# A VISION FOR THE FUTURE

## ANNUAL REPORT 2016

# COMMISSIONERS' REPORT

**As a public utility, we strive to balance the needs of our current customers with the needs of future generations.** While we are focused on ensuring that our utility is postured to meet the evolving demands of customers in the near future, we also need to ensure that our current decisions protect our access to low-cost energy for generations to come. From developing strategies that emphasize smaller, more predictable price increases for our retail customers, to making investments in our operations so we can continue to generate low-cost renewable energy, we must always balance the needs of customers alongside the need for delivering long-term value into the future.

In the past year, we began a 10-year project to renovate the turbines and generators at Priest Rapids Dam. This extensive work replaces and rehabilitates aging equipment that is nearing the end of its life expectancy. The project begins on the heels of similar work at Wanapum Dam. By doing this, our two dams, with their capacity to generate more than 2,000 megawatts of power, will continue generating clean, renewable energy for our region in the decades to come.

As the licensed operator of Wanapum and Priest Rapids dams, which collectively make up the Priest Rapids Project, our obligations go beyond energy production and delivery. We take seriously our responsibility of providing fish passage through our dams, protecting habitat, preserving cultural resources, and facilitating public access to recreation opportunities on the Columbia River. In 2016, we began renovations at the Crescent Bar Recreation Area. The first phase of enhancements includes a new RV campground, new boat launch, public parking facilities and improved river-access locations. When finished, public access to this prime recreation site will be available for all to enjoy.

To accommodate the needs of our growing county, we are also in the process of constructing a combination of eight new and refurbished substations to build a more resilient electric system and preserve our legacy of reliable energy. Our county is experiencing tremendous growth across all spectrums of customer-classes, from single-family homes to large industrial facilities. These eight substations will accommodate and likely attract continued growth. In 2016, we began this infrastructure investment through an innovative design-build program where our staff partnered with expert contractors to rapidly and efficiently complete this work. Through this process, work that would have normally taken several years to finish is now expected to be completed in 2018.

As the utility industry becomes more complex and service-expectations increase from customers, regulators and policymakers, we know that our workforce is our greatest asset in delivering the outcomes our communities expect. Our primary goal is for every employee to return home safely each day and return to work safely the next day. In 2016, the utility took necessary steps to elevate the importance of our safety value through the development of a safety improvement initiative. This effort is focused on empowering our employees to take responsibility for their safety at work and at home. This initiative is designed to drive lasting changes and safety performance outcomes that reflect our vision of excellence.

We are grateful for the opportunity to serve our customers as we respond to the present demands and also make investments that will provide significant benefit for generations to come in the county. We believe it is our duty to honor the legacy of those who came before us, to ensure that we are poised to meet any opportunity and challenge both present and to come.

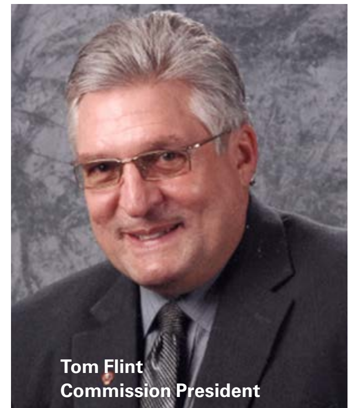
*Tom Flint, President*

*Larry Schaapman, Vice President*

*Terry Brewer, Secretary*

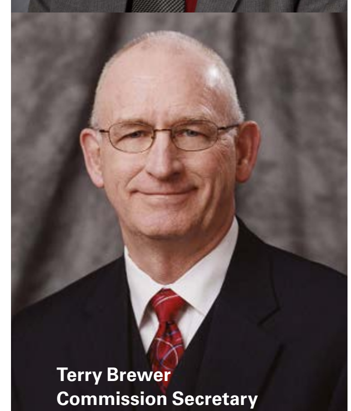
*Bob Bernd, Commissioner*

*Dale Walker, Commissioner*

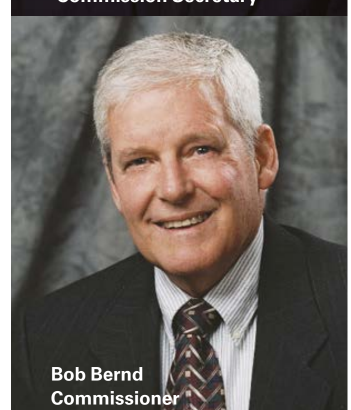


**Tom Flint**
**Commission President**

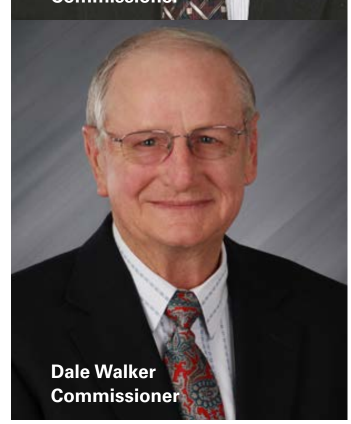
**Larry Schaapman**
**Commission Vice President**



**Terry Brewer**
**Commission Secretary**



**Bob Bernd**
**Commissioner**



**Dale Walker**
**Commissioner**

## MANAGER'S LETTER

**It is no accident that Grant County is, in many ways, the envy of the country at present.** While communities across the United States struggle with flat or reduced growth, Grant County prospers. It is the collective contributions of county residents both past and present that allow our Public Power model to thrive. While we recognize and honor the contributions of the past, our current good fortune is a position we are working to preserve well into the future. This past year we have made progress toward ensuring that we are able to power our county's way of life for decades to come.

Kevin Nordt
General Manager

As our projections into the coming decade reveal a continued growth trajectory for our county, we are committed to ensuring we grow in a way that is focused on preserving long-term value for customers. We are in business to serve every customer, ranging from senior residents living on fixed incomes, small business start-ups, irrigators putting food on tables around the world, and large industrial companies powering the digital space. Quality service, at an affordable price is the essence of Public Power and an element ingrained in the DNA of our company. It is our present commitment and vision for the future.

In mid-2016, I unveiled a new five-year initiative called Vision 2021 that is designed to drive the pursuit of long-term value creation for our customers. This plan touches every employee and results in outcomes that benefit all customers. More on this plan can be found in the pages that follow.

A key aspect of this plan involves taking a hard look at our existing organizational structure and business operations. This examination resulted in developing a new organizational design and reporting structure so we are prepared to meet existing and future customer needs. We now have an organizational structure that better equips us to deliver on key performance and financial commitments going forward. We also unveiled an enterprise-wide business planning process designed to deliver better outcomes across operations, safety, finance and workforce development. Vision 2021 is driven by a desire to look ahead and meet customer needs and performance metrics outlined in our strategic plan. We are fortunate to be in a strong operational and financial position today, but must take proactive actions now to ensure we remain on solid footing for years to come.

