Office of the Washington State Auditor
Pat McCarthy

November 9, 2023

Board of Commissioners
Public Utility District No. 1 of Snohomish County
Everett, Washington

Contracted CPA Firm's Audit Report on Financial Statements and Federal Single Audit

We have reviewed the audit report issued by a certified public accounting (CPA) firm on the financial statements and compliance with federal grant requirements of Public Utility District No. 1 of Snohomish County for the fiscal year ended December 31, 2022. The District contracted with the CPA firm for this audit and requested that we accept it in lieu of performing our own audit.

Based on this review, we have accepted this report in lieu of the audit required by RCW 43.09.260. The Office of the Washington State Auditor did not audit the accompanying financial statements or Public Utility District No.1 of Snohomish County's compliance with federal grant agreements and, accordingly, we do not express an opinion on those financial statements or on compliance.

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

Sincerely,

Pat McCarthy

Pat McCarthy, State Auditor

Olympia, WA

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Report of Independent Auditors

The Board of Commissioners
Public Utility District No. 1 of Snohomish County
Everett, Washington

Report on the Audit of the Financial Statements

Opinions

We have audited the financial statements of Public Utility District No. 1 of Snohomish County, Washington (the District), which comprise the District's combined and individual statements of net position, and the related combined and individual statements of revenues, expenses and changes in net position and cash flows of the Electric, Generation, and Water Systems, as of and for the year ended December 31, 2022, and the District's combined statements as of and for the year ended December 31, 2021, and the related notes to the financial statements.

In our opinion, the accompanying financial statements referred to above present fairly, in all material respects, the combined financial position of the District as of December 31, 2022 and 2021, and the individual financial positions of the Electric, Generation, and Water Systems as of December 31, 2022, and the respective changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinions

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards (Government Auditing Standards)*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the District and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Emphasis of Matter

As discussed in Note 4 to the financial statements, the District adopted the provisions of Government Accounting Standards Board Statement No. 87, *Leases*, effective January 1, 2021. The combined financial statements for the year ended December 31, 2021, have been retroactively restated in accordance with the requirements of the new accounting standard. Our opinion is not modified with respect to this matter.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the District's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinions. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the District's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control–related matters that we identified during the audits.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis, schedule of proportionate share of the net pension liability – PERS, schedule of employer contributions – PERS, and schedule of changes in total other post-employment benefits (OPEB) liability and related ratios, be presented to supplement the basic financial statements. Such information is the responsibility of management and, 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 audits 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.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The accompanying schedules of Electric System – statements of revenues, expenses, and debt service coverage, Electric System – revenue and statistical data, and Water System – statements of revenues, expenses, debt service coverage, and statistical data are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the combined financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 4, 2023, 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 solely 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 the effectiveness of the District's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Moss Adams LLP

Everett, Washington
April 4, 2023

Combined Statements of Net Position

December 31, 2022 and 2021

(In thousands)

	2022				As restated 2021
Assets	Electric System	Generation System	Water System	Combined	Combined
Current Assets:					
Cash and temporary investments:					
Cash and cash equivalents	$ 31,667	$ 4,723	$ 2,926	$ 39,316	$ 49,294
Temporary investments	78,635	3,199	3,423	85,256	78,939
Total Cash and Temporary Investments	**110,302**	**7,922**	**6,349**	**124,572**	**128,233**
Accounts and other receivables, net	117,845	268	2,668	120,782	110,597
Intersystem loans receivable	3,338	–	–	–	–
Materials and supplies	46,993	–	1,636	48,629	33,487
Prepayments and other	6,974	296	161	7,431	6,870
Total Current Assets	**285,452**	**8,486**	**10,814**	**301,414**	**279,187**
Long-Term Investments & Special Funds:					
Long-term investments	119,685	3,903	728	124,316	97,509
Special funds - bond funds and other	306,278	13,073	19,172	338,523	300,480
Total Long-Term Investments & Special Funds	**425,963**	**16,976**	**19,900**	**462,839**	**397,989**
Utility Plant:					
Plant in service	2,153,992	354,851	181,325	2,690,168	2,590,107
Construction work in progress	155,155	6,230	3,731	165,116	134,289
Total utility plant	2,309,147	361,081	185,056	2,855,284	2,724,396
Accumulated depreciation	(889,383)	(162,063)	(47,562)	(1,099,008)	(1,035,934)
Net Utility Plant	**1,419,764**	**199,018**	**137,494**	**1,756,276**	**1,688,462**
Other Assets:					
Conservation loans and other receivables, net	3,183	–	281	3,464	9,109
Lease receivable	22,268	–	805	23,073	25,817
Intersystem loans and receivables	27,538	–	–	–	–
FERC licenses	–	13,969	–	13,969	14,511
Net pension assets	42,009	844	1,259	44,112	116,646
Other assets	–	170	–	170	139
Total Other Assets	**94,998**	**14,983**	**2,345**	**84,788**	**166,222**
Total Assets	**2,226,177**	**239,463**	**170,553**	**2,605,317**	**2,531,860**
Deferred Outflows of Resources					
Unamortized loss on refunding debt	851	1,877	–	2,728	4,086
Net pension and OPEB deferrals	46,213	1,341	1,207	48,761	20,914
Total Deferred Outflows of Resources	**47,064**	**3,218**	**1,207**	**51,489**	**25,000**
Total Assets and Deferred Outflows	**$2,273,241**	**$ 242,681**	**$ 171,760**	**$2,656,806**	**$2,556,860**

The accompanying notes are an integral part of these combined financial statements.

Combined Statements of Net Position

December 31, 2022 and 2021

(In thousands)

	2022				As restated 2021
Liabilities	Electric System	Generation System	Water System	Combined	Combined
Current Liabilities:					
Accounts payable	$ 80,301	$ 1,011	$ 1,850	$ 83,162	$ 56,445
Accrued taxes	18,760	93	100	18,953	17,791
Accrued interest	1,673	267	35	1,975	1,790
Other accrued liabilities	31,683	1	5	31,689	29,893
Customer deposits	3,191	–	9	3,200	3,360
Current maturities of long-term debt	11,985	5,355	893	18,233	18,436
Intersystem loans payable	–	3,338	–	–	–
Total Current Liabilities	**147,593**	**10,065**	**2,892**	**157,212**	**127,715**
Long-Term Debt:					
Revenue bonds	453,398	61,267	5,628	520,293	478,346
Other notes payable	–	–	4,919	4,919	6,127
Total Long-Term Debt	**453,398**	**61,267**	**10,547**	**525,212**	**484,473**
Other Liabilities:					
Intersystem loans and payables	–	27,538	–	–	–
FERC license obligations	–	13,969	–	13,969	14,511
Net pension liability	24,368	665	638	25,671	11,285
Lease liability	4,251	152	–	4,403	1,827
Other liabilities	65,237	1,161	1,217	67,616	68,425
Total Other Liabilities	**93,856**	**43,485**	**1,855**	**111,659**	**96,048**
Total Liabilities	**694,847**	**114,817**	**15,294**	**794,083**	**708,236**
Deferred Inflows of Resources					
Unearned FERC license contributions	–	4,000	–	4,000	4,500
Net pension deferrals	43,907	835	1,287	46,028	121,811
Other deferred inflows	29,707	2,769	1,042	33,518	36,837
Total Deferred Inflows of Resources	**73,614**	**7,604**	**2,329**	**83,546**	**163,148**
Net Position					
Net investment in capital assets	1,099,776	134,273	126,858	1,360,907	1,299,188
Restricted:					
Reserve funds	745	6,378	854	7,977	8,172
Rate stabilization	111,550	–	1,456	113,007	117,896
Net pension assets (liabilities)	(49,160)	(1,563)	(1,254)	(51,977)	20,556
Debt service and other	31,730	6,428	16,817	54,975	52,112
Unrestricted	310,139	(25,256)	9,406	294,288	187,552
Total Net Position	**1,504,780**	**120,260**	**154,137**	**1,779,177**	**1,685,476**
Total Liabilities, Deferred Inflows and Net Position	**$2,273,241**	**$ 242,681**	**$ 171,760**	**$2,656,806**	**$ 2,556,860**

The accompanying notes are an integral part of these combined financial statements.

Combined Statements of Revenues, Expenses, and Changes in Net Position

Years ended December 31, 2022 and 2021

(In thousands)

	2022				2021
	Electric System	Generation System	Water System	Combined	Combined
Operating Revenues:					
Retail sales	$ 655,785	$ –	$ 14,329	$ 670,114	$ 647,009
Wholesale sales	73,375	28,743	769	74,144	43,423
Other	36,161	221	408	36,790	32,978
Total Operating Revenues	**765,321**	**28,964**	**15,506**	**781,048**	**723,410**
Operating Expenses:					
Purchased power	363,509	–	–	334,766	310,693
Purchased water	–	–	3,600	3,600	3,217
Operations	193,586	5,415	4,594	203,596	188,233
Maintenance	48,624	4,476	2,047	55,147	39,608
Depreciation	60,948	5,784	3,497	70,229	68,063
Taxes	40,732	93	775	41,600	40,424
Total Operating Expenses	**707,399**	**15,768**	**14,513**	**708,938**	**650,238**
Net Operating Income	**57,922**	**13,196**	**993**	**72,110**	**73,172**
Interest Charges:					
Interest	18,842	4,752	369	22,653	20,156
Amortization of debt related costs	(5,587)	(2,269)	(397)	(8,253)	(3,484)
Total Interest Charges	**13,255**	**2,483**	**(28)**	**14,400**	**16,672**
Other Income and Expense:					
Interest income, fair value adjustments, net	(3,115)	93	(38)	(4,369)	(840)
Other income and expense, net	3,585	287	3,123	6,997	3,319
Total Other Income and Expense	**472**	**380**	**3,085**	**2,628**	**2,479**
Net Income Before Capital Contributions	**45,139**	**11,093**	**4,107**	**60,338**	**58,979**
Capital Contributions	**28,294**	**135**	**4,934**	**33,363**	**34,037**
Net Income	**73,433**	**11,228**	**9,040**	**93,701**	**93,016**
Net Position, Beginning of year	1,431,347	109,032	145,097	1,685,476	1,592,460
Net Position, End of year	**$1,504,780**	**$ 120,260**	**$ 154,137**	**$ 1,779,177**	**$ 1,685,476**

The accompanying notes are an integral part of these combined financial statements.

