may only accrue PTO. Employees may also sell PTO to the District under certain conditions. Upon termination, or resignation with adequate notice, the employee will be paid for all unused PTO. Additionally, the District will deposit 50% of the value of any remaining SLB into a qualified MSA VEBA medical reimbursement account for the Operations VEBA group only.

PTO is charged as a component of payroll overhead as time is incurred by an employee. A corresponding liability is recognized until such time an employee uses or sells PTO to the District in accordance with the terms of the plan. Changes in compensated absences during the current fiscal period are as follows:

Outstanding personal time off (PTO) balance, December 31, 2015	\$ 1,951,222
Personal time off accrued during 2016	1,748,204
Personal time off used during 2016	(1,626,500)
Outstanding Personal time off (PTO) balance, December 31, 2016	\$ 2,072,926

The District estimates \$1,609,785 of PTO will be used in the next fiscal year. The current and noncurrent liability for PTO appears on the Statement of Net Position.

k) Debt Premiums and Discounts and Issuance Costs

Amounts stemming from original issue and reacquired bonds, including premiums and discounts are amortized over the life of the issue whether defeased or held to term. Resulting differences are amortized using the straight-line basis. Issuance costs are expensed in the year issued.

l) Debt Refundings

For current and advance refunding resulting in defeasance of debt, the difference between the reacquisition price and the net carrying amount of the old debt (gain or loss) is deferred and amortized as a component of interest expense over the remaining life of the old debt or the new debt, whichever is shorter. These amounts are reported as deferred inflows or outflows of resources on the Statement of Net Position.

m) Revenue Recognition

Revenues from retail sales of electricity include an estimate for energy delivered to customers between the last billing date and the end of the year.

n) 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.

o) Financial Statement Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 2 - DEPOSITS AND INVESTMENTS

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

Deposits and investments as of December 31, 2016 consist of the following:

By Type of Deposit	Maturities	Amount	Categorized on Financial Statements		
			Cash & Cash Equivalent	Restricted Bond Funds	Noncurrent Assets
Petty cash and change funds		\$ 8,550	\$ 8,550	\$ -	\$ -
Bank Deposits--unrestricted		7,266,502	7,266,502	-	-
Bank Deposits--restricted		2,890,943	-	-	2,890,943
Investments:					
State Treasurer's Local Government Investment Pool (LGIP)	35 days average	1,885,821	1,689	1,884,132	-
Govn't Agency --FHLM	5/24/2019	990,110	-	990,110	-
Govn't Agency --FNMA	11/25/2019	1,336,465	-	1,336,465	-
Total Cash and Investments		\$ 14,378,391	\$ 7,276,741	\$ 4,210,707	\$ 2,890,943

Investments Measured at Amortized Cost

The amount held by the District in the State Treasurer's Local Government Investment Pool (LGIP) at year end, was \$1,885,821, and had an average maturity of 35 days.

The LGIP portfolio is invested in a manner that meets the maturity, quality, diversification and liquidity requirements set forth by GASB for external investment pools that elect to measure, for financial reporting purposes, investments at amortized cost.

Investments measured at Fair Value

The District measures and reports investment at fair value using the valuation input hierarchy established by generally accepted accounting principles, as follows:

- Level 1: Quoted prices in active markets for identical assets or liabilities;
- Level 2: These are quoted market prices for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other than quoted prices that are not observable;
- Level 3: Unobservable inputs for an asset or liability.

U.S. Agency and U.S. Treasury Securities classified in Level 2 are valued using quoted prices for similar securities and interest rates. The level of fair value measurement is based on the lowest level of significant input for the security type in its entirety. There are no Level 1 or Level 3 security classifications to report.

At December 31, 2016, the District had the following investments measured at fair value:

Investments by Fair Value	12/31/2016	Fair Value Measurements Using		
		Quoted Prices in Active markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Govn't Agency --FHLM	\$ 990,110	\$ -	\$ 990,110	\$ -
Govn't Agency --FNMA	1,336,465	-	1,336,465	-
	\$ 2,326,575	\$ -	\$ 2,326,575	\$ -

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 2 - DEPOSITS AND INVESTMENTS (cont.)

Custodial Credit Risk – For deposits, this is the risk that in the event of a bank failure, the District’s deposits may not be returned. All District deposits and certificates of deposit are held by public depositories authorized by the PDPC and are not subject to custodial credit risk. State law requires public depositories to fully collateralize their uninsured public deposits with approved third-party safekeeping agents and provide for independent oversight of this program.

Interest Rate Risk – The District’s investment policy requires matching investment maturities to meet anticipated cash flow requirements. The policy limits investment maturities to not more than three years from the settlement date, unless approved by the Board of Commissioners.

Credit Risk – The District’s investment policy conforms with State law which restricts investments of public funds to debt securities and obligations of the U.S. Treasury, U.S. Government agencies and certain U.S. Government sponsored corporations, certificates of deposit and other evidences of deposit at financial institutions qualified by the Washington State Public Deposit Protection Commission (PDPC), bankers’ acceptances, investment-grade general obligation debt of state and local governments and public authorities as well as State, County, municipal or school district bonds or in warrants of taxing districts of the State and the Washington State Local Government Investment Pool (LGIP).