The hard work of our employees over this past year can often go ignored when we are doing our job well. While this work may go unnoticed, it's important to recognize that we have once again delivered a service that offers county residents some of the most affordable energy prices in the country. Affordable energy has attracted some of the most successful companies in the US to build and invest in our county. These businesses provide jobs with above-average wages, support small businesses and are contributing local sales and property taxes that help build libraries, schools, police and fire stations, roads and other vital infrastructure.

Through the expertise of our engineering and skilled craft, including linemen, electricians, mechanics and many others, we enjoy a reliable electric system that served residents in some of the warmest and coldest months. In the rare instances when the power goes out, most of our customers don't wait days, they wait an hour or less.

Beyond investments in infrastructure and affordable energy, I am proud of our investments in educational outreach programs for our local young people through electrical safety trainings, energy education at our new Grant PUD Visitors Center, solar car races with county schools, salmon lifecycle education, and cultural resource education at our new Wanapum Heritage Center.

One of our greatest accomplishments over this past year involves an increased emphasis on the safety of our employees. Employees have taken on a challenge to identify ways to deliver our standard of excellence as it relates to our safety value. This past year, our employees built a strong foundation toward improving our safety culture and performance outcomes both on the job and at home. Our end-goal is to operate in a way that meets customer needs but does so in a manner that reflects best-in-class safety standards.

Grant PUD is proud to be an integral part of the growth occurring in our county. My commitment is to advance our PUD in a way that is balanced, measured and focused on delivering long term value into the future.

*Kevin Nordt - General Manager*

# OUR PURPOSE: DELIVERING VALUE TO OUR CUSTOMERS

**Grant County Public Utility District (Grant PUD) was established by local residents over 75 years ago.** Formed by local citizens, we are inherently connected to the communities we serve.

Our customers depend on us to generate and deliver reliable and affordable energy. A basic principle of public power is to provide the same high quality of service to all of our customers regardless of size or geographic location. We are also dedicated to protecting the strong financial health of Grant PUD for the benefit of all customers both today and into the future.

## OUR VISION:

**Excellence in Service and Leadership**

## OUR MISSION:

**To efficiently and reliably generate and deliver energy to our customers**

# VISION 2021

**Wouldn't it be great if you could plan for the expected price of gasoline, groceries or medicine through 2024?**

In 2016, Grant PUD launched a five-year initiative designed to drive long-term value creation for our customers. This plan, called Vision 2021, encompasses a strategy that culminates in hitting key financial targets over the next five years. In line with this vision, a focus for 2016 was to review and refine our existing organizational structure. The goal of this examination was to evaluate which aspects of our structure worked and identify aspects that were impediments to meeting current and future customer expectations.

This examination revealed that modernizing our organizational structure was a foundational first step toward making decisions efficiently and at the right level. The end result of this effort is a streamlined senior leadership structure that includes a general manager and three senior officers overseeing three primary business units. This structure is designed to deliver excellence across customer engagement, operations and finance.

Our customers have been very clear in what they seek: safe, reliable energy at a stable, predictable price as well as exemplary performance in compliance and stewardship. Through the bedrock Public Power principle of local decision-making; our elected board of commissioners acts on behalf of our customers and is directly accountable to them. The commissioners work to preserve the long-term health of the utility, define our mission, ▶

# Key Areas of Focus

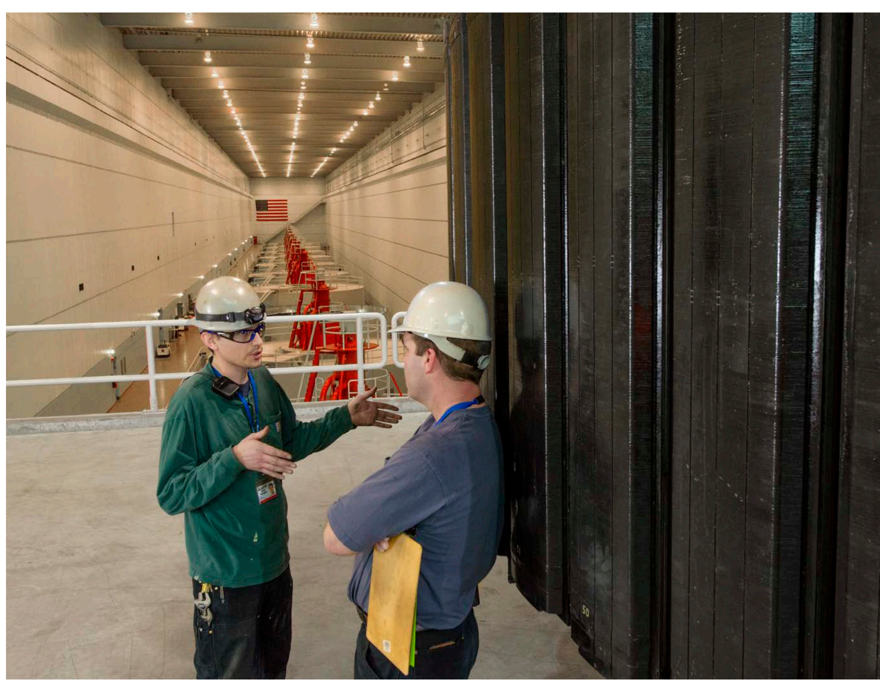

vision, and strategic objectives. Our Strategic Plan is the driving force behind all of our actions outlined in Vision 2021.

We recognize that changes to Grant PUD's structure alone will not lead to better financial and operational outcomes for our customers. In addition to structural changes, the utility is also determined to drive improvement in the following areas:

1) Implement Grant PUD's vision for safety. Our goal is for everyone to go home safe every day.
2) Create a comprehensive wholesale telecom business plan that defines and supports a sustainable broadband network.
3) Establish a formal business-planning process throughout the entire company. Some non-critical projects may need to be modified, placed on hold, or eliminated altogether. This only happens through the input and coordination of front-line employees.