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Combined Statements of Cash Flows

Years ended December 31, 2022 and 2021

(In thousands)

	2022				2021
	Electric System	Generation System	Water System	Combined	Combined
Cash Flows from Operating Activities:					
Cash received from customers	$731,465	$ 28,844	$ 15,224	$746,790	$668,474
Cash payments to suppliers	(587,455)	(6,502)	(8,013)	(573,227)	(469,836)
Cash payments to employees	(101,306)	(5,941)	(4,284)	(111,531)	(106,414)
Cash payments for taxes	(39,202)	(107)	(781)	(40,090)	(36,876)
Other cash received (paid)	104,413	1,551	1,347	107,311	27,520
Net Cash Provided by Operating Activities	**107,915**	**17,845**	**3,493**	**129,253**	**82,868**
Cash Flows from Capital & Related Financing Activities:					
Capital construction	(118,059)	(6,234)	(6,562)	(130,855)	(107,639)
Proceeds from debt	68,519	–	1,620	70,139	107,745
Repayment of debt	(11,510)	(5,120)	(1,716)	(18,346)	(17,551)
Debt issuance costs	(543)	–	–	(543)	(615)
Interest paid on debt	(18,629)	(4,774)	(375)	(22,468)	(19,971)
Capital contributions	26,290	135	1,724	28,149	26,994
Intercompany loans	3,585	(3,585)	–	–	–
Other cash received (paid)	4,443	155	660	5,258	–
Net Cash Provided by (Used for) Capital & Related Financing Activities	**(45,904)**	**(19,423)**	**(4,649)**	**(68,666)**	**(11,037)**
Cash Flows from Investing Activities:					
Sale of special funds and investment securities	314,954	16,386	23,142	354,482	288,673
Purchase of special funds and investment securities	(398,572)	(17,924)	(21,224)	(437,720)	(390,858)
Interest on investment securities	10,079	629	302	9,700	7,101
Net Cash Provided by (Used for) Investing Activities	**(73,539)**	**(909)**	**2,220**	**(73,538)**	**(95,084)**
Cash Flows from Non–Capital Financing Activities:					
Non–capital grants received	2,889	84	–	2,973	1,209
Net Cash Provided by Non–Capital Financing Activities	**2,889**	**84**	**–**	**2,973**	**1,209**
Net Increase (Decrease) in Cash & Cash Equivalents	**(8,639)**	**(2,403)**	**1,064**	**(9,978)**	**(22,044)**
Beginning of Year	40,306	7,126	1,862	49,294	71,338
Cash & Cash Equivalents – End of Year	**$ 31,667**	**$ 4,723**	**$ 2,926**	**$ 39,316**	**$ 49,294**

The accompanying notes are an integral part of these combined financial statements.

Combined Statements of Cash Flows (continued)

Years ended December 31, 2022 and 2021

(In thousands)

	2022				2021
	Electric System	Generation System	Water System	Combined	Combined
Reconciliation of Net Operating Income to Net Cash Provided by Operating Activities:					
Net Operating Income (Loss)	$ 57,922	$ 13,195	$ 993	$ 72,110	$ 73,172
Adjustments to net operating income					
Depreciation Expense	60,948	5,784	3,496	70,228	68,063
Pension and OPEB Related	(20,587)	(637)	(539)	(21,763)	(46,347)
Other cash received (paid)	(593)		(3)	(596)	(2,872)
(Increase) decrease in receivables	(4,771)	(119)	(28)	(4,918)	(16,889)
(Increase) decrease in other assets	(14,244)	(105)	(1,191)	(15,540)	(2,053)
Increase (decrease) in payables	25,071	232	1,414	26,717	7,516
Increase (decrease) in other liabilities	4,169	(505)	(649)	3,015	2,278
Total Adjustments	**49,993**	**4,650**	**2,500**	**57,143**	**9,696**
Net Cash Provided by Operating Activities	**$ 107,915**	**$ 17,845**	**$ 3,493**	**$ 129,253**	**$ 82,868**
Non–cash Investing, Capital and Related Financing Activities					
Non–cash contributions	$ 3,977		$ 3,210	$ 7,188	$ 9,089
Changes in valuation of financial instruments	(11,390)	(276)	(405)	(12,071)	(5,046)
Amortization of debt related costs	5,587	2,269	397	8,254	3,484

The accompanying notes are an integral part of these combined financial statements.

Notes to Combined Financial Statements

December 31, 2022 and 2021

Note 1
Summary of Significant Accounting Policies

Public Utility District No. 1 of Snohomish County, Washington, (the PUD) is a public electric and water utility serving Snohomish County and Camano Island in Island County, Washington. The PUD's operations consist of three systems: the Electric System, the Generation System, and the Water System. The PUD is governed by a three-member Board of Commissioners (the Commission), which is elected for staggered six-year terms. The legal responsibilities and powers of the PUD, including the establishment of rates and charges for services rendered, are exercised through the Commission.

The Electric System is made up of the PUD's electric transmission and distribution system and the microgrid system that went into service in 2022. The Generation System is composed of the PUD's Henry M. Jackson Hydroelectric Project and four smaller hydroelectric projects, and a biofuel generator that went in to service in 2022. The Water System is made up of the PUD's water distribution system.

The accompanying financial statements for 2022 include the individual and combined statements of net position for the Electric System, Generation System, and Water System, and the individual and combined statements of revenues, expenses, and changes in net position, and the individual and combined statements of cash flows for each system. System columns presented in the financial statements and notes may not add to the combined totals due to the elimination of intercompany transactions, which consist of intersystem loans and routine intercompany transactions.

The PUD's financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when incurred. Revenues and costs that are directly related to the generation, purchase, transmission, and distribution of electricity or water are reported as operating revenues and expenses. All other revenues and expenses are reported as non-operating revenues and expenses.

The accompanying financial statements have been prepared in conformity with Generally Accepted Accounting Principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The PUD's other significant accounting and financial policies are described in the following sections.

Retail Sales

The PUD bills Electric and Water System customers for their consumption on a monthly basis. The accompanying financial statements include estimated unbilled revenues for electricity and water delivered to customers between the last billing date and the end of the year. Unbilled electric revenue was $47.4 million and $40.5 million as of December 31, 2022, and 2021, respectively. Unbilled water revenue was $731 and $607 thousand as of December 31, 2022, and 2021, respectively. Power sales and purchase transactions are recognized over the duration of the contracts as a component of retail and wholesale revenue and purchased power operating expenses.

Cash Equivalents

The PUD considers highly liquid, short-term investments with original maturities of three months or less to be cash equivalents.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are recorded when invoices are issued and are written off when they are determined to be uncollectible. A reserve is established for uncollectible accounts receivable based upon historical write-off trends and knowledge of specific circumstances that indicate collection of an account may be unlikely. The allowance for doubtful accounts was $3.4 million and $14.1 million as of December 31, 2022 and 2021, respectively. In 2022, the PUD resumed the practice of disconnecting service for non-payment and reduced the allowance for doubtful accounts to reflect the change in accounts receivable. In December 2022, the PUD received a grant of $11.2 million to help alleviate customer accounts in arrears.

Material and Supplies

Material and supplies are recorded at average cost and consist primarily of materials for construction and maintenance of utility plant.

Special Funds

Special funds are restricted or limited-use funds that have been established in accordance with Commission resolutions, bond resolutions, state law or other agreements. These funds, which consist of cash, cash equivalents, and investments, are restricted for specific purposes, including debt service, bond reserves, rate stabilization, qualifying capital expenditures, postemployment benefits, FERC license commitments, and other reserve requirements. It is the PUD's policy to use unrestricted funds prior to using restricted funds except for bond proceeds used for qualifying capital expenditures and funds set aside for debt service payments.

Unamortized Loss on Refunding Debt

The difference between the cost to defease outstanding debt and the carrying value of bonds defeased by refunding bonds is deferred and amortized over the shorter of the remaining term of the refunded bonds or the term of the refunding bonds, using the straight-line or effective-interest method. This difference for bonds defeased by operating funds is charged in the current period.

Net Position

Net position consists of the following components:

> ***Net investment in capital assets*** – This component consists of capital assets, net of accumulated depreciation reduced by the net outstanding debt balances related to capital assets, net of unamortized debt related costs.
>
> ***Restricted*** – This component consists of assets and liabilities with constraints placed on use. Constraints include those imposed by bond covenants or third-party contractual agreements, and resources restricted by Board resolution.
>
> ***Unrestricted*** – This component consists of assets and liabilities that do not meet the definition of "net investment in capital assets" or "restricted."

Compensated Absences

Employees accrue paid time off (PTO) or vacation in varying amounts according to their years of service. Accrued liability for PTO and vacation was $17.6 million and $16.9 million at December 31, 2022 and 2021, respectively. These liabilities are presented as part of other liabilities.

Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. The PUD has used estimates in determining reported amounts including unbilled revenue, allowance for doubtful accounts, accrued liability for injuries and damages, depreciable lives of utility plant, pensions, and other contingencies. Actual results could differ from these estimates.