Concentration of Credit Risk - The investment policy requires diversification of investments by security type and institution, with the exception of U.S. Treasuries and the LGIP.

NOTE 3 – DERIVATIVE INSTRUMENTS

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

It is the District’s policy to document and apply as appropriate the normal purchase and normal sales 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 and natural gas that require the physical delivery and which are expected to be used or sold by the reporting entity in the normal course of business are generally considered “normal purchases and normal sales.” These transactions are excluded from GASB Statement No. 53 and therefore are not required to be recorded at fair value in the financial statements. Financial swaps for electricity and natural gas are considered to be derivatives under GASB Statement No. 53, but generally do not meet the “normal purchases and normal sales” criteria.

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

Fair Value at December 31, 2016				
Classification	Amount	Classification	Amount	Notional
Cash Flow Hedges				
Deferred Outflow	\$ 2,860,411	Derivative Liability	\$ 2,860,411	1,452 MWh
Deferred Inflow	\$ 2,629,576	Derivative Asset	\$ 2,629,576	1,368 MWh

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 3 – DERIVATIVE INSTRUMENTS (cont.)

The fair values of the commodity swap contracts were based on the futures price curve for the Mid-Columbia Intercontinental Exchange for electricity and the Sumas index for natural gas.

Objectives & 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 the projected load and resource balance positions. Generally, several strategies are employed to hedge the District's resource portfolio, including:

- *Combustion Turbine* – The District purchases gas for future periods to generate electricity when the Frederickson Plant (See Note 11) is economically viable on a marginal basis for that period on parameters established by the Risk Management Committee (RMC). If load projections indicate the District does not require the electricity to serve its customers; an equivalent quantity of power will concurrently be sold or otherwise hedged for the same period.
- *Surplus Purchased Power Resources* – The District hedges projected surpluses in future periods by selling power forward, at a fixed price, either physically or financially. The District will, on occasion, sell physical power forward in the next calendar month at a price based on the Mid-Columbia index to perfect financial forward sales which settle based on the same index.
- *Deficit Power Resources* – The District hedges projected power resource deficits in future periods by purchasing power at a fixed price, either physically or financially. If the Frederickson Project is economically viable for the deficit period, the District will purchase gas to operate the plant.

Authorized Derivatives under the Risk Management Policy:

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

Risks

Credit Risk – The District has developed a credit policy that establishes guidelines for setting credit limits and monitoring credit exposure on a continual basis. The policy addresses frequency of counterparty credit evaluations, credit limits per specific counterparty and counterparty credit concentration limits.

Commodity transactions, both physical and financial, are entered into only with counterparties approved by the District's Risk Management Committee for credit worthiness. The District had 44 counterparties with approved credit limits for electric power and natural gas sales and purchases as of December 31, 2016. Counterparty credit limits are based on The Energy Authority's (TEA) (see Note 11) proprietary credit rating system and other factors. Credit ratings range from not-rated to AA, with a majority of counterparties rated between BBB- and AA. Not rated counterparties either provide additional security or are assigned credit limits of \$25,000 or less.

Basis Risk – The District proactively works to eliminate or minimize basis risk on energy transactions by entering into derivative transactions the settle pursuant to an index derived from market transactions at the point physical delivery is expected to take place. There are no derivative transactions outstanding that carry basis risk as of December 31, 2016. As applicable, power related transactions are to be settled on the relevant Mid – Columbia index and all gas transactions are to be settled on the relevant Sumas/Huntingdon index. The District has ready access to electric transmission and natural gas transportation capacity at those respective trading points.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 3 – DERIVATIVE INSTRUMENTS (cont.)

Termination Risk – As of December 31, 2016, no termination events have occurred and there are no outstanding transactions with material termination risk.

There is no rollover, interest rate or market access risk for these derivative transactions as of December 31, 2016.

NOTE 4 - UTILITY PLANT AND DEPRECIATION

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

	Beginning Balance	Additions	Deletions	Ending Balance
Utility plant not being depreciated:				
Land	\$ 10,772,064	\$ 49,672	\$ -	\$ 10,821,736
Construction in Progress	7,978,459	11,383,211	(12,527,070)	6,834,600
Total utility plant not being depreciated	\$ 18,750,523	\$ 11,432,883	\$ (12,527,070)	\$ 17,656,336
Utility plant being depreciated:				
Transmission	\$ 38,601,009	\$ 1,539,669	\$ -	\$ 40,140,678
Distribution	250,255,280	9,084,430	(357,349)	258,982,362
General	52,367,228	1,397,896	(491,506)	53,273,618
Other	18,171,907	-	-	18,171,907
Total utility plant being depreciated	\$ 359,395,424	\$ 12,021,995	\$ (848,855)	\$ 370,568,564
Accumulated Depreciation	(144,046,693)	(11,999,594)	2,093,079	(153,953,208)
Total Utility Plant, Net	\$ 234,099,254	\$ 11,455,284	\$ (11,282,846)	\$ 234,271,692

The District has active construction projects as of December 31, 2016 in the amount of \$6,834,600; these are listed as Construction in Progress on the Statement of Net Position.

NOTE 5 – SHORT-TERM DEBT

The District has a \$10,000,000 Line of Credit with Bank of America. As of December 31, 2016 there were no advances on this loan. The District incurred costs of \$40,667 to maintain access to these funds.