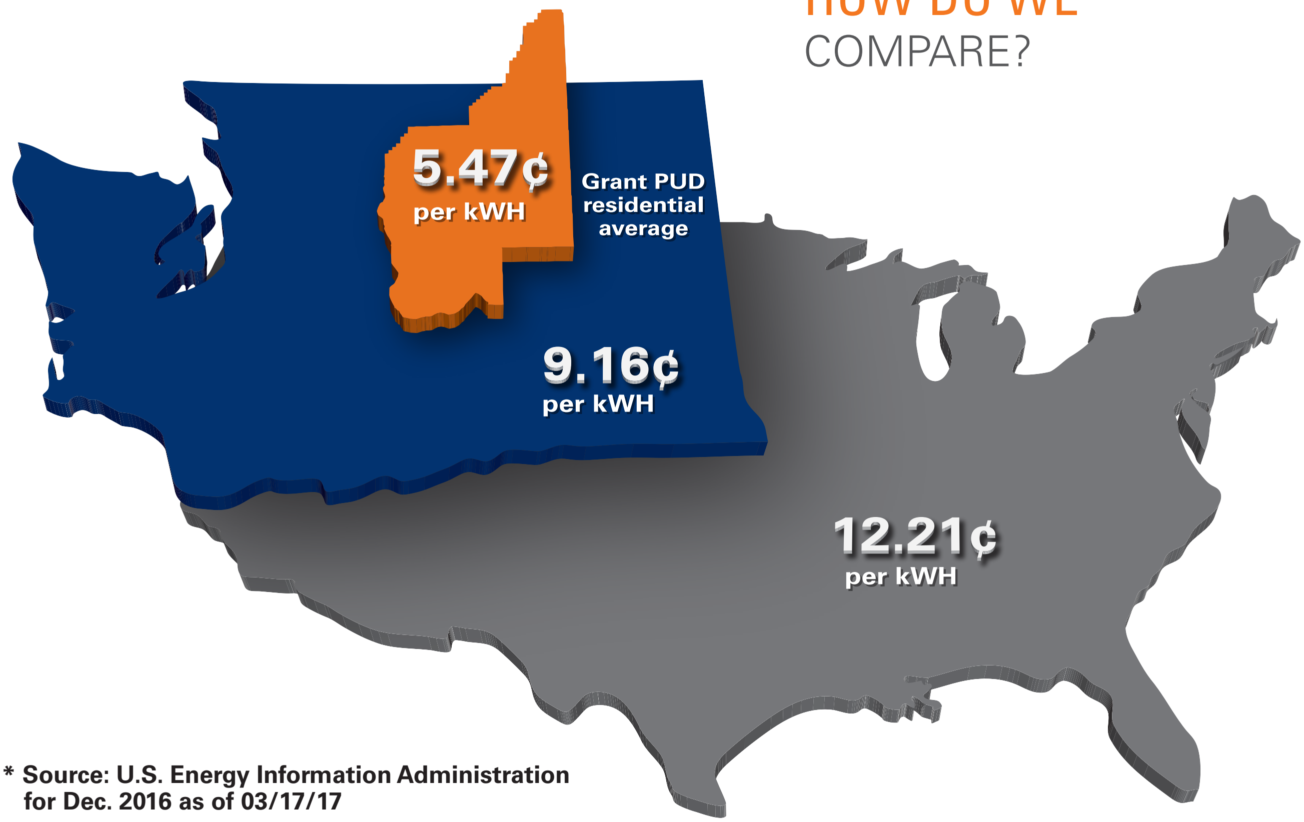
Recognizing that we have some performance gaps relative to achieving key targets does not diminish the fact that our employees have accomplished truly amazing things over the past several years. It is ultimately the blend of employee talent and spirit that will allow us to close the performance gaps within the timeline outlined in Vision 2021.

Our need to drive change is the result of one of the most competitive and dynamic marketplaces we have ever been in before. The rehabilitation of our generating plants and implementing all the licensing requirements has put strong upward pressure on our production costs, which together with downward price pressure in the wholesale markets, has adversely impacted our bottom line. In addition, our assets, compliance requirements, and work processes are more complex than they have ever been. So it is not surprising that we need to evolve and adapt as an organization. We are by no means alone in this. Utilities all over the nation, and especially in this region, are wrestling with these same issues. While difficult, we set our vision on the future and embark on a path of change over the coming years so our customer needs are satisfied.



# DELIVERING: LOW-COST & RELIABLE ENERGY

## HOW DO WE COMPARE?

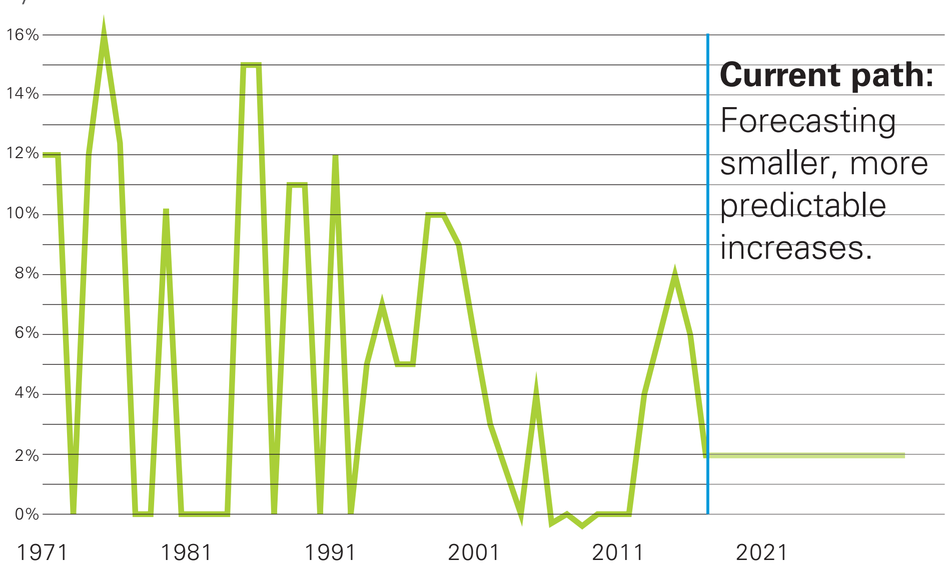



* Source: U.S. Energy Information Administration for Dec. 2016 as of 03/17/17

For several decades we had a reactive rate policy, which resulted in large increases following years with no increase. Our current proactive strategy reflects our customers' preferences for smaller, more predictable price increases phased in over time.

### Historic Price Increases

By all classes 1971 – 2016




## OUR GOAL:

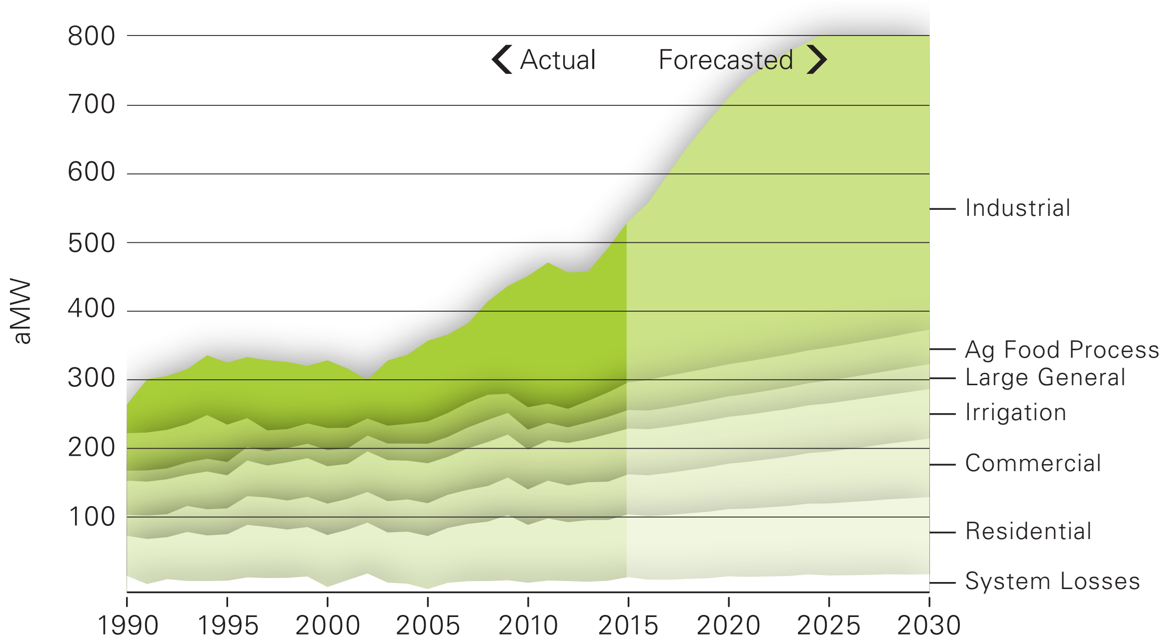
Stable & predictable customer outcomes.