During 2022, a change in accounting estimate was made for the provision of outstanding damage claims. The newly adopted accounting estimate is preferable over the prior method used bringing the provision balance closer to the five-year actual average uncollectible. The impacted accounts are bad debt expense and provision for uncollectible accounts.

In 2022, the PUD implemented a new reporting module for long-term debt which improved the precision of related bond premium and discount amortization calculations. The implementation and associated change in estimate for amortization calculations resulted in a $5 million increase in net position for the period.

Accounting Changes and Reclassifications

In June 2017, the GASB issued Statement No. 87 *Leases*, which establishes a standard for lease accounting based on the fact that leases are a financial exchange for the right to use an underlying asset. The PUD has adopted the provisions of GASB Statement No. 87 effective January 1, 2021, which resulted in the restatement of financial position as of December 31, 2021. (Note 4)

Certain reclassifications have been made to the 2021 financial statements to conform to the 2022 presentation.

Note 2
Special Funds and Cash and Temporary Investments

The PUD's investment policy authorizes the investment of funds in U.S. Treasury, federal and United States government-sponsored enterprise agency obligations, interest-bearing demand or time deposits, municipal bonds, supranational securities, bankers' acceptances, and certain other investments. Interest-bearing demand or time deposits with a qualified public depository of the State of Washington are protected and collateralized under the Washington State Public Deposit Protection Act. In all instances, the PUD evaluates the creditworthiness of the financial institutions with which it invests.

All PUD investments are in compliance with the State of Washington statutes and PUD bond resolutions. Substantially all PUD investments are recorded at fair value based on observable market prices or indices. The relative type of PUD's investments at December 31, 2022 and 2021 are summarized in Table 1.

Table 1
Special Funds and Cash and Temporary Investments

	Electric System		Generation System		Water System	
	2022	2021	2022	2021	2022	2021
U.S. Treasury Securities	56%	53%	43%	44%	38%	50%
U.S. Agency Obligations						
Federal Home Loan Bank	14%	12%	3%	–	25%	4%
Federal Farm Credit Bank	8%	7%	–	–	21%	17%
Federal National Mortgage Association	3%	5%	–	–	–	2%
Federal Home Loan Mortgage Corporation	4%	6%	–	–	–	–
Private Export Funding Corporation	–	1%	–	–	–	–
Cash and Interest–bearing Demand or Time Deposits	4%	3%	–	–	1%	1%
Washington State Local Government Investment Pool	11%	13%	54%	56%	15%	26%

The PUD invests funds consistent with the following objectives: conform with state and local statutes, preserve principal, maintain adequate liquidity, and maximize yield. The PUD's investments are purchased with the objective of holding the security until maturity.

Investment securities owned by the PUD are registered in the PUD's name and held in trust by banks or trust companies. Other PUD investments are insured by federal depository insurance or protected against loss as they are on deposit with financial institutions recognized as qualified public depositories of the State of Washington.

The Washington State Local Government Investment Pool (LGIP) is an investment vehicle operated by the Washington State Treasurer, offering governmental agency investors the economies of scale available from a multi-billion-dollar pooled fund investment portfolio. As of December 31, 2022, LGIP investments include primarily U.S. Agency Securities, U.S. Treasury Securities, repurchase agreements, and interest-bearing bank deposits. The PUD records these investments at amortized cost.

The PUD must give notice to the LGIP if the PUD plans to withdraw over $1.0 million on the same day. The LGIP may suspend withdrawals or liquidate if the difference between the amortized cost per share and the market net asset value per share results in material dilution or other unfair results. The LGIP may suspend redemptions if the New York Stock Exchange suspends trading or closes, if the US bond markets are closed, and if the Securities and Exchange Commission declares an emergency.

In order to address custodial credit risk, all investments except cash, interest-bearing demand or time deposits, and funds held in the LGIP, which are not evidenced by securities, are held in the PUD's name by a third-party custodian. The PUD addresses concentration of credit risk by investing in a diversified portfolio.

The PUD manages its exposure to decreases in the fair value of its investments arising from increasing interest rates by setting maturity limits for its investments. All funds are invested in instruments with maturities of less than five years, with the weighted average maturity of the invested portfolio remaining below three years. The PUD's investment policy specifies that the investment portfolio be structured so maturing investments match projected cash flow needs in order to mitigate interest rate risk. Investment maturities for combined special funds and cash and temporary investments as of December 31, were as follows (in thousands):

	2022		2021	
Term	Amount Invested	Percent of Invested Fund	Amount Invested	Percent of Invested Fund
Less than 30 days	$ 94,097	16%	$ 88,520	17%
30 to 90 days	45,572	8%	35,555	7%
90 days to 1 year	136,977	23%	155,510	29%
1 year to 5 years	283,099	48%	221,938	42%
Bond reserves invested to bond maturity	27,667	5%	24,698	5%
	$ 587,412	**100%**	**$ 526,221**	**100%**

Fair value is the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. The PUD's investments, at fair value, can be categorized by valuation techniques into two levels. Level 1 investments are traded on a national securities exchange and are valued at the last reported sales price on the last business day of the year. Level 2 investments are valued using pricing models maximizing the use of observable inputs for similar securities.

The table below shows the fair value hierarchy for each system's investments subject to fair value measurement, as of December 31 (in thousands):

	2022						2021	
	Electric		Generation		Water		Combined	
	Level 1	Level 2	Level 1	Level 2	Level 1	Level 2	Level 1	Level 2
U.S. Treasury Notes	$ 301,502	$ –	$ 10,701	$ –	$ 9,993	$ –	$ 276,974	$ –
Federal Home Loan Mortgage Corporation	–	22,934	–	–	–	–	–	27,954
Federal Farm Credit Bank	–	40,641	–	–	–	5,439	–	36,501
Federal Home Loan Bank	–	77,768	–	730	–	6,460	–	57,357
Federal National Mortgage Association	–	14,887	–	–	–	–	–	26,494
Private Export Funding Corp.	–	–	–	–	–	–	–	2,421
Assets valued at fair value	**$301,502**	**$ 156,230**	**$10,701**	**$ 730**	**$ 9,993**	**$ 11,899**	**$ 276,974**	**$150,727**

Note 3
Capital Assets

Utility Plant

Utility plant is stated at cost. The PUD's capitalization threshold for utility plant is $5,000. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, ranging from 5 to 77 years. When utility plant assets are retired, the original cost together with removal costs, less salvage, is charged to accumulated depreciation. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and betterments is capitalized. See Table 2 for additional utility plant details.

The PUD periodically reviews the carrying value of its utility plant and other equipment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

Capital Contributions

The PUD records capital contributions from customers and developers, primarily relating to expansions to the PUD's distribution facilities, as a separate category of non-operating revenue.

Table 2
Utility Plant
(In thousands)

	2020	2021			2022		
	Ending Balance	Additions	Retirements & Transfers	Ending Balance	Additions	Retirements & Transfers	Ending Balance
Electric System							
Transmission	$ 182,706	$ 4,395	$ (802)	$ 186,299	$ 3,566	$ (687)	$ 189,178
Distribution	1,317,397	72,529	(8,698)	1,381,228	62,066	(6,354)	1,436,940
General Plant & Other	417,967	11,140	(3,644)	425,463	29,085	(3,986)	450,562
Land & Non-depreciable assets[1]	74,806	649	(1)	75,454	1,861	(3)	77,312
Plant in Service	1,992,876	88,713	(13,145)	2,068,444	96,578	(11,030)	2,153,992
Construction Work in Progress	103,177	21,430	–	124,607	30,548	–	155,155
Utility Plant	2,096,053	110,143	(13,145)	2,193,051	127,126	(11,030)	2,309,147
Less Accumulated Depreciation	(784,514)	(56,383)	6,523	(834,374)	(57,638)	2,629	(889,383)
Net Utility Plant	**$1,311,539**	**$ 53,760**	**$ (6,622)**	**$1,358,677**	**$ 69,488**	**$ (8,401)**	**$1,419,764**

[1] *Plant in service includes right-to-use assets of $4.1 million and $2.2 million December 31, 2022 and 2021 respectively.*

	2020 Ending Balance	2021 Additions	2021 Retirements & Transfers	2021 Ending Balance	2022 Additions	2022 Retirements & Transfers	2022 Ending Balance
Generation System							
Generation/Production	$ 295,025	$ 1,413	$ (331)	$ 296,107	$ 1,940	$ (280)	$ 297,767
Transmission	2,811	–	–	2,811	326	(221)	2,916
Distribution	6,820	15	–	6,835	1,979	–	8,814
General Plant & Other	30,387	786	–	31,173	855	(524)	31,504
Land & Non-depreciable assets[2]	13,822	–	–	13,822	28	–	13,850
Plant in Service	348,865	2,214	(331)	350,748	5,128	(1,025)	354,851
Construction Work in Progress	3,300	1,823	–	5,123	1,107	–	6,230
Utility Plant	352,165	4,037	(331)	355,871	6,235	(1,025)	361,081
Less Accumulated Depreciation	(151,742)	(5,600)	39	(157,303)	(5,254)	494	(162,063)
Net Utility Plant	**$ 200,423**	**$ (1,563)**	**$ (292)**	**$ 198,568**	**$ 981**	**$ (531)**	**$ 199,018**

[2] *Plant in service includes right-to-use assets of $0.2 million and $0 December 31, 2022 and 2021 respectively.*