NOTE 6 - LONG-TERM LIABILITIES

Refunded Debt

The District issued \$ 16,110,000 of general obligation refunding bonds to provide resources to purchase U.S. Government Series securities that were placed in an irrevocable trust for the purpose of generating resources for all future debt service payments on \$ 17,891,444 of refunded debt. As a result, the refunded bonds are considered to be defeased and the liability has been removed from the statement of net position. This advance refunding was undertaken to reduce total debt service payments over the next 16 years by \$2,012,789 and resulted in an economic gain at redemption of \$1,470,703.

The amount of debt defeased in substance, but still outstanding at year-end was \$17,891,444.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 6 - LONG-TERM LIABILITIES (cont.)

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

Issue	Beginning Balance 1/1/16	New Issues	Principal Payments/ Refundings/ Reductions	Ending Balance 12/31/16	Due Within One- Year
2006 Electric Revenue Bonds - Maturing 2008 – 2028, Interest Rate ranges from 3.68% to 5%, Original Par Amount \$65.080M	\$ 20,000,000	-	\$ 20,000,000	\$ -	\$ -
2010 Electric Revenue Bonds (Taxable Build America Bonds) – Maturing 2031 – 2040, Interest Rate 6.707%, Original Par \$27.090M	27,090,000	-	-	27,090,000	-
2013 Electric Revenue Bonds – Maturing July 1, 2018 – 2033; Interest Ranges from 3.75% to 5%; Original Par \$32.430M	32,430,000	-	-	32,430,000	-
2015 Electric Revenue Bonds – Maturing July 1, 2016 – January 1, 2045; Interest Ranges from 4% to 4.125%; Original Par \$51.63M	50,860,000	-	-	50,860,000	750,000
2016 Electric Revenue Bonds-Maturing January 1, 2017 to July 1, 2032; Interest Ranges from 4% to 5%; Original Par \$16.110 M	-	16,110,000	-	16,110,000	1,870,000
SUBTOTAL BONDS PAYABLE	\$ 130,380,000	\$ 16,110,000	\$ 20,000,000	\$ 126,490,000	\$ 2,620,000
Plus Unamortized Bond Premium on bonds payable, 2006, 2013, 2015 and 2016 issuances	8,278,263	2,042,517	2,236,272	8,084,508	
TOTAL BONDS PAYABLE	\$ 138,658,263	\$ 18,152,517	\$ 22,236,272	\$ 134,574,508	\$ 2,620,000
Community Economic Revitalization Board (CERB) Loan – Ten Year Term due January 1, 2023, 0% Interest	137,920	-	17,240	120,680	17,240
TOTAL DEBT PAYABLE	138,796,183	18,152,517	22,253,512	134,695,188	2,637,240
Post Employment Benefits Other Than Pension (OPEB)	11,468,589	1,254,020	-	12,722,609	-
Net Pension Liability	12,137,275	3,636,492	-	15,773,767	-
Compensated Absences	1,951,222	1,748,204	1,626,500	2,072,926	1,609,785
TOTAL LONG TERM LIABILITIES	\$ 164,353,269	\$ 24,791,233	\$ 23,880,012	\$ 165,264,490	\$ 4,247,025

There are limitations and requirements contained in the various bond indentures. The District is in compliance with all significant limitations and restrictions including compliance with federal arbitrage requirements. The District spends bond proceeds within the allowable period of time to avoid a negative arbitrage position.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 6 - LONG-TERM LIABILITIES (cont.)

Future Debt Service requirements on the revenue bonds and loan are as follows:				
<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>	
2017	\$ 2,637,240	\$ 6,327,912	\$ 8,965,152	
2018	3,712,240	6,454,576	10,166,816	
2019	3,607,240	6,278,701	9,885,941	
2020	3,792,240	6,101,226	9,893,466	
2021	3,982,240	5,910,976	9,893,216	
2022-2026	21,184,480	26,443,093	47,627,573	
2027-2031	31,530,000	20,333,068	51,863,068	
2032-2036	29,865,000	11,431,643	41,296,643	
2037-2041	20,690,000	4,476,723	25,166,723	
thereafter	5,610,000	454,928	6,064,928	
Total	\$ 126,610,680	\$ 94,212,846	\$ 220,823,526	

NOTE 7 - PENSION PLAN

The following table represents the aggregate pension amounts for all plans subject to the requirements of the GASB Statement 68, *Accounting and Financial Reporting for Pensions* for the year 2016:

Aggregate Pension Amounts – All Plans	
Pension liabilities	\$(15,773,767)
Pension assets	\$ 0
Deferred outflows of resources	\$ 3,023,194
Deferred inflows of resources	\$(349,046)
Pension expense/expenditures	\$2,196,595

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 Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 7 - PENSION PLAN (cont.)

Public Employees' Retirement System (PERS)

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

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

Contributions

The **PERS Plan 1** member contribution rate is established by State statute at 6 percent. The employer contribution rate is developed by the Office of the State Actuary and includes an administrative expense component that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates. The PERS Plan 1 required contribution rates (expressed as a percentage of covered payroll) for 2016 were as follows:

PERS Plan 1		
Actual Contribution Rates:	Employer	Employee*
PERS Plan 1	6.23%	6.00%
PERS Plan 1 UAAL	4.77%	6.00%
Administrative Fee	0.18%	
Total	11.18%	6.00%

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

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.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 7 - PENSION PLAN (cont.)