## Load Growth

While growth is happening throughout all of our customer groups, including residential, small commercial, irrigation, food processing and industrial, much of the current growth is courtesy of the large industrial class. Because these large industrial customers pay above our cost to serve their needs, growth in this class has benefited other customer classes in the form of prices that are lower than they would have been absent the growth. The value of this retail margin from large customers provided a benefit of approximately $150 million from 2004 to 2013.

### Grant PUD 2016 Medium Load Forecast

Retail sales by rate class




## Paying for Energy Infrastructure

When a Grant County resident builds a new home or business, he or she pays the upfront cost of connecting the property to our existing electric system infrastructure. The same holds true for commercial and industrial customers who require additional infrastructure to serve their needs. A program known as Contributions In Aid of Construction (CIAC) is founded on the cause-a-cost, bear-a-cost philosophy. Under the CIAC, large customers who need reinforcement to power lines, transmission lines, transformers or substations are required to pay their share of the cost upfront. This program ensures that the financial burden for these upgrades are born by those who will benefit from them. Mechanisms like these protect all customers in other classes. In 2016, we constructed $4.6 million of infrastructure expansions and enhancements that were funded by the CIAC program.

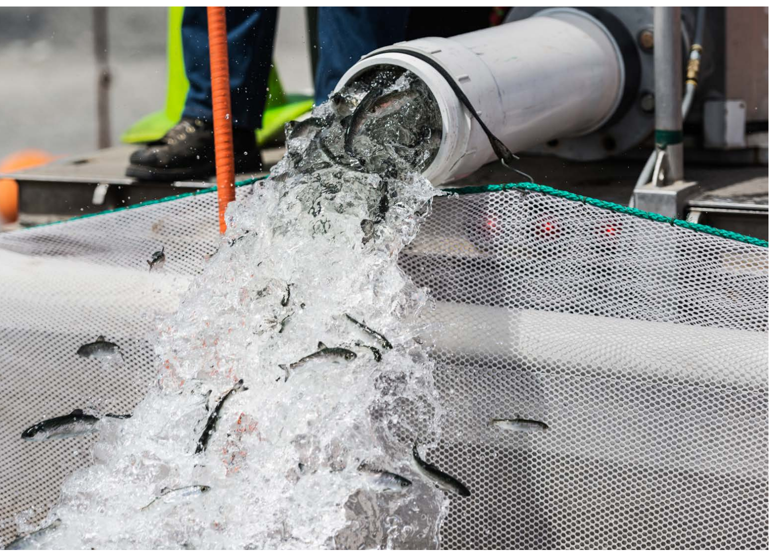
## Balancing Growth

Grant County continues to be viewed as a place synonymous with opportunity. We are taking a proactive approach to managing growth in a way that considers all of our customers. We constantly engage in financial planning to balance the impacts of growth within our customer classes, address the costs of delivering a quality service, and, at the same time, reduce our risk profile. Balancing these details and developing policy that reflects public feedback, enables us to keep our prices low while we improve our financial position.

# DELIVERING VALUE: THROUGH OUR SERVICES

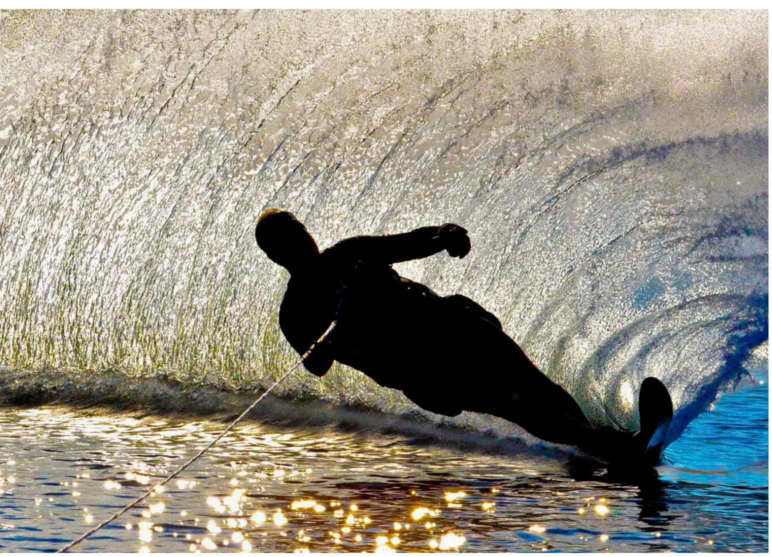

## Hydro Generation

Wanapum and Priest Rapids dams, collectively known as the Priest Rapids Project, are the economic engines that power Grant PUD's ability to provide low-cost, reliable electricity to our customers.  We are investing millions of dollars to modernize these facilities, which are now entering into their sixth decade of service. This work allows our hydro system to continue generating clean, renewable power, providing successful fish passage, helping with river flows and furnishing recreational opportunities.



## Fish Population Preservation

One of our main responsibilities as the operator of the Priest Rapids Project is to protect and enhance native fish populations on the Columbia River. Grant PUD is committed to this responsibility and partners with operators of hatcheries, acclimation facilities, and habitat preservation and restoration projects throughout the Columbia River Basin. We have made significant upgrades at our dams to enhance juvenile fish passage, while at the same time gaining more efficiency in our hydropower operations. We believe that native fish populations are vital to the heritage of our region and we are committed to preserving them. In 2016, we released 10 million juvenile fish into the native habitat.