	2020 Ending Balance	2021 Additions	2021 Retirements & Transfers	2021 Ending Balance	2022 Additions	2022 Retirements & Transfers	2022 Ending Balance
Water System							
Generation/Production	$ 9,356	$ 45	$ (4)	$ 9,397	$ 21	$ –	$ 9,418
Transmission & Distribution	139,001	4,550	(398)	143,153	10,421	(52)	153,522
General Plant & Other	14,207	–	–	14,207	91	(82)	14,216
Land & Non-depreciable assets	4,054	104	–	4,158	–	11	4,169
Plant in Service	166,618	4,699	(402)	170,915	10,533	(123)	181,325
Construction Work in Progress	1,230	3,330	–	4,560	–	(829)	3,731
Utility Plant	167,848	8,029	(402)	175,475	10,533	(952)	185,056
Less Accumulated Depreciation	(42,182)	(3,239)	1,164	(44,257)	(3,540)	235	(47,562)
Net Utility Plant	**$ 125,666**	**$ 4,790**	**$ 762**	**$ 131,218**	**$ 6,993**	**$ (717)**	**$ 137,494**

Note 4
Leases

In June 2017, the GASB issued Statement No. 87 Leases, which established a standard to enhance consistency in accounting and financial reporting for leases based on the fact that leases are a financial exchange for the right-to-use an underlying asset. To comply with the statement the lessor and lessee involved in the lease agreement are required to recognize on their financial statements a lease receivable and deferred inflow of resources or a lease liability and intangible right-to-use lease asset, respectively. The PUD adopted the provisions of GASB Statement No. 87 on January 1, 2021, and restated the individual and combined statements of net position as of December 31, 2021, accordingly, to reflect the implementation of this statement as summarized below (in thousands):

	Electric	Water
December 31, 2021, balances previously reported		
Right-to-use asset	$ –	$ –
Lease liability	–	–
Deferred inflow - leases	–	–
Lease receivable	–	–
Restatement for adoption of GASB Statement No. 87		
Right-to-use asset	$ 2,169	$ –
Lease liability	(2,169)	–
Deferred inflow - leases	(24,363)	(1,454)
Lease receivable	24,363	1,454
As restated December 31, 2021		
Right-to-use asset	$ 2,169	$ –
Lease liability	(2,169)	–
Deferred inflow - leases	(24,363)	(1,454)
Lease receivable	24,363	1,454

The District is both a lessor and a lessee:

For leases with a maximum possible term of 12 months or less at commencement, the PUD recognizes revenue or expense based on the provisions in each contract. For all other leases (i.e., those that are not short-term) as a lessee or lessor the PUD recognizes a right-to-use asset, and lease liability or a lease receivable, and deferred inflow, respectively, in accordance with GASB Statement No. 87.

District as a lessee - The following table summarizes the balances of leased assets by major classes reported in Net Utility Plant as of December 31, 2022 (in thousands):

	December 31, 2022	
	Electric	Generation
Right-to-use asset - Land	$ 4,071	$ –
Less Accumulated amortization	242	–
Right-to-use asset - Land, net	3,829	–
Right-to-use asset - Building	419	161
Less Accumulated amortization	140	9
Right-to-use asset - Building, net	279	152
Total Right-to-use assets	**$ 4,108**	**$ 152**

The PUD is involved in several leases and subleases of land and buildings to perform District operations. The obligations relating to these leases have been recognized on the Combined Statement of Net Position as both a right-to-use asset and the related lease liability equal to the present value of the lease payments in each agreement payable during the contracted term. In 2022, the PUD recorded $0.4 million as amortization and $0.1 million as interest expense to recognize these leased assets.

All lessee activity resides within the Electric System with the exception of one Generation System lease related to the biofuel project. The seven-year lease for the biofuel project was implemented in September 2022, with future annual principal and interest payment of approximately $30,000. As of December 31, 2022, the PUD had principal and interest requirements for active leasing activities, as follows (in thousands):

Year Ended December 31	Principal	Interest	Total
2023	$ 283	$ 138	$ 421
2024	279	137	416
2025	139	137	276
2026	145	136	281
2027	151	135	286
2028-2032	292	666	958
2033-2037	145	653	798
2038-2042	372	601	973
2043-2047	752	483	1,235
2048-2052	1,311	265	1,576
2053-2054	534	17	551
Total	**$ 4,403**	**$ 3,368**	**$ 7,771**

District as a lessor - The PUD is also involved in lease agreements as the lessor of assets such as land and pole attachments. These leases are ancillary to the PUD's mission to provide power to its rate payers. The PUD primarily leases space to telecom entities which allows them to provide services to networks.

The PUD has lessor agreements with remaining contract terms ranging from two to thirteen years. These agreements are recorded at their net present value of $23.1 million on the *Combined Statement of Net Position*. The PUD also recognized $4.3 million of lease income, and $0.3 million in lease interest income recorded as other income for the year ended December 31, 2022.

The District monitors changes in circumstances that may require remeasurement of a lease. Remeasurements of leases were performed during the year ended December 2022 as a result of changes to pole attachments throughout the year.

Note 5
Long-Term Debt

Debt service (principal and interest) payments on the PUD's revenue bonds and other notes payable to maturity, excluding intersystem borrowing, are set forth in Table 3.

Table 3
Debt Service (Principal & Interest)
(In thousands)

	Electric System Revenue Bonds		Generation System Revenue Bonds		Water System Revenue Bonds		Water System Loans	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2023	$ 11,985	$ 19,969	$ 5,355	$ 3,206	$ 475	$ 263	$ 418	$ 56
2024	12,815	19,773	5,610	2,937	500	239	418	53
2025	14,860	19,682	1,410	2,654	525	214	418	48
2026	14,275	19,173	1,480	2,583	550	188	418	43
2027	14,695	18,678	1,560	2,505	580	161	418	38
2028-2032	81,470	83,248	9,120	11,207	2,630	337	1,524	131
2033-2037	100,230	59,340	11,765	8,556	–	–	985	63
2038-2042	83,290	32,146	15,165	5,155	–	–	736	22
2043-2047	38,170	19,705	11,065	1,125	–	–	–	–
2048-2052	53,190	7,329	–	–	–	–	–	–
Total	**$ 424,980**	**$ 299,043**	**$ 62,530**	**$ 39,928**	**$ 5,260**	**$ 1,402**	**$ 5,337**	**$ 454**

The Electric, Generation and Water Systems' revenues, net of specified operating expenses, are pledged as security for the systems' revenue bonds until their respective bonds are defeased or repaid. Principal and interest paid for 2022 and 2021 was $40.2 million and $37.1 million, respectively. Total revenues available for debt service as defined for the same periods was $162.8 million and $129.5 million. On December 31, 2022, annual principal and interest payments are expected to require between 23% and 25% of revenues.

Tax-exempt revenue bonds make up the majority of the PUD's long-term debt and are subject to Internal Revenue Service Code (the Code) requirements for arbitrage rebate. Rebates are calculated based on earnings on gross proceeds of the bonds that are in excess of the amount prescribed by the Code.

Electric System

A summary of principal outstanding on Electric System long-term debt follows (in thousands):

	December 31, 2022	December 31, 2021
Series 2022A Revenue bonds, 5.0%, due 2025-2052, earliest call 2032	$ 61,050	$ –
Series 2021A Revenue bonds, 5.0%, due 2026-2051, earliest call 2031	78,685	78,685
Series 2020A Revenue Refunding bonds, 0.4-1.5%, due 2022-2028	46,825	48,755
Series 2015 Revenue bonds, 5.0%, due 2022-2040, earliest call 2025	121,205	123,625
Series 2012 Revenue Refunding bonds, 4.0%, due 2022	–	5,610
Series 2010A Revenue bonds, 4.8-5.6%, due 2022-2035, currently callable	117,215	118,765
Total Principal Outstanding on Long-Term Debt	**$424,980**	**$375,440**

In July 2022, the PUD issued $61.1 million of Series 2022A Electric System Revenue bonds at a premium of $7.5 million with an average interest rate of 3.4%. The proceeds from the bonds will be used to finance additions, betterments and improvements to and renewals, replacement and extensions of the Electric System.

In June 2021, the PUD issued $78.6 million of Series 2021A Electric System Revenue bonds at a premium of $25.9 million with an average interest rate of 1.5%. The proceeds from the bonds will be used to finance additions, betterments and improvements to and renewals, replacements and extensions of the Electric System.

Changes in the Electric System long-term debt during the years ended December 31, 2022, and 2021, follow (in thousands):

	2020	2021			2022		
	Balance	Additions	Reductions	Balance	Additions	Reductions	Balance
Revenue bonds, face amount	$ 307,840	$ 78,685	$ (11,085)	$ 375,440	$ 61,050	$ (11,510)	$ 424,980
Unamortized bond premium	16,830	25,921	(3,331)	39,420	7,469	(6,434)	40,454
Unamortized bond discount	(72)	–	5	(67)	–	16	(51)
Total Debt	324,598	104,606	(14,411)	414,793	68,519	(17,928)	465,384
Less: Current maturities	(11,085)			(11,510)			(11,985)
Total Long-Term Debt	**$ 313,513**			**$ 403,283**			**$ 453,398**

The PUD is obligated as part of its bond resolution to purchase for use in its Electric System all power available to the Electric System from the Generation System. The PUD is also unconditionally obligated by the bond resolution to set aside revenues in amounts sufficient to pay, to the extent not otherwise paid, all the debt service on the Generation System bonds on a parity of lien with the Electric System Senior bonds.

The PUD is required to maintain a cash reserve for certain Electric System bonds. At December 31, 2022 and 2021, the PUD held the reserve requirement of $21.3 million and $18.3 million, respectively, in the Electric System.

The fair value of the Electric System's long-term debt was $447.6 million and $458.7 million, respectively, at December 31, 2022 and 2021. The fair value of the Electric System's long-term debt is estimated based on quoted market prices for the same or similar issues.