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

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

Contributions

The **PERS Plan 2/3** employer and employee contribution rates are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. The Plan 2/3 employer rates include a component to address the PERS Plan 1 UAAL and an administrative expense that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and Plan 3 contribution rates. The PERS Plan 2/3 required contribution rates (expressed as a percentage of covered payroll) for 2016 were as follows:

PERS Plan 2/3		
Actual Contribution Rates:	Employer 2/3	Employee 2*
PERS Plan 2/3	6.23%	6.12%
PERS Plan 1 UAAL	4.77%	
Administrative Fee	0.18%	
Employee PERS Plan 3		varies

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

Both district and the employees made the required contributions.

The District's actual PERS plan contributions were \$788,915 to PERS Plan 1 and \$1,000,927 for PERS Plan 2/3 for the year ended December 31, 2016.

Actuarial Assumptions

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2016 with a valuation date of June 30, 2015. The actuarial assumptions used in the valuation were based on the results of the Office of the State Actuary's (OSA) 2007-2012 Experience Study.

Additional assumptions for subsequent events and law changes are current as of the 2015 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2016. Plan liabilities were rolled forward from June 30, 2015, to June 30, 2016, reflecting each plan's normal cost (using the entry-age cost method), assumed interest and actual benefit payments.

- Inflation: 3.0% total economic inflation; 3.75% salary inflation

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 7 - PENSION PLAN (cont.)

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

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

- For all systems, except LEOFF Plan 2, the assumed valuation interest rate was lowered from 7.8% to 7.7%. Assumed administrative factors were updated.
- Valuation software was corrected on how the nonduty disability benefits for LEOFF Plan 2 active members is calculated.
- New LEOFF Plan 2 benefit definitions were added within the OSA valuation software to model legislation signed into law during the 2015 legislative session.

Discount Rate

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

Long-Term Expected Rate of Return

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

Estimated Rates of Return by Asset Class

Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2016, are summarized in the table below. The inflation component used to create the table is 2.2 percent and represents the WSIB's most recent long-term estimate of broad economic inflation.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 7 - PENSION PLAN (cont.)

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

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	\$8,768,451	\$7,271,296	\$5,982,901
PERS 2/3	\$15,654,578	\$8,502,471	\$(4,426,027)

Pension Plan Fiduciary Net Position

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

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

At June 30, 2016, the District reported a total pension liability of \$15,773,767 for its proportionate share of the net pension liabilities as follows:

	Liability (or Asset)
PERS 1	\$ 7,271,296
PERS 2/3	8,502,471
TOTAL	\$15,773,767

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

	Proportionate Share 6/30/15	Proportionate Share 6/30/16	Change in Proportion
PERS 1	0.126008%	0.135394%	0.009386%
PERS 2/3	0.155214%	0.168870%	0.013656%

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 7 - PENSION PLAN (cont.)

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 Non-employer Allocations* for all plans except LEOFF 1.

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

Pension Expense

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

	Pension Expense
PERS 1	\$ 905,297
PERS 2/3	\$ 1,291,298
TOTAL	\$ 2,196,595

Deferred Outflows of Resources and Deferred Inflows of Resources

At December 31, 2016, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

PERS 1	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 0	\$ 0
Net difference between projected and actual investment earnings on pension plan investments	183,080	0
Changes of assumptions	0	0
Changes in proportion and differences between contributions and proportionate share of contributions	0	0
Contributions subsequent to the measurement date	362,924	0
TOTAL	\$ 546,004	\$ 0

PERS 2/3	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 452,751	\$ (280,681)
Net difference between projected and actual investment earnings on pension plan investments	1,040,457	0
Changes of assumptions	87,880	0
Changes in proportion and differences between contributions and proportionate share of contributions	430,887	(68,365)
Contributions subsequent to the measurement date	465,215	0
TOTAL	\$ 2,477,189	\$ (349,046)

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 7 - PENSION PLAN (cont.)

Combined PERS Plan 1,2 & 3	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 452,751	\$ (280,681)
Net difference between projected and actual investment earnings on pension plan investments	1,223,537	0
Changes of assumptions	87,880	0
Changes in proportion and differences between contributions and proportionate share of contributions	430,887	(68,365)
Contributions subsequent to the measurement date	828,139	0
TOTAL	\$ 3,023,193	\$ (349,046)

Deferred outflows of resources related to pensions resulting from the District's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2017. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31	PERS 1
2017	\$ (45,078)
2018	\$ (45,078)
2019	\$ 168,139
2020	\$ 105,097
2021	
Thereafter	
TOTAL	\$ 183,080

Year ended December 31:	PERS 2/3
2017	\$ 112,039
2018	\$ 112,039
2019	\$ 918,806
2020	\$ 520,044
2021	\$ 0
Thereafter	\$ 0
Total	\$1,662,929

NOTE 8 - POST EMPLOYMENT BENEFITS OTHER THAN PENSIONS (OPEBs)

Plan Description: In accordance with collective bargaining agreements and compensation policies, the District provides 90% employer paid post-retirement medical, visions and prescription benefits for qualified retired employees and their eligible dependents until age 65. The plan is a single employer defined benefit plan; the District is not in a Risk Pool for Medical coverage.