## Recreation Opportunities

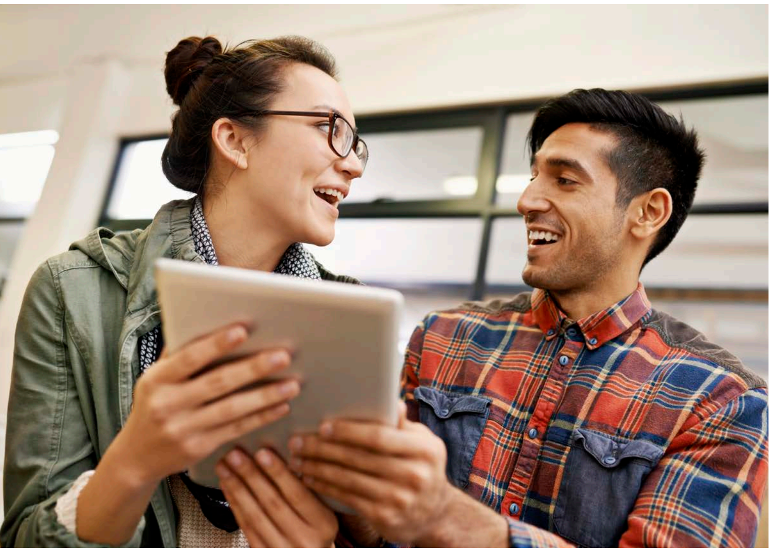
One of the benefits of our regionally-coordinated hydroelectric system is the increased recreation opportunities for people on the Columbia River and shoreline. We provide recreation opportunities and public access to the river and our lands year round. According to a recent study, more than 350,000 people visit Grant PUD's lands annually. We are putting the final touches on a project to enhance 20 recreation sites by 2018. These upgrades allow access and enjoyment for everyone, including those who need ADA accessibility. Along with our investment in these upgrades, we also have staff members dedicated to monitoring and maintaining these locations.

## Education

As a public utility, we have a responsibility to our current and future customers. One of the ways we fulfill this responsibility is through our investment in educational programs. We partner with local, regional and national organizations to empower our communities with the knowledge they need to understand the importance of electrical safety, water safety, habitat protection and energy efficiency.

## Reliable Power

We want to always be there whenever our customers need us. Making sure reliable power is there for our customers happens through extensive planning, scheduling and maintenance. To accommodate the needs of our growing county, we began an innovative project in 2016 to build two new substations and significant upgrades to six existing substations. This work is expected to be complete by 2018 and will ensure that the power keeps flowing to our customers for years to come.



## High Speed Network

Since 2001, Grant PUD has taken on the task of bringing a broadband network to Grant County. After 15 years, our fiber optic service is available to 70 percent of customers, offering speeds up to 1 gigabit per second through participating internet service providers. More and more of our customers rely on this network to connect to their online world. Our high speed network provides Grant County's rural economy with a competitive edge.

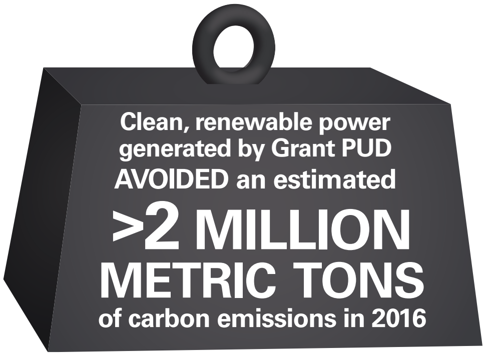
# GENERATING: CLEAN AND RENEWABLE ENERGY


**With our two dams on the Columbia River, as well as smaller hydropower projects and our share of the Nine Canyon Wind Project, we have the capacity to generate more than 2,100 megawatts of clean, renewable energy.**
Every watt of energy we generate is carbon free. Every decision we make as a utility is balanced with our desire to act as good stewards of our resources and environment.

We are investing hundreds of millions of dollars into upgrading our turbines and generators at Wanapum and Priest Rapids dams. This investment maximizes the potential energy flowing through the Columbia River, and provides safer fish passage. We have modified our dams to create new fish bypass facilities for migrating juvenile salmonids. These facilities have the added benefit of reducing the amount of water we must ▶

pass through the spillway, which can have a negative impact to fish.

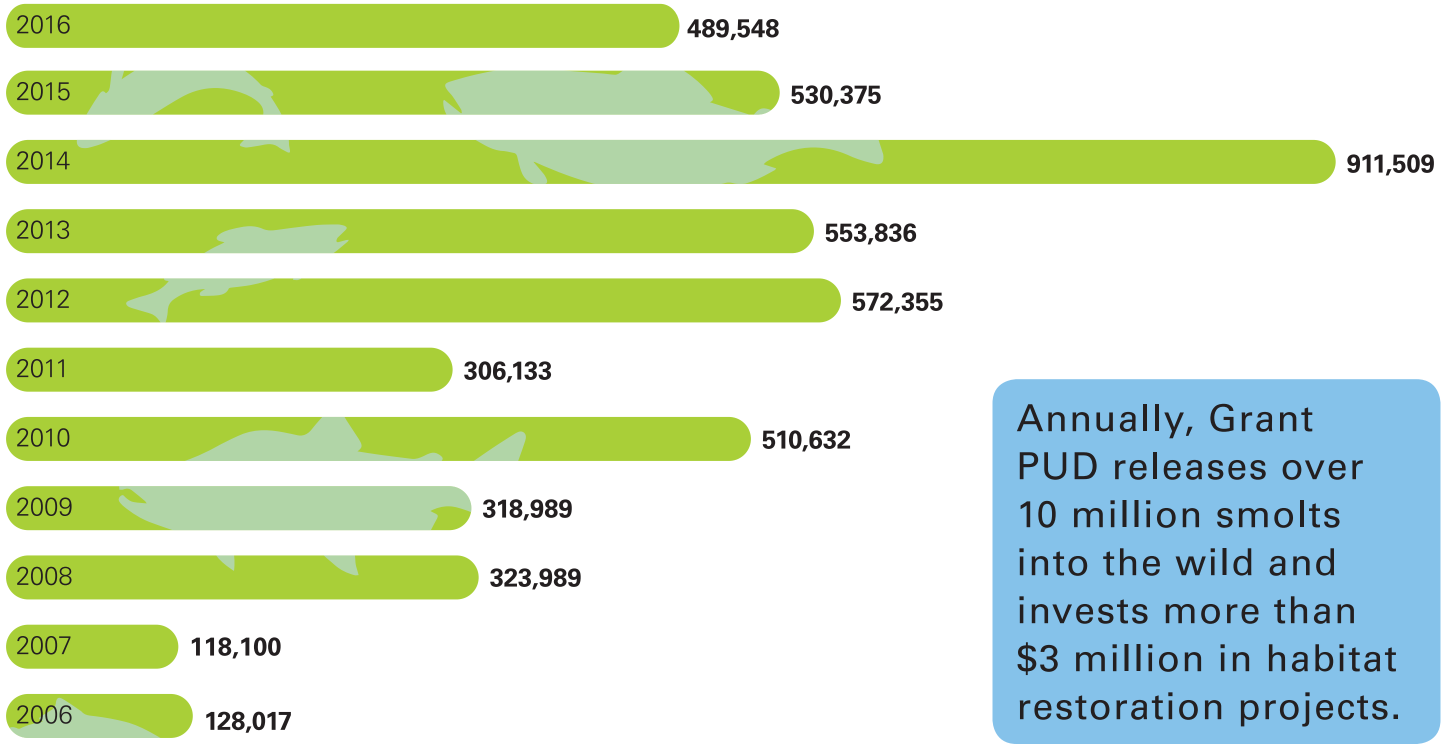
Our hydropower facilities also provide a fast-ramping generation resource that can effectively integrate with variable windpower generation in the region as we coordinate to meet the power demands of customers. With large coal-fired resources in the Northwest being taken off line, our hydropower facilities will become even more important to ensure that there will always be power available to meet the growing demands of our region. Our long-term vision is to have carbon-free generating facilities remain an important and reliable resource for decades to come.