Generation System

A summary of principal outstanding on Generation System long-term debt follows (in thousands):

	December 31, 2022	December 31, 2021
Series 2020A Revenue Refunding bonds, 5.0%, due 2022-2024	$ 9,925	$ 14,550
Series 2015 Revenue bonds, 5.0%, due 2025-2045, earliest call 2025	39,985	39,985
Series 2010B Revenue bonds, 5.3-5.7%, due 2022-2040, currently callable	12,620	13,115
Total Principal Outstanding on Long-Term Debt	**$ 62,530**	**$ 67,650**

Changes in the Generation System long-term debt during the years ended December 31, 2022, and 2021, follow (in thousands):

	2020	2021			2022		
	Balance	Additions	Reductions	Balance	Additions	Reductions	Balance
Revenue bonds, face amount	$ 72,540	$ –	$ (4,890)	$ 67,650	$ –	$ (5,120)	$ 62,530
Unamortized bond premiums	6,759	–	(766)	5,993	–	(1,895)	4,098
Unamortized bond discounts	(9)	–	1	(8)	–	2	(6)
Total Debt	79,290	–	(5,655)	73,635	–	(7,013)	66,622
Less: Current maturities	(4,890)			(5,120)			(5,355)
Total Long-Term Debt	**$ 74,400**			**$ 68,515**			**$ 61,267**

The PUD is required to maintain a cash reserve for certain Generation System bonds. At December 31, 2022 and 2021, the PUD maintained the reserve requirement of $6.0 million in the Generation System.

The fair value of the Generation System's long-term debt was $64.9 million and $79.3 million, respectively, at December 31, 2022 and 2021. The fair value of the Generation System's long-term debt is estimated based on quoted market prices for the same or similar issues.

Water System

A summary of principal outstanding on Water System long-term debt follows (in thousands):

	December 31, 2022	December 31, 2021
Series 2019 Revenue Refunding bonds, 5.0%, due 2022-2031	$ 5,260	$ 5,715
Series 2011 Revenue Refunding bonds, 4.0-5.0%, due 2022	–	845
State of Washington Drinking Water Revolving Fund loans:		
equal principal payments plus 1.0% interest due annually through 2042	2,944	3,921
equal principal payments plus 1.0% interest due annually through 2034	1,495	1,619
equal principal payments plus 1.5% interest due annually through 2029	578	661
equal principal payments plus 1.5% interest due annually through 2027	320	384
equal principal payments plus 2.5% interest due annually through 2023	–	48
Total Principal Outstanding on Long-Term Debt	**$ 10,597**	**$ 13,193**

Changes in the Water System long-term debt during the years ended December 31, 2022, and 2021, follow (in thousands):

	2020	2021			2022		
	Balance	Additions	Reductions	Balance	Additions	Reductions	Balance
Revenue bonds, face amount	$ 7,780	$ –	$ (1,220)	$ 6,560	$ –	$ (1,300)	$ 5,260
Unamortized bond premiums	1,498	–	(210)	1,288	–	(445)	843
Other notes payable	3,851	3,139	(357)	6,633	–	(1,296)	5,337
Total Debt	13,129	3,139	(1,787)	14,481	–	(3,041)	11,440
Less: Current maturities	(1,576)			(1,806)			(893)
Total Long-Term Debt	**$ 11,553**			**$ 12,675**			**$ 10,547**

The Water System periodically enters into low-interest loan agreements with the Washington State Public Works Trust Fund and the State of Washington Drinking Water Revolving Fund. These funds have provided various loans to the PUD for the repair, replacement, rehabilitation, and reconstruction of water facilities. In 2022 and 2021, the PUD initiated drawdowns of $2.2 million and $3.1 million respectively, to pay costs associated with acquiring and improving the Warm Beach Water System which was transferred to the PUD in 2018. Of the $2.2 million drawdown initiated in 2022, $0.6 million was recorded as a receivable at December 31, 2022 and subsequently received in January 2023. As of December 31, 2022, the PUD processed final loan closeout documentation related to the Warm Beach Water System loans, allowing the PUD to recognize 50% loan forgiveness, directly reducing the outstanding loan liability by $3.1 million.

The PUD is required to maintain a cash reserve for certain Water System bonds. At December 31, 2022 and 2021, the PUD maintained the reserve requirement of $0.4 million.

The fair value of the Water System's long-term Revenue Bonds was $5.8 million and $7.8 million, respectively, at December 31, 2022 and 2021. The fair value for the Washington State Public Works Trust Fund loan and the State of Washington Drinking Water Revolving Fund loans approximate the carrying amounts since such loans are exclusive and have no market.

Note 6
Retirement and Deferred Compensation Plans

DEFINED BENEFIT PENSION PLANS

The Public Employee Retirement System (PERS) is a cost-sharing multiple-employer retirement system comprised of three separate pension plans for membership purposes. PERS Plan 1 and PERS Plan 2 are defined benefit plans and PERS Plan 3 is a defined benefit plan with a defined contribution component. PERS members include elected officials, state employees, and employees of governmental agencies in the State of Washington.

PERS members who joined the system by September 30, 1977, are Plan 1 members. Those who joined after that date are Plan 2 members unless they exercised an option to transfer their membership to Plan 3. PERS members joining the system on or after March 1, 2002, for state and higher education employees, or September 1, 2002, for local government employees have the irrevocable option of choosing membership in either PERS Plan 2 or Plan 3. The option must be exercised within 90 days of employment. Employees who fail to choose within 90 days default to Plan 2.

PERS is comprised of and reported as three separate plans for accounting purposes. Plan 1 accounts for defined benefits of Plan 1 members; Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members; and Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portion of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

General Benefits Provided

PERS provides retirement, disability, and death benefits. Benefit provisions are established by state statute and can only be modified by the state legislature.

PERS Plan 1 and Plan 2 retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the PERS Plan 1 and Plan 2 defined benefit plans accrue interest at a rate specified by the Director of the Washington State Department of Retirement Systems (DRS). Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan.

The benefit provisions stated in the following paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not receiving them yet are bound by the provisions in effect at the time they terminated their public service.

Substantially all full-time and qualifying part-time PUD employees participate in PERS which is administered by DRS. The state Legislature establishes, and amends, laws pertaining to the creation and administration of all public retirement systems.

Both the PUD and the employees made the required contributions. The PUD's required contributions for the years ended December 31, were (in thousands):

	PERS Plan 1	PERS Plan 2	PERS Plan 3
2022	$ 39	$ 13,262	$ 2,666
2021	$ 83	$ 14,081	$ 2,811
2020	$ 91	$ 14,560	$ 2,898

PERS Plan 1 Description

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.

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 2022 were as follows:

Actual Contribution Rates	*Employer*	*Employee*
September 2020 through June 2021	12.97%	6.00%
July 2021 through August 2022	10.25%	6.00%
September 2022 through December 2022	10.39%	6.00%

The PUD's contributions as reported by PERS to the plan were $5.8 million, and $6.4 million for the years ended December 31, 2022, and 2021, respectively.

PERS Plan 2/3 Description

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

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules.

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

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

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 2022 were as follows:

Actual Contribution Rates	*Employer Plan 2/3*	*Employee Plan 2*	*Employee Plan 3*
September 2020 through June 2021	12.97%	7.90%	varies
July 2021 through August 2022	10.25%	6.36%	varies
September 2022 through December 2022	10.39%	6.36%	varies

The PUD's contributions as reported by PERS to the plan were $10.0 million, and $10.8 million for the years ended December 31, 2022, and 2021, respectively.

Pension Financial Statement Balances

At June 30, 2022, the PUD reported total pension assets of $18.4 million for its proportionate share of the net pension assets and liabilities. The pension liability was $25.7 million for PERS Plan 1 and the pension asset was $44.1 million for PERS Plan 2/3.

At June 30, 2021, the PUD reported a total pension liability of $105.3 million for its proportionate share of the net pension assets and liabilities. The pension liability was $11.3 million for PERS Plan 1 and net pension assets of $116.6 million for PERS Plan 2/3.

The PUD's proportionate share of the net pension plan for PERS Plan 1 was 0.92% and 0.92% for June 30, 2022 and 2021 respectively. The PUD's proportionate share of the PERS Plan 2/3 was 1.19% and 1.17% for June 30, 2022 and 2021 respectively.

Employer contribution transmittals received and processed by 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 DRS in the Schedules of Employer and Non-employer Allocations for all plans.

The collective net pension liability was measured as of June 30, 2022, and the actuarial valuation date on which the total pension liability (asset) is based was as of June 30, 2021, with update procedures used to roll forward the total pension liability to the measurement date.

For the years ended December 31, 2022, and 2021, the PUD recognized a pension expense of $6.0 million and a pension credit of $5.8 million, respectively, for PERS Plan 1 and a pension credit of $23.8 million and $37.0 million, respectively, for PERS Plan 2/3.

At December 31, the PUD reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources (in thousands):

	2022				2021			
	PERS 1		*PERS 2/3*		*PERS 1*		*PERS 2/3*	
	Deferred Outflow	*Deferred Inflow*	*Deferred Outflow*	*Deferred Inflow*	*Deferred Outflow*	*Deferred Inflow*	*Deferred Outflow*	*Deferred Inflow*
Differences between expected and actual experience	$ –	$ –	$ 10,930	$ 999	$ –	$ –	$ 5,665	$ 1,430
Net difference between projected and actual investment earnings on pension plan investments	–	4,254	–	32,612	–	12,522	–	97,488
Change of assumptions	–	–	24,586	6,438	–	–	170	8,284
Changes in proportion and differences between contributions and proportionate share of contributions	–	–	1,518	1,725	–	–	2,545	2,087
Contributions subsequent to measurement date	2,997	–	5,002	–	2,867	–	4,820	–
	$ 2,997	$ 4,254	$ 42,036	$ 41,774	$2,867	$ 12,522	$ 13,200	$ 109,289

Deferred outflows of resources related to pensions resulting from the PUD's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2023. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension (credit) expense as follows (in thousands):

Year ended December 31:	PERS 1	PERS 2/3
2022	$ –	$ (98)
2023	(1,800)	14,115
2024	(1,635)	(11,784)
2025	(2,051)	(7,782)
2026	1,232	(9,265)
2027 - 2028	–	10,074
Total	**$ (4,254)**	**$ (4,740)**

Actuarial Assumptions

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2022 with a valuation date of June 30, 2021. The actuarial assumptions used in the valuation were based on the results of the Office of the State Actuary's (OSA) 2013-2018 Demographic Experience Study and the 2021 Economic Experience Study.