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

Annual OPEB Cost: The District's annual OPEB cost is calculated based on the annual required contribution (ARC) of the employer. 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 on-going basis, is projected to cover normal costs each year and amortize any unfunded actuarial accrued liabilities over a period not to exceed 30 years. The District implemented GASB 45 prospectively in 2008. The District's annual required OPEB expense is \$2,420,466 and is equal to the Annual Required Contribution including interest.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 8 - POST EMPLOYMENT BENEFITS OTHER THAN PENSIONS (OPEBs)

Funding Status and funding progress: In 2016, the payment of employment health care benefits for retirees and qualified dependents totaled \$1,166,445. The current year funding resulted in an addition to the accrued OPEB Liability of \$ 1,254,020. The District's total accrued OPEB Liability for the years ended December 31, 2016, 2015, and 2014 was \$12,722,609, \$11,468,589, and \$10,613,690, respectively.

Actuarial Assumptions: The actuarial valuation includes estimates of the value reported and assumptions about the probability of the events in the future. The actuarial assumptions included in the valuation included a rate of return on investments of 4% and an annual increase of between 6% and 12% of health care costs. Other actuarial assumptions included estimates of future employment levels, retirement ages of active employees and morbidity/termination rates. The assumptions will be reviewed and updated in 2017. As these assumptions are reviewed in future periods, new estimates of OPEB costs and liabilities may result.

Determination of Annual Required Contribution	December 31, 2016	December 31, 2015	December 31, 2014	December 31, 2013
Normal Cost at Year End	\$812,438	\$812,438	\$812,438	\$812,438
Amortization of UAAL	\$1,608,028	\$1,608,028	\$1,608,028	\$1,608,028
Annual Required Contribution (ARC)	\$2,420,466	\$2,420,466	\$2,420,466	\$2,420,466
Determination of Net OPEB Obligation				
Annual Required Contribution	\$2,420,466	\$2,420,466	\$2,420,466	\$2,420,466
Contributions Made	\$1,166,446	\$1,565,567	\$1,216,804	\$1,069,035
Increase in Net OPEB Obligation	\$1,254,020	\$854,899	\$1,203,662	\$1,351,431
Net OPEB Obligation beginning of year	\$11,468,589	\$10,613,690	\$9,410,028	\$8,058,597
Net OPEB Obligation end of year	\$12,722,609	\$11,468,589	\$10,613,690	\$9,410,028

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

Fiscal Year Ended	Annual OPEB Cost	Percentage of OPEB Cost Contributed	Net OPEB Obligation at year end
12/31/13	\$2,420,466	44.17%	\$ 9,410,028
12/31/14	\$2,420,466	50.27%	\$10,613,690
12/31/15	\$2,420,466	64.68%	\$11,468,589
12/31/16	\$2,420,466	48.19%	\$12,722,609

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 9 - DEFERRED COMPENSATION PLANS

The District offers its employees deferred compensation programs created in accordance with Internal Revenue Code Sections 401 and 457. The plans, available to all District employees, permit them to defer a portion of their current salary, up to defined limits, until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency as defined in IRS Code.

In accordance with IRS Code, all plan assets are held in trust for the exclusive benefit of participants and their beneficiaries, and as such are not included in the District's financial statements.

The Grays Harbor County PUD No. 1 401(k) Savings Plan (the Plan) provides that participants may make voluntary payroll deferral contributions, on a pre-tax basis, up to the amount established annually by the Internal Revenue Service as the deferral ceiling.

The District has no liability for losses under the plans but does have the duty of due care that would be required of an ordinary prudent fiduciary. Empower Retirement, the Trustee of the plan, administers both plans.

NOTE 10 – RISK MANAGEMENT

Liability Insurance

The District is a member of the Public Utility Risk Management Services Self-Insurance fund (PURMS). RCW Chapter 48.62 authorizes the governing body of any one or more governmental entities to form together into or join a pool or organization for the joint purchasing of insurance, and/or joint self-insuring, and/or joint hiring or contracting for risk management services to the same extent that they may individually purchase insurance, self insure, or hire or contract for risk management services. An agreement to form a pooling arrangement was made pursuant to the provisions of RCW Chapter 54.16. The liability pool was formed on December 31, 1976 when certain PUDs in the State of Washington joined together by signing an Agreement to pool their self-insured losses and jointly purchase insurance and administrative services. Nineteen members currently belong to PURMS.

Additional pools for property and health and welfare coverage were added in March 1997 and April 2000, respectively, under the same agreements and with the same membership. All members do not participate in all pools. The District does not participate in the PURMS health and welfare pool.

The liability pool has a \$1 million self-insured retention with \$3 million in dedicated reserves. The Plan is in the process of raising the dedicated reserve balance to \$3.25 million. In addition, the fund purchases \$60 million of excess general liability insurance. The fund also purchases \$35 million in directors' and officers' liability coverage with retention of \$500,000, which includes an additional retention of \$250,000 for employment practices. In 2016, the Fund added Cyber-security coverage of \$10 million with a \$500,000 retention. The deductible is \$250.