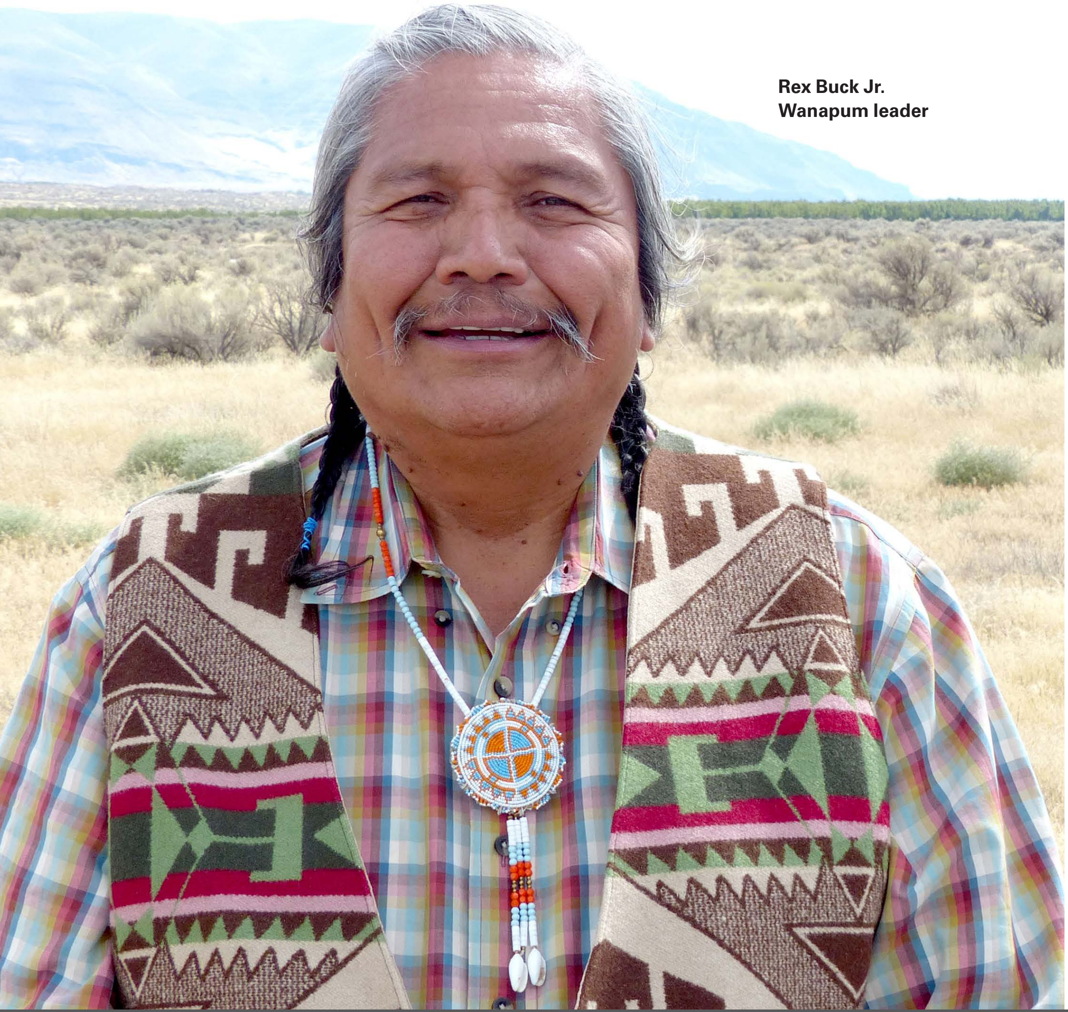

# BOLSTERING: MIGRATING FISH POPULATIONS

**Grant PUD is one of the greatest contributors to the enhancement and protection of anadromous fish, resident fish and habitat conservation in the region.** While generating and delivering energy is our mission, it cannot be accomplished without regard for our surroundings and being a leader in environmental stewardship. The decisions we make, from operating our hydroelectric facilities and hatchery projects to improve juvenile salmonid survival, as well as supporting conservation and habitat restoration programs, are geared toward protecting our environment. These enhancement programs cover a broad area of the Columbia River Basin; from Penticton, British Columbia downstream to the Hanford Reach. Grant PUD releases over 10 million smolts into the wild and invests more than $3 million in habitat restoration projects annually. Favorable ocean conditions, coupled with these collective efforts contribute to the strong and in some cases, record-breaking, returns experienced in recent years.

**Fish Counts at Priest Rapids Dam**
Chinook, Sockeye, Coho, and Steelhead




Annually, Grant PUD releases over 10 million smolts into the wild and invests more than $3 million in habitat restoration projects.