Additional assumptions for subsequent events and law changes are current as of the 2021 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2022. Plan liabilities were rolled forward from June 30, 2021, to June 30, 2022, reflecting each plan's normal cost (using the entry-age cost method), assumed interest and actual benefit payments. Other assumptions included:

- Inflation: 2.75% total economic inflation; 3.25% salary inflation
- Salary increases: In addition to the base 3.25% salary inflation assumption, salaries are also expected to grow by promotions and longevity.
- Investment rate of return: 7.00%

Mortality rates were developed using the Society of Actuaries' Pub. H-2010 mortality rates, which vary by member status (e.g. active, retiree, or survivor), as the base table. OSA applied age offsets for each system, as appropriate, to better tailor the mortality rates to the demographics of each plan. OSA applied the long-term MP-2017 generational improvement scale, also developed by the Society of Actuaries, to project mortality rates for every year after the 2010 base table. Mortality rates are applied on a generational basis; meaning, each member is assumed to receive additional mortality improvements in each future year throughout their lifetime.

Methods did not change from the prior contribution rate setting June 30, 2019 Actuarial Valuation Report (AVR), however OSA introduced a temporary method change to produce asset and liability measures for the June 30, 2020 AVR. There were also the following assumption changes:

- OSA updated the Joint-and-Survivor Factors and Early Retirement Factors in the model. Those factors are used to value benefits for early retirement and survivors of members that are deceased prior to retirement. These factors match the administrative factors provided to DRS for future implementation that reflect current demographic and economic assumptions.

The discount rate used to measure the total pension liability for all DRS plans was 7.0%. To determine that rate, an asset sufficiency test was completed to test whether each pension plan's fiduciary net position was sufficient to make all projected future benefit payments for current plan members. Based on OSA's 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 7.0% was used to determine the total liability.

The long-term expected rate of return on the DRS pension plan investments of 7.0% was determined using a building-block-method. In selecting this assumption, OSA reviewed the historical experience data, considered the historical conditions that produced past annual investment returns, and considered Capital Market Assumptions (CMAs) and simulated expected investment returns provided by the Washington State Investment Board (WSIB). The WSIB uses the CMA's and their target asset allocation to simulate future investment returns at various future times.

Estimated Rates of Return by Asset Class

The table below summarizes the 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, 2022. The inflation component used to create the table is 2.2% and represents the WSIB's most recent long-term estimate of broad economic inflation.

Asset Class	Target Allocation	Long-term Expected Real Rate of Return
Fixed Income	20%	1.50%
Tangible Assets	7%	4.70%
Real Estate	18%	5.40%
Global Equity	32%	5.90%
Private Equity	23%	8.90%

Sensitivity of Net Pension Liability/(Asset)

The table below presents the PUD's proportionate share of the net pension liability/(asset) calculated using the current discount rate, as well as the PUD's proportionate share of the net pension liability if it were calculated using a discount rate that is 1 percentage point lower or 1 percentage point higher than the current rate (in millions).

	2022			2021		
	1% Decrease (6.0%)	Discount Rate (7.0%)	1% Increase (8.0%)	1% Decrease (6.4%)	Discount Rate (7.4%)	1% Increase (8.4%)
PERS Plan 1	$ 34.3	$ 25.7	$ 18.1	$ 19.2	$ 11.3	$ 4.4
PERS Plan 2/3	51.9	(44.1)	(123.0)	(33.2)	(116.6)	(185.3)

Pension Liability Allocation

The pension liability has been allocated to the Electric, Generation and Water Systems, based on percentages of staffing levels between the systems. The PUD's proportionate share of net pension liability (asset) for each plan, as of December 31, is as follows (in thousands):

	December 31, 2022		December 31, 2021	
	PERS Plan 1	PERS Plan 2/3	PERS Plan 1	PERS Plan 2/3
Electric System	$ 24,368	$ (42,009)	$ 10,760	$ (110,623)
Generation System	665	(844)	243	(2,966)
Water System	638	(1,259)	281	(3,056)

Pension Plan Fiduciary Net Position

Detailed information about each defined benefit pension plans' fiduciary net position is available in the separately issued DRS ACFR financial report. The DRS ACFR may be obtained by writing to: Department of Retirement Systems, Communications Unit, P.O. Box 48380, Olympia WA 98504-8380

POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS (OPEB)

The PUD implemented GASB No. 75 to recognize net liability related to OPEB and its disclosure requirements. There are two OPEB plans, healthcare and life insurance. They are a single-employer defined benefit OPEB plan administered by the PUD. There are no stand-alone financial statements presented for either of these plans.

Plan Descriptions

Healthcare Plan

The PUD administers retiree self-insured medical and vision insurance and Health Reimbursement arrangement (HRA) benefits for eligible retirees hired before July 1, 2009, and their dependents. Retiree benefit provisions are established by Commission resolution.

In general, the PUD pays a contribution toward the retiree's PUD group health plan premiums or to a Health Reimbursement Arrangement (HRA). For retirees and their dependents under age 65 who elect a PUD group medical plan, the PUD contribution is based on 75% of the premium for the most commonly elected retiree health plan during the prior year. Retirees and their dependents under age 65 who waive PUD group medical plan coverage receive a $180 monthly contribution into their HRA. When a retiree or dependent becomes eligible for Medicare at age 65, the retiree is no longer eligible for the group medical plan; however, the PUD contributes $180 a month to the retiree's HRA. This OPEB plan is closed to employees hired after July 1, 2009. In 2022 and 2021, the PUD contributed $2.4 and $2.9 million, respectively, to the plans. Plan members receiving benefits contributed $0.4 million in 2022 and contributed $0.4 million in 2021.

Retiree Life Insurance

The PUD administers life insurance benefits related to a term life insurance plan terminated in 1986 for eligible retirees. The retiree life insurance benefit provisions were established by Commission resolution.

Employees who were covered by the PUD's group term life insurance prior to November 1986 may reinstate this insurance at the time of retirement subject to a $60,000 maximum benefit. Retiree insurance premium contribution amounts are established by the Commission. The PUD entered into an insurance contract to fully insure the life insurance obligation, and contributed $345,000 and $354,000 towards the premium in 2022 and 2021, respectively.

Valuation Date, Measurement Date and Reporting Date

The Valuation Date of OPEB liability is December 31, 2020. This is the date as of which the census data is gathered, and the actuarial valuation is performed. The Measurement Date is December 31, 2021. This is the date as of which the total OPEB liability is determined and rolled forward to the reporting date of December 31, 2022. The reporting date is December 31, 2022, the PUD's fiscal year-end. GASB Statement No. 75 allows a lag of up to one year between the measurement date and the reporting date. There have been no significant changes between the valuation date and fiscal year ends. No adjustment is required between the measurement date and the reporting date.

Actuarial assumptions and other inputs

The total OPEB liability in the December 31, 2022, actuarial valuation was determined using the following actuarial assumptions and other inputs, applied to all periods included in the measurement, unless otherwise specified:

Inflation	2.0% based on Actuary's capital market expectations.
Salary increases	2.75% for which the assumption above inflation is based upon the most recent pension valuation for Plan 2 of the Public Employees Retirement System (PERS), a subset of the Washington State Retirement Systems.
Discount rate	2.06% as of the measurement date of December 31, 2021
Healthcare cost trend rates	6.5 % for 2020, decreasing to an ultimate rate of 4.5 % for 2040 and later years.
Retirees' share of health benefit-related costs	25% of projected health insurance premiums for retirees.
Life insurance cost trend rates	4.5% for 2022-2027
Retirees' share of life benefit-related costs	25% of projected life insurance premiums for retirees in 2022 and after.

The discount rate was based on 20-Year Tax-Exempt Municipal Bond Yield, as required by GASB Statement No. 75.

Mortality rates were based on the RP-2000 Healthy Mortality Table for Males or Females, as appropriate, with 100% of Scale BB fully generational offset one year.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The actuarial assumptions used in the December 31, 2021, valuation were based on the results of an actuarial experience study for the period ended December 31, 2020.

OPEB Liability

As of December 31, 2022, the PUD's total OPEB liability for retiree healthcare was $41.6 million, and $5.5 million for retiree life benefits, recorded in other accrued and other liabilities. The annual payroll of active employees covered by the plan was $70.1 million in 2022, compared to $74.1 million in 2021.

The following census of membership was used in the actuarial valuation:

	Healthcare	Life
Retirees (and beneficiaries for healthcare)	643	209
Active employees	469	3
	1,112	**212**

The following table shows the changes in the PUD's net OPEB liability (in thousands):

HEALTHCARE	2022			2021
	Electric	Generation	Water	Combined
Net OPEB liability – beginning of year	$ 39,934	$ 961	$ 1,004	$ 46,302
Changes for the year:				
Service Cost	923	29	24	1,569
Interest on total OPEB liability	835	26	22	1,274
Effect of economic/demographic gains/(losses)	–	–	–	(905)
Effect of assumptions changes or inputs	224	7	6	(3,602)
Expected benefit payments	(2,290)	(71)	(60)	(2,739)
Net Changes	(308)	(9)	(8)	(4,403)
Net OPEB liability – end of year	**$ 39,626**	**$ 952**	**$ 996**	**$ 41,899**

LIFE	2022			2021
	Electric	Generation	Water	Combined
Net OPEB liability – beginning of year	$ 5,423	$ 141	$ 143	$ 4,942
Actuarial beginning of year adjustment				
Changes for the year:				
Service Cost	4	–	–	12
Interest on total OPEB liability	111	3	3	132
Effect of economic/demographic gains/(losses)	–	–	–	884
Effect of assumptions changes or inputs	32	1	1	38
Expected benefit payments	(332)	(10)	(9)	(301)
Net Changes	(185)	(6)	(5)	765
Net OPEB liability – end of year	**$ 5,238**	**$ 135**	**$ 138**	**$ 5,707**

Changes of assumptions and other inputs reflect a change in the discount rate from 2.12 percent in 2021 to 2.06 percent in 2022. The schedule of changes in the PUD's total OPEB liability and related ratios is included in the Required Supplementary Information.