The majority of the property in the property pool has a \$250,000 self-insured retention. Certain classes of property have higher retention requirements up to \$750,000. In addition, the fund purchases \$200 million of excess insurance over the \$250,000 (or higher) retention level. The deductible varies, but for most classes or property is \$250.

Members of each pool are assessed to maintain the designated self-insured retention.

After termination, a member is still responsible for their share of contributions to the pools for any unresolved, unreported, and in-process claims for the period they were a signatory to the agreement.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 10 – RISK MANAGEMENT (cont.)

The pools are fully funded by its current and former members. Claims are filed by members with the Administrator, Pacific Underwriters, Seattle, WA, which has been contracted to perform claims adjustment and loss prevention services. The District's share of unfunded claims liability as of December 31, 2016, was \$462,045.

The pools are governed by a Board of Directors, which is comprised of one designated representative from each participating member. The Administrator and an elected Administrative Committee are responsible for conducting the business affairs of the pool.

The following table illustrates payments to the insurance pools with PURMS:

Year Ended	Liability Pool	Property Pool
December 31, 2016	\$ 504,878	\$191,968
December 31, 2015	\$ 334,544	\$ 173,889
December 31, 2014	\$ 371,178	\$ 232,882

The District had no settlements that exceeded insurance coverage in each of the past three years.

Self-Funded Employee Dental, Medical and Vision Coverage

The District provides its employees and retirees with a self-funded dental program, administered for a fee by the Washington Dental Service. The District, through a collective bargaining agreement, is responsible for 90% of the cost of the dental program. The program is reviewed and monitored by the District's Health & Welfare Committee, which recommends funding levels to ensure program solvency. The reserves for the dental program are maintained in the Employee Benefits Trust.

The District and its employees both participate in the cost of monthly medical premiums. Premiums are held in the Medical/Dental Claims Trust Funding Account (Trust). The District uses a Minimum Premium Funding arrangement. Its service provider, Premiera Blue Cross, determines premium levels, and is paid an administrative fee for their services.

The District purchases individual Stop Loss insurance in the amount of \$90,000, and maintains a Rate Stabilization Reserve for claims funding.

Self-Funded Employee Dental, Medical and Vision Claims Activity	
	2016
Claims Liability, beginning of year	\$ -0-
Claims Incurred	\$4,485,585
Payments on Claims	\$4,485,585
Claims Liability, end of year	\$ -0-

Total contributions to the Trust by the District and employees during 2016 for medical and dental coverage were \$4,676,065.

NOTE 11 - CONSERVATION PROGRAMS

The District is required by the state of Washington's Energy Independence Act to "identify and achieve all cost-effective conservation" in the District's service territory. For the 2016-17 biennium, the District's Commission adopted a target of .73 average megawatts of conservation.

For residential customers, the District provides rebates on home weatherization, electric heating system upgrades (including duct-testing and sealing), solar water heating systems, energy efficient lighting, and some appliances.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 11 - CONSERVATION PROGRAMS (cont.)

Non-residential customers can take advantage of a flexible offering of conservation incentives. The majority of projects implemented involve heating and cooling system upgrades, energy efficient lighting, and motor and compressor upgrades for industrial customers.

The District participates in the Bonneville Power Administration's conservation incentive programs to help fund its conservation programs. Bonneville provides conservation funding to the District through the Energy Efficiency Incentive (EEI) program. Under the EEI program, the District invoices BPA after conservation projects are completed and receives incentives based upon the type and number of measures implemented. In 2015, the District received approximately \$1.141M through the EEI program, a little over 80% of total District spending on conservation.

NOTE 12 - POWER SUPPLY

BPA Power Contract

In October 2011 the District entered a new seventeen-year Block and Slice Power Sales Agreement with BPA commencing October 1, 2011, replacing the previous long-term agreement. These agreements incorporate provisions of the Pacific Northwest Electric Power Planning and Conservation Act of 1980 (Public Law 96-501) and the Bonneville Project Act of 1937 such as preference and priority in the distribution and marketing of BPA's federal power to publicly owned preference customers, such as the District. The contract provides federal power in amounts based on the District's annual Net Requirements in the form of two products: Block and Slice. This load base allocation is expressed as a percentage of the entire Bonneville Power generation portfolio, of which the District's contract share is 1.852%. This means that, on an annual basis, the District will receive energy equal to its Annual Net Requirements under BPA defined critical hydrological conditions. This allocation is apportioned approximately evenly between the Slice and Block.

The Block product provides power in pre-agreed upon monthly amounts, ranging 52MW to 81MW. The base rate for Block power is \$1,961,053 per 1% of the system allocated to Block. This allocation percentage changes very slightly annually based on projected system capabilities and is currently .88173%. The Block component has two additional monthly charge components, the "Non-Slice" credit and the Load Shaping charge. The Non Slice credit reimburses the District for its proportional share of Federal off-system sales and the Load Shaping charge materializes as either a credit or a cost depending on the District's monthly load profile. All of these charges are predetermined prior to the onset of the October-September fiscal year, the sum of the 3 ranges between \$1,106,989 and \$1,797,649 for BPA's 2016 fiscal year.