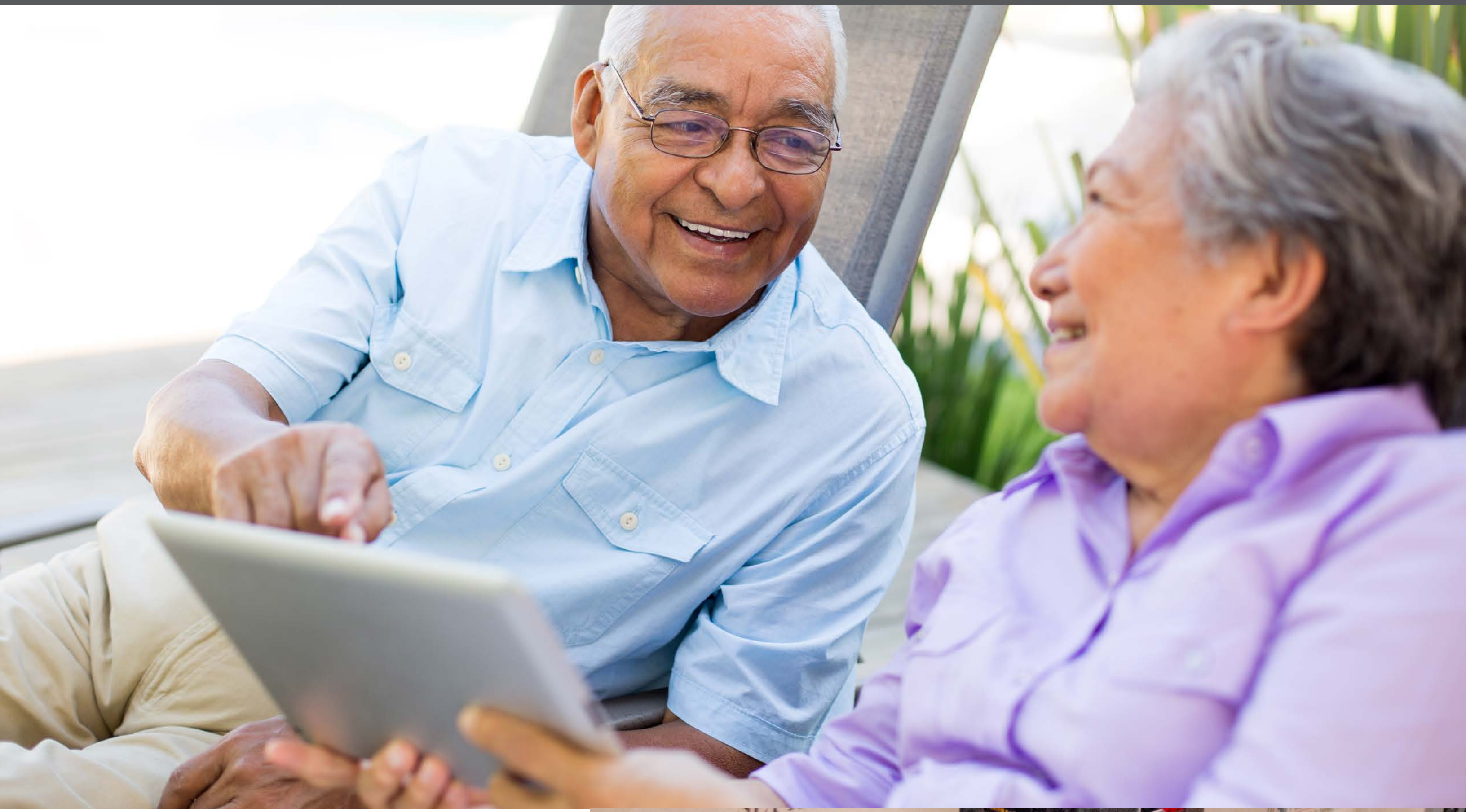


Rex Buck Jr.
Wanapum leader

**For more than 60 years, Grant PUD and the Wanapum, which have made their home at Priest Rapids for time immemorial, have worked together to protect, preserve and perpetuate the natural and cultural resources of the Priest Rapids Project.** Brought together in the 1950s with the federal licensing of Priest Rapids and Wanapum dams, the two groups committed to a long-lasting relationship built on mutual trust and respect. As construction of the dams began, the Wanapum stood in support of the utility. In return, the Wanapum maintain their traditional culture and religious lifestyles at their ancestral home. Grant PUD has shown its commitment to preserving the Wanapum heritage by actively monitoring significant cultural heritage sites, protecting the Priest Rapids Project shoreline and partnering with the Wanapum in the construction of the new Wanapum Heritage Center, which opened its doors in 2015.

# PRESERVING: THE WANAPUM HERITAGE

# CONNECTING: WITH OUR HIGH SPEED NETWORK



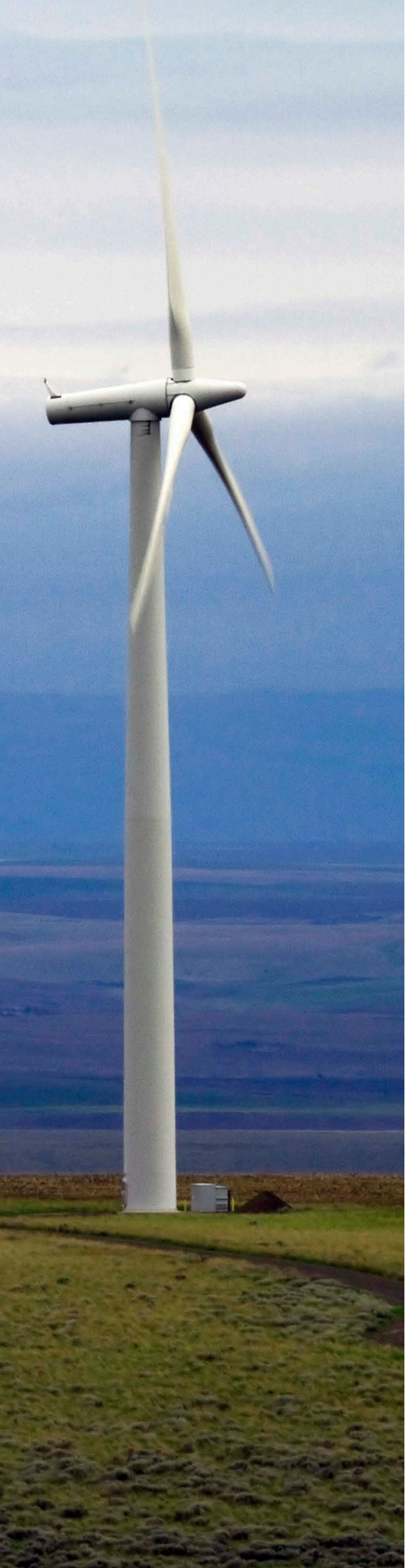
**For 15 years, Grant PUD has worked to bring a wholesale high speed communications network to Grant County.** We have extended a fiber-optic network to about 70 percent of the population, providing one of the fastest communication networks in the world. This network has improved the quality of life for our customers and enhanced education and business opportunities in Grant County. A high speed internet connection has become a priority for many of our customers in Grant County and our network provides the fastest connection possible in Grant County with fiber speeds up to 1 gigabit per second. In the past three years, 4,904 new subscribers have signed up for our fiber optic service offered through our participating retail internet service providers. As we look toward the future, we plan to continue operating our High Speed Network as part of our strategic plan.


**We have operated our High Speed Network for 15 years to provide broadband service to Grant County customers through one of our participating retail Internet Service Providers.**

## 13,000+ CUSTOMERS SUBSCRIBE TO OUR WHOLESALE NETWORK


# CONTRIBUTING: TO OUR COMMUNITY

**For more than 75 years, Grant PUD has served the energy needs of rural Grant County.** Like other public power utilities in the U.S., it's our connection with local communities that remains unchanged. We are consumers of the product that we deliver. Our families and neighbors are directly impacted by our work. This drives our effort to keep energy affordable and reliable.  Certain aspects of our work can't be measured in a bottom-line number on a financial statement. Some of our most significant accomplishments occur as we invest in community education with local children about electrical and water safety. Beyond education, we also provide incentive programs to help our customers become more energy efficient and save money and have developed a reduced-rate program for both seniors and disabled residents with low incomes. We are proud that our customers can see our employees using their free time to actively engage in programs and causes that contribute to the health, welfare and improvement of our community.