Sensitivity Analysis

Sensitivity of the total OPEB liability to changes in the discount rate

The following presents the total OPEB liability of the PUD, calculated using the discount rate of 2.12%, as well as what the PUD's total OPEB liability would be if it were calculated using a discount rate that is 1 percentage point lower (1.12%) or 1 percentage point higher (3.12%) than the current rate (in millions):

	2022		
	1% Decrease (1.06%)	Current Discount Rate (2.06%)	1% Increase (3.06%)
Healthcare	$ 45.9	$ 41.6	$ 37.9
Life	6.1	5.5	5.0

Sensitivity of the total OPEB liability to changes in the healthcare cost trend rate

The following presents the total OPEB liability of the PUD, calculated using the current healthcare cost trend rates as well as what the PUD's total OPEB liability would be if it were calculated using trend rates that are 1 percentage point lower or 1 percentage point higher than the current healthcare cost trend rates (in millions):

	2022		
	1% Decrease 5.50% Graded Down to 3.50%	Current Trend Rate 6.50% Graded Down to 4.50%	1% Increase 7.50% Graded Down to 5.50%
Healthcare	$ 40.1	$ 41.6	$ 43.3

OPEB Financial Statement Balances

For the year ended December 31, 2022, and 2021, the PUD recognized OPEB healthcare expense of $1.0 million and $1.9 million, respectively. For OPEB life insurance, the PUD recognized OPEB expense of $0.2 million for each of the years ended December 31, 2022, and 2021. At December 31, 2022, the PUD reported deferred outflows of resources and deferred inflows of resources related to OPEB healthcare from the following sources (in thousands):

	2022	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 104	$ (403)
Changes of assumptions or other inputs	2,001	(2,205)
Total	**$ 2,105**	**$ (2,608)**

There were no deferred outflows and deferred inflows of resources related to OPEB life plan.

Amounts currently reported as deferred outflows of resources and deferred inflows of resources related to other post–employment benefits will be recognized in OPEB credit (expense) as follows (in thousands):

Measurement Period Ending December 31:	
2023	$ (744)
2024	203
2025	40
	$ (501)

POSTEMPLOYMENT DEFINED CONTRIBUTION AND HEALTHCARE PLANS

The PUD offers several defined contribution plans and a healthcare plan to employees.

Employees hired after July 1, 2009, are not eligible for the postemployment defined benefit healthcare plan but are instead eligible for a defined contribution healthcare plan. This plan is also known as the Retirement Health Savings (RHS) Plan. Under this plan, the PUD contributed $55.08 per month into an employee's individual HRA account in January through March 2022. Effective April 2022, the PUD contributed $56.18 each month into the plan. This amount will be adjusted by two percent (2%) annually, on April 1 of each calendar year. These funds are available to the employee for qualified health care costs upon separation from employment from the PUD.

The PUD administers a Non-PERS 401(a) Plan and Trust effective October 1, 1998. Participation in this profit-sharing plan is offered to eligible employees of the PUD as defined in the plan document. The Plan provides certain Employer Contributions to Participants equal to the employer contributions that would have been made to Plan 2 of PERS if Participants in the plan had been eligible to participate in PERS. The PUD recorded as pension expense contributions to the 401(a) Plan of $4 thousand and $17 thousand in 2022 and 2021, respectively. These funds are available to the Participant following a settlement date as defined in the plan document.

The PUD administers an Internal Revenue Code Section 457 deferred compensation program, covering eligible employees as defined in the plan document. Participants may contribute and defer, up to defined limits, a portion of their current year's salary. There is no contribution to this plan from the PUD. The deferred compensation is not available to employees until termination, retirement, death or an unforeseeable emergency. All plan assets are held in trust for the exclusive benefit of participants and their beneficiaries.

The PUD administers a 401(k) Savings Plan effective May 1, 1985. Participation in the Plan is offered to eligible employees of the PUD as defined in the plan document. The Plan is a defined contribution plan, which provides that participants may make voluntary salary deferral contributions, on a pretax basis, up to a maximum amount as indexed for cost–of–living adjustments. In 2022, the contribution limit for employees was $20,500. The catch-up contribution limit for employees aged 50 and over was $6,500. Employee contributions are fully vested. Employer contributions are vested after 3 years of employment. Effective January 2022, the PUD makes matching contributions in an amount equal to 100% of the first 2.5% of a participant's compensation contributed as a salary deferral. The PUD recorded as pension expense for matching contributions to the 401(k) Savings Plan of $3.1 million and $2.3 million in 2022 and 2021, respectively.

Note 7
BPA Power Purchase Agreement

The PUD is a preference customer of the BPA, from which it acquired approximately 83% and 80% of its energy purchases in 2022 and 2021 respectively.

The PUD purchases power from BPA under power supply contracts offered pursuant to the Pacific Northwest Electric Planning and Conservation Act. These contracts provide the PUD with the ability to purchase power in excess of its declared resources on an as-needed basis. The PUD entered into contracts with BPA to purchase approximately 75-85% of its power requirements from the federal agency through 2028.

Energy Northwest Nuclear Projects Nos. 1, 2 and 3

The PUD entered into participation agreements in Energy Northwest's Nuclear Projects Nos. 1, 2 and 3. The PUD, Energy Northwest and BPA have entered into separate Net Billing Agreements with respect to Energy Northwest's Project No. 1, Project No. 2 and 70% ownership share of Project No. 3. The PUD is obligated to purchase from Energy Northwest, and BPA is obligated to purchase from the PUD, a maximum of approximately 20%, 15% and 19%, respectively, of the capacity of Project Nos. 1 and 2 and Energy Northwest's 70% ownership share of Project No. 3. BPA is unconditionally obligated to pay Energy Northwest the PUD's pro rata share of the total annual costs of the projects, including debt service on revenue bonds issued to finance the projects. The effect of these net billing agreements is that the cost of power sold by BPA to all of its customers, including the PUD, includes the cost of these projects.

Notwithstanding the assignment of the PUD's share of the capability of a net billed project to BPA, the PUD remains unconditionally obligated to pay to Energy Northwest its share of the total annual costs of the projects to the extent payment is not received by Energy Northwest from BPA. The PUD has not made payments under this contract.

Note 8
Generation System Projects

The Generation System consists of the PUD's Henry M. Jackson Hydroelectric Project (Jackson Project), four smaller hydroelectric projects and one biofuel generator. In 2022 and 2021, these projects supplied 5% and 6% of the PUD's energy needs.

Henry M. Jackson Hydroelectric Project

The Jackson Project is a multipurpose hydroelectric project with a capacity of 111.8 megawatts.

The project is currently operating under a 45-year license issued by the Federal Energy Regulatory Commission (FERC) that will expire in 2056. The license agreement includes requirements for fish, wildlife, and recreation enhancement in the Jackson Project area. The PUD has also negotiated settlement agreements with the cities of Everett and Sultan, Washington Department of Fish and Wildlife, United States Forest Service, and the Tulalip Tribes that call for funding commitments over the course of the 45-year license.

Small Hydroelectric Projects

The Generation System owns four small hydroelectric projects. Two of these, the Youngs Creek Hydroelectric Project (Youngs Creek) and the Woods Creek Hydroelectric Project (Woods Creek) are located near Sultan, Washington, in Snohomish County. Completed in 2011, Youngs Creek has a capacity of 7.5 megawatts, and its FERC license expires in 2042. Woods Creek was purchased by the PUD in 2008, has a capacity of 650 kilowatts, and was upgraded by the PUD to meet current operating standards. This project is exempt from FERC licensing.

The PUD's other two projects, Calligan Creek Hydroelectric Project (Calligan Creek) and Hancock Creek Hydroelectric Project (Hancock Creek), were completed and began operations in 2018. These 6.0 megawatt run-of-the-river hydroelectric projects are situated near North Bend, Washington, in King County. The 50-year FERC licenses for each project will expire in 2065.

Biofuel Project

In September of 2022 the Generation System started operating a biogas engine generator which has a capacity of 675 kilowatts. The generator is owned and operated by the PUD. The space it occupies is leased from Qualco Energy on a lease agreement that runs through 2028. Qualco Energy blends food and agriculture waste in a digester, and sells the resulting biogas to the PUD to fuel the generator.

Note 9
Related Party Transactions

The Generation System sells power to the Electric System at the cost of power produced including debt service and any other cash transactions. The Generation System sold $28.6 million and $23.7 million of power in 2022 and 2021, respectively, to the Electric System.

The Electric and Generation Systems periodically enter into loan transactions between the systems for various purposes including to defease bonds, to fund energy generation project construction, and to fund energy generation project studies, including the purchase and development of small hydroelectric projects. These loans are assigned terms consistent with the associated asset acquired, and interest rates are set at tax-exempt bond market rates at the time of the loan.

Electric System loans to the Generation System were $30.9 million and $34.5 million at December 31, 2022 and 2021, respectively. The Generation System recorded interest expense on these loans of $1.3 million in 2022 and $1.4 million in 2021.