The Slice product, on the other hand, provides the District with access to a more variable product: .96996% of the Federal System Output (the District's Slice), which is based on the output of the federal system each hour. The output consists of federal hydroelectric projects and some non-federal projects, including thermal projects such as the Columbia Generating Station, all adjusted for storage and return obligations. The FY 2016 applicable base-rate for Slice purchases is also \$1,961,053 per month for each percent of Slice plus the Load Based Cost Recovery Adjustment Charge (LBCRAC), currently 0%, with the adjusted base rate subject to an annual true up by BPA based upon updated actual costs allocated to the Slice System. Technical Operating Procedures have been established to provide Slice purchasers with the ability to calculate, schedule, and account for their share of Slice Output on an hourly basis. This product does not include transmission services. Moreover, by its nature, there is a greater degree of potential for exposure – and benefit – depending upon snow-pack amount and timing of runoff and other conditions that affect water, and therefore hydroelectric system output.

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 12 - POWER SUPPLY (cont.)

BPA Transmission Services

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

In order to obtain necessary transmission services, the District entered into a long-term service agreement with BPA for Point-To-Point transmission services commencing April 30, 1997, terminating July 1, 2023.

Frederickson CT

The District has entered into a 20-year purchase commitment for purchase of 45 MW of capacity with displacement and sales rights from the Frederickson Project, a natural gas-fired combined-cycle combustion turbine. The Frederickson Project is located near Tacoma, Washington.

Nine Canyon Wind Project

In 2002 the District entered into a 20-year purchase agreement with Energy Northwest for 12.5% of the output, or an estimated 8MW of capacity from the Nine Canyon Wind Project, phases I and II, located near Kennewick, Washington. The District is also participating in Phase III of the Nine Canyons Wind Project, which provides an additional 12MW of nameplate capacity, for a total of 20MW or 20.5% of the 96MW project. Power costs for 2016 were \$ 79 /MWh based on production of 51,516 MWhs.

Coastal Energy Project

The Coastal Energy Project is a 6MW capacity wind farm located outside Grayland, WA and operated by Coastal Community Action Program (CCAP). The District entered into a 20-year power purchase contract with CCAP to purchase the output from the project.

Pasco CT

The District partnered with Franklin County PUD during 2001-2002 to jointly build and operate the Franklin/Grays Harbor PUDs Peak Generating Station, a 44MW-generating project consisting of four natural gas fueled simple-cycle combustion turbines. The Franklin Project provides the District with both backup and peaking generation capacity. The District's ownership share is one-half of the output of the project, or 22MW. The District's two 11MW units connect to Franklin County PUD's system, where costs incurred are shared equally by both utilities. During 2010, the District's Pasco CT plant became temporarily inoperable. In 2013, certain repairs were conducted to make the plant operable and available for sale. In 2015, District management determined the fair market value of the plant is approximately \$5.4 million based on sales of similar assets, this resulted in a reduction in carrying value of the asset by \$979,802.

Sierra Pacific Industries

The Sierra Pacific Industries operates a biomass generation facility and the District has contracted to purchase 6aMW from the plant. The District had the option to purchase additional output from the facility beginning in 2014 and subsequently exercised this option and is currently purchasing 11 aMW.

The Energy Authority

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

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 12 - POWER SUPPLY (cont.)

Market Purchases and Sales

Through its membership in the Western Systems Power Pool (WSPP), the District has the ability to buy and sell power for terms of one year or less with nearly all utilities in the Western United States and Canada, as well as many power marketers. The District has also entered into NAESB and ISDA agreements with several counterparties for the purpose of making financial and gas hedging transactions when market conditions and resource availability warrant.

Power Market Risk Management Policies and Procedures

The District's Risk Management Committee, with oversight and review by the Board of Commissioners, actively manages financial risk. The District periodically updates the risk management policy to incorporate improved procedures and practices.

NOTE 13 - TELECOMMUNICATIONS

The District has constructed a fiber optic network that encompasses approximately 200 miles of cable. The District presently operates a digital microwave system that provides communications throughout Grays Harbor County. These systems significantly improve the safety and reliability of the District's operations and, as an additional benefit, provides state-of-the-art communications to the residents of Grays Harbor County.

The District intends to continue to expand its fiber optic network to critical points in its substations, transmission and distribution systems, as well as to other key areas within Grays Harbor County. Under the "Excess Capacity" model, the District allows retail providers to lease wholesale services. These services include fiber optic connectivity, WDM Circuits, space on District microwave towers, and co-location facilities. The District sells services to retail providers on a wholesale basis only. The District currently operates seven co-location facilities within Grays Harbor County. Revenue from Telecom activity is included in Other Non-operating Revenue on the Comparative Statement of Revenue, Expenses and Changes in Net Position.

The following table details the telecommunications activity:

	2016
Operating Revenue	
Telecom Revenue	\$410,896
Total Operating Revenue	\$410,896
Operating Expenses	
Payroll & Fleet maintenance	82,940
Materials & Parts	18,180
Total Operating Expenses	101,120

Public Utility District No. 1 of Grays Harbor County
Notes to Financial Statements
For the Year Ended December 31, 2016

NOTE 14 - LITIGATION

Miscellaneous Claims

The District is occasionally the defendant in claims charging negligence in the location of power poles struck by motor vehicles and other miscellaneous issues involving the siting of power poles. District employees may also be involved in collisions involving motor vehicles where claims for damages and/or injuries result.