Note 10
Self-Insurance Fund

The PUD maintains a comprehensive insurance program that includes liability insurance coverage of $50 million in excess of a $2 million self–insured retention per occurrence. This coverage insures against certain losses arising from property damage or bodily injury damage claims filed by third parties against the PUD. On December 31, 2022, the PUD's $2 million self–insured retention was fully funded. Self–insurance funds are included in special funds at market value, with a balance of $9.8 and $10.0 million as of December 31, 2022, and 2021, respectively.

Note 11
Contingencies

The PUD is involved in various claims arising in the normal course of business. The PUD does not believe that the ultimate outcome of these matters will have a material adverse impact on its financial position or results of operations.

The PUD has received federal and state grants for specific purposes that are subject to review and audit by the grantor agencies. Such audits could lead to requests for reimbursements to the grantor agency for expenditures disallowed under terms of the grants. Management believes such disallowances, if any, would be immaterial.

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* Incorporated by reference only

MOSSADAMS

Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Board of Commissioners
Public Utility District No. 1 of Snohomish County
Everett, Washington

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Public Utility District No. 1 of Snohomish County, Washington (the District), which comprise the District's combined and individual statements of net position, and the related combined and individual statements of revenues, expenses and changes in net position and cash flows of the Electric, Generation, and Water Systems, as of and for the year ended December 31, 2022, and the related notes to the financial statements, and have issued our report thereon dated April 4, 2023.

Report on 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) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that were not identified.

Report on 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 its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

Moss Adams LLP

Everett, Washington
April 4, 2023

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Report of Independent Auditors on Compliance for the Major Federal Program; Report on Internal Control Over Compliance; and Report on the Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

The Board of Commissioners
Public Utility District No. 1 of Snohomish County
Everett, Washington

Report on Compliance for the Major Federal Program

Opinion on the Major Federal Program

We have audited Snohomish County Public Utility District No. 1 (the District)'s compliance with the types of compliance requirements identified as subject to audit in the OMB *Compliance Supplement* that could have a direct and material effect on the District's major federal program for the year ended December 31, 2022. The District's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

In our opinion, the District complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2022.

Basis for Opinion on the Major Federal Program

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America (GAAS); the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States *(Government Auditing Standards)*; and the audit requirements of Title 2 U.S. *Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Our responsibilities under those standards and the Uniform Guidance are further described in the Auditor's Responsibilities for the Audit of Compliance section of our report.

We are required to be independent of District and to meet our other ethical responsibilities, in accordance with relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion on compliance for the major federal program. Our audit does not provide a legal determination of the District's compliance with the compliance requirements referred to above.

Responsibilities of Management for Compliance

Management is responsible for compliance with the requirements referred to above and for the design, implementation, and maintenance of effective internal control over compliance with the requirements of laws, statutes, regulations, rules, and provisions of contracts or grant agreements applicable to the District's federal programs.

Auditor's Responsibilities for the Audit of Compliance

Our objectives are to obtain reasonable assurance about whether material noncompliance with the compliance requirements referred to above occurred, whether due to fraud or error, and express an opinion on the District's compliance based on our audit. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS, *Government Auditing Standards*, and the Uniform Guidance will always detect material noncompliance when it exists. The risk of not detecting material noncompliance from fraud is higher than for that resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Noncompliance with the compliance requirements referred to above is considered material, if there is a substantial likelihood that, individually or in the aggregate, it would influence the judgment made by a reasonable user of the report on compliance about the District's compliance with the requirements of the major federal program as a whole.

In performing an audit in accordance with GAAS, *Government Auditing Standards,* and the Uniform Guidance, we

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material noncompliance, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the District's compliance with the compliance requirements referred to above and performing such other procedures as we considered necessary in the circumstances.
- Obtain an understanding of District's internal control over compliance relevant to the audit in order to design audit procedures that are appropriate in the circumstances and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over compliance. Accordingly, no such opinion is expressed.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and any significant deficiencies and material weaknesses in internal control over compliance that we identified during the audit.

Report on Internal Control Over Compliance

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the Auditor’s Responsibilities for the Audit of Compliance section above and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies in internal control over compliance. Given these limitations, during our audit we did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, material weaknesses or significant deficiencies in internal control over compliance may exist that were not identified.

Our audit was not designed for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, no such opinion is expressed.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the financial statements of the District as of and for the year ended December 31, 2022, and have issued our report thereon dated April 4, 2023, which contained an unmodified opinion on those financial statements. Our audit was performed for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

Moss Adams LLP

Everett, Washington
April 4, 2023

Supplementary Information

Public Utility District No. 1 of Snohomish County
Schedule of Expenditures of Federal Awards
Year Ended December 31, 2022

Federal Grantor/Pass Through Grantor/ Program or Cluster Title	ALN Number	Pass Through Entity Identifying Number	Federal Expenditures	Passed-through to Subrecipients
ENVIRONMENTAL PROTECTION AGENCY				
Pass through Washington State Department of Health:				
Capitalization Grants for Drinking Water State Revolving Funds Cluster	66.468	Warm Beach Loan 2016-026	$ 2,245,319	$ -
DEPARTMENT OF HOMELAND SECURITY				
Pass through the State of Washington:				
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	97.036	FEMA 4168-DR-WA	35,760	-
	97.036	FEMA 4249-DR-WA	231,718	-
	97.036	FEMA 4539-DR-WA	43,287	-
	97.036	FEMA 4635-DR-WA	245,672	-
			556,438	-
DEPARTMENT OF THE TREASURY				
Pass through Washington State Department of Commerce				
Covid-19 State and Local Fiscal Recovery Funds	21.027	SLFRP0002	11,190,099	-
US DEPARTMENT OF ENERGY				
Pass through Washington State Department of Commerce				
Solar Deployment Grants	81.041	DE-EE0008296	112,033	-
DEPARTMENT OF COMMERCE				
Pass through Washington State Recreation and Conservation Office:				
Pacific Coast Salmon Recovery Program	11.438	NA20NMF4380250	45,902	-
Total Expenditures of Federal Awards			$ 14,149,791	$ -

See Notes to Schedule of Expenditures of Federal Awards.

Note 1 – Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards (Schedule) presents the expenditures of federal awards of the Snohomish County Public Utility District No. 1 (the District) for the year ended December 31, 2022. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the District, it is not intended to and does not present the net position, changes in net position, or cash flows of the District.

The District's reporting entity is defined in Note 1 of the District's financial statements. All federal awards from federal agencies are included in the Schedule.

Note 2 – Summary of Significant Accounting Policies

The accompanying Schedule is prepared whereby eligible grant expenditures are recorded when reimbursement of the grant expenditures are received from the granting agency. Disaster Grants from the Department of Homeland Security are prepared on the same basis of accounting as the District's financial statements using the accrual basis of accounting, whereby eligible grant expenditures are recorded when incurred (i.e., when goods are received or services provided). Such expenditures are recognized following the cost principles in Uniform Guidance wherein certain types of expenditures are not allowable or limited as to reimbursement. Expenditures reported include any property or equipment acquisitions incurred under federal programs. Pass-through identifying numbers are presented where available.

The amount shown as current year expenditures represent only the federal grant portion of the program costs. Entire program costs, including the District's portion, are more than shown.

The District is not eligible to use an indirect rate on these federal awards, therefore the de minimis indirect cost rate as described in 2 CFR 200.414 is not being utilized.

Note 3 – Drinking Water State Revolving Fund

August 2018, the District entered into two loan agreements with a total of $6,251,709 to fund the projects of the Warm Beach Water Association consolidation. Funding was provided by the Environment Protection Agency, through the Drinking Water State Revolving Fund (DWSRF) programs of the Washington State Department of Health, which acted as the pass-through agency. As of December 31, 2021, the District has submitted costs for draws under the loan 2016-026 totaling $3,532,862 and received reimbursement of $2,665,165 for the year ended December 31, 2021. The District also submitted costs for draws under the loan 2017-2265 totaling $2,245,319 as of December 31, 2022 and received reimbursement for $1,620,148 during the year ended December 31, 2022. A final loan draw of $625,171 was recorded as a receivable at December 31, 2022.

Note 4 – Dept of Treasury Grant to WA DOC for Utility Residential Customer Arrearages

In November 2022, the District entered into a grant agreement with Washington State Department of Commerce to receive funds usable for Utility accounts with Arrearages from March 2020 to December 2021 related to COVID-19, meeting specific conditions. In December 2022, the District received and applied $11,190,099 to qualified Customer Accounts before December 31, 2022.

Section I – Summary of Auditor's Results

Financial Statements

Type of auditor's report issued on whether the financial statements audited were prepared in accordance with GAAP:	Unmodified
Internal control over financial reporting:	
• Material weakness(es) identified?	☐ Yes ☒ No
• Significant deficiency(ies) identified?	☐ Yes ☒ None reported
Noncompliance material to financial statements noted?	☐ Yes ☒ No

Federal Awards

Internal control over major federal programs:	
• Material weakness(es) identified?	☐ Yes ☒ No
• Significant deficiency(ies) identified?	☐ Yes ☒ None reported
Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	☐ Yes ☒ No

Identification of major federal programs and type of auditor's report issued on compliance for major federal programs:

ALN Number	*Name of Federal Program or Cluster*	*Type of Auditor's Report Issued on Compliance for Major Federal Programs*
21.027	Department of Treasury Grant to Washington DOC Covid-19 State and Local Fiscal Recovery Funds	Unmodified

Dollar threshold used to distinguish between type A and type B programs:	$ 750,000
Auditee qualified as low-risk auditee?	☒ Yes ☐ No

Section II – Financial Statement Findings

None reported.

Section III – Federal Award Findings and Questioned Costs

None reported.