The District is insured against liability over such matters and vigorously defends actions it deems defensible. Because of the District's insurance and defense policy it is believed that none of the claims made or incurred, whether filed or not, is expected to have any material consequence to the District.

NOTE 15 – ACCOUNTING AND REPORTING CHANGES

The District implemented GASB Statements No. 72, "Fair Value Measurement and Application" and No. 79, "Certain External Investment Pools and Pool Participants" in 2016.

NOTE 16 – PRIOR PERIOD ADJUSTMENT

The District identified an error in the application of accounting principles, specifically GASB Statement No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions". The error resulted in a reduction of Unrestricted Net Assets of \$11,468,589.

PUBLIC UTILITY DISTRICT No.1 of GRAYS HARBOR COUNTY
 Required Supplementary Information
 Schedule of Proportionate Share of the Net Pension Liability--PERS Plan 1
 As of June 30, 2016
 Last 10 Fiscal Years

	2015	2016
	PERS I	PERS I
Employer's Proportion of the Net Pension Liability	0.12600800%	0.13539400%
Employer's Proportionate share of the Net Pension Liability	\$ 6,591,390	\$ 7,271,296
Employer's Covered Payroll- July to June	\$ 14,070,199	\$ 15,969,769
Employer's Proportionate share of the Net Pension Liability as a percent of covered payroll	46.85%	45.53%
Plan fiduciary Net Position as a percent of the Total Pension Liability	59.10%	57.03%

Notes to the Schedule of Proportionate Share of the Net Pension Liability

Note 1

There are no factors at year end that significantly affect trends in the amounts reported above.
 The district is responsible for its proportionate share of the PERS Plan I unfunded actuarial accrued liability (UAAL).
 The Washington State Department of Retirement Systems assesses a fee based on all covered payroll for PERS Plan 2/3 to assist in funding the UAAL.

Note 2

GASB 68 was implemented by the District in 2015. As such, only information from 2015 onwards is available for this schedule.

PUBLIC UTILITY DISTRICT No.1 of GRAYS HARBOR COUNTY
 Required Supplementary Information
 Schedule of Proportionate Share of the Net Pension Liability--PERS Plan 2/3
 As of June 30, 2016
 Last 10 Fiscal Years

	2015	2016
	PERS 2 & 3	PERS 2 & 3
Employer's Proportion of the Net Pension Liability	0.15521400%	0.16887000%
Employer's Proportionate share of the Net Pension Liability	\$ 5,545,885	\$ 8,502,471
Employer's Covered Payroll- July to June	\$ 13,773,011	\$ 15,706,030
Employer's Proportionate share of the Net Pension Liability as a percent of covered payroll	40.27%	54.14%
Plan fiduciary net position as a percent of the Total Pension Liability	89.20%	85.82%

Notes to the Schedule of Proportionate Share of the Net Pension Liability

Note 1

There are no factors at year end that significantly affect trends in the amounts reported above.

Note 2

GASB 68 was implemented by the District in 2015. As such, only information from 2015 onwards is available for this schedule.

PUBLIC UTILITY DISTRICT No.1 of GRAYS HARBOR COUNTY
 Required Supplementary Information
 Schedule of Employer Contributions--PERS I
 As of December 31, 2016
 Last 10 Fiscal Years

	2015	2016
Statutorily or contractually required contributions	\$ 604,975	\$ 788,915
Contributions in relation to the statutorily or contractually required contributions	\$ (604,975)	\$ (788,915)
Contribution deficiency (excess)	\$ -	\$ -
Employer's covered employee payroll	\$ 13,534,925	\$ 16,377,386
Contributions as a percentage of covered employee payroll	4.47%	4.82%

Notes to Schedule of Employer Contributions:**Note 1:**

There are no factors at year end that significantly affect trends in the amounts reported above.

Note 2

GASB 68 was implemented by the District in 2015. As such, only information from 2015 onwards is available for this schedule.

PUBLIC UTILITY DISTRICT No.1 of GRAYS HARBOR COUNTY
 Required Supplementary Information
 Schedule of Employer Contributions--PERS 2/3
 As of December 31, 2016
 Last 10 Fiscal Years

	2015	2016
Statutorily or contractually required contributions	\$ 755,193	\$ 1,000,927
Contributions in relation to the statutorily or contractually required contributions	\$ (755,193)	\$ (1,000,927)
Contribution deficiency (excess)	\$ -	\$ -
Employer's covered employee payroll	\$ 13,277,696	\$ 16,178,628
Contributions as a percentage of covered employee payroll	5.69%	6.19%

Notes to Schedule of Employer Contributions:**Note 1:**

There are no factors at year end that significantly affect trends in the amounts reported above.

Note 2

GASB 68 was implemented by the District in 2015. As such, only information from 2015 onwards is available for this schedule.

PUBLIC UTILITY DISTRICT No.1 of GRAYS HARBOR COUNTY
 Required Supplementary Information
 Schedule of Other Post Employment Benefits
 For the Year Ended December 31, 2016

Other Post Employment Benefits For the Year Ended December 31, 2016						
Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (AAL)* (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/2006	0	\$27,806,000	\$27,806,000	0%	N/A	N/A

ABOUT THE STATE AUDITOR'S OFFICE

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

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

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

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

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

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

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

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