## Power Production System Statistics

### Priest Rapid Dam

| | |
|---|---|
| Generation Units | 10 |
| Rated Capacity | 956,000 kilowatts |
| Length | 10,103 ft. concrete/earthfill |
| Rated Head | 78 ft. |
| Construction Started | July 1956 |
| First Power Generation | 1959 |

### Wanapum Dam

| | |
|---|---|
| Generation Units | 10 |
| Rated Capacity | 1,116,800 kilowatts |
| Length | 8,637 ft. concrete/earthfill |
| Rated Head | 80 feet |
| Construction Started | July 1959 |
| First Power Generation | 1963 |

### Nine Canyon Wind Project

| | |
|---|---|
| 12.54% of Project – Peak Capacity | 12,000 kilowatts |
| First Power Generation | September 2003 |

### Quincy Chute Hydroelectric Project

| | |
|---|---|
| Rated Capacity | 9,400 kilowatts |
| First Power Generation | October 1985 |

### Potholes East Canal Headworks Project

| | |
|---|---|
| Rated Capacity | 6,500 kilowatts |
| First Power Generation | September 1990 |

## Electric System Statistics

**as of December 31, 2016**

| | |
|---|---|
| Overhead Distribution Lines | 2,779 miles |
| Underground Distribution Lines | 1,057 miles |
| Overhead Transformers | 24,215 |
| Padmount Transformers | 9,380 |
| 115kV Transmission Lines | 264 miles |
| 230kV Transmission Lines | 199 miles |

### Substations:

| | |
|---|---|
| Distribution | 45 |
| Transmission | 5 |
| Transmission/Distribution | 3 |

## Active Meters

**as of December 31, 2016**

| | |
|---|---|
| Residential | 37,056 |
| Commercial | 3,990 |
| Irrigation | 5,129 |
| Large Commercial | 113 |
| Industrial | 91 |
| Street Light and Other | 113 |
| TOTAL | 46,492 |

## High Speed Network

**as of December 31, 2016**

| | |
|---|---|
| Number of customers with fiber-optic availability | 29,429 |
| Number of customers using fiber-optic service | 13,188 |
| Number of customers with wireless network availability | 2,829 |
| Number of customers using wireless service | 211 |

## CONTACT INFORMATION

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**E-mail:** publicaffairs@gcpud.org

**Website:** grantpud.org

**Mailing address:** PO Box 878, Ephrata WA 98823

# Public Utility District No. 2 of Grant County, Washington
# Financial Statements
# December 31, 2016 and 2015

# *Table of contents*

# Report of Independent Auditors

To the Board of Commissioners of
Public Utility District No. 2 of
Grant County, Washington

We have audited the accompanying financial statements of Public Utility District No. 2 of Grant County, Washington (the "District"), which comprise the statements of net position as of December 31, 2016 and December 31, 2015, and the related statements of revenues and expenses and changes in net position, and of cash flows for the years then ended and the related notes to the financial statements.

### *Management's Responsibility for the Financial Statements*

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

### *Auditors' Responsibility*

Our responsibility is to express an opinion on the financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the District's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Public Utility District No. 2 of Grant County, Washington as of December 31, 2016 and December 31 2015, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Emphasis of a Matter***

As discussed in Notes 1 and 2 to the financial statements, the District adopted the provisions of Governmental Accounting Standards Board Statement No. 72*, Fair Value Measurement and Application*, in 2016 and changed the manner in which they present certain fair value hierarchy disclosures related to investments. Our opinion is not modified with respect to this matter.

***Other Matter***

*Required Supplementary Information*

The accompanying management's discussion and analysis on pages 3 through 12 and the required supplementary information, Schedule of the District's Proportionate Share of the Net Pension Liability, Schedule of the District's Contributions and Schedule of Funding Progress for Postretirement Health Benefits Program on page 60 through 62, are required by accounting principles generally accepted in the United States of America to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our 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.

*Other Information*

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The Supplemental Disclosures of Telecommunication Activities in Note 11 are presented for purposes of additional analysis and are not a required part of the basic financial statements. The 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. The information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Supplemental Disclosures of Telecommunication Activities is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

PricewaterhouseCoopers LLP

April 28, 2017

As of December 31, 2016, Public Utility District No. 2 of Grant County, Washington (the "District") comprises two operating systems: the Electric System and the Priest Rapids Project which consists of the Priest Rapids Hydroelectric Production Development ("Priest Rapids") and the Wanapum Development ("Wanapum"). The Priest Rapids Project is operated under Federal Energy Regulatory Commission ("FERC") License, Project No. 2114.

Presented below is a discussion and analysis of the financial activities for the years ended December 31, 2016, 2015, and 2014. Please read it in conjunction with the financial statements, which follow this section.

**FINANCIAL HIGHLIGHTS**

- The District produced a positive change in net financial position of \$82.2 million, \$73.4 million, and \$53.5 million during 2016, 2015, and 2014 respectively. Despite the regional challenges of low wholesale power prices, the District was able to add to the financial well-being of the utility. Two key components to this success are the slice contracts and pooling agreement of the Electric System to mitigate the effect of the fluctuation in wholesale power prices and water variability for generation (see "*Slice and Pooling Agreements*").

- As of March 2015, the reservoir behind Wanapum Dam was restored to normal operating level. The reservoir had been lowered due to a fracture that was discovered on the upstream side of Wanapum Dam's Spillway in February of 2014. The District, in coordination with FERC and other stakeholders, spent the remainder of 2014 and early 2015 resolving the fracture and the operational challenges it presented. In July of 2016, the District filed a proof of loss under its general liability insurance policy and claimed \$13.2 million after the deductible. Details of the fracture and the course of action the District followed are discussed in Note 12 to the financial statements.

- In September of 2015, the rating agencies of Moody's, Standard & Poor's, and Fitch all reaffirmed their ratings of all Electric System and Priest Rapids Project bonds of Aa3/stable, AA/stable, and AA/stable, respectively. These ratings have been in effect from Moody's, Standard & Poor's, and Fitch since 2010, 2013, and 2005, respectively. The rationale for the ratings included strong operations, strong liquidity, equity funding of capital projects, strong availability, low production costs, low-cost power supply, and strong financial and risk management practices. These high grade credit ratings allow the District to receive competitive interest rates in the bond market and help keep the costs down for District ratepayers and power purchasers.

| Sortable Table Key | Moody's | Fitch | S&P |
|---|---|---|---|
| Highest grade credit | Aaa | AAA | AAA |
| Very high grade credit | Aa1, Aa2, Aa3 | AA+, AA, AA- | AA+, AA, AA- |
| High grade credit | A1, A2, A3 | A+, A, A- | A+, A, A- |
| Good credit grade | Baa1, Baa2, Baa3, Baa4 | BBB+, BBB, BBB- | BBB+, BBB, BBB- |
| Speculative grade credit | Ba1, Ba2, Ba3 | BB+, BB, BB- | BB+, BB, BB- |
| Very speculative credit | B1, B2, B3 | B+, B, B- | B+, B, B- |
| Substantial risks - In default | Caa1, Caa2, Caa3, Ca | CCC, CC, C, RD, D | CCC+, CCC, CCC-, CC, C, D |

(Source: Wall Street Journal)

- In April of 2016, the District issued $50 million of revenue bonds to finance improvements to the Electric System through a direct placement bond held with Bank of America, N.A. In October of 2015, the District issued $90.7 million of revenue and refunding bonds and $90 million in Clean Renewable Energy Bonds, at a net premium of $10.7 million, associated with the Priest Rapids Project. The refunding of $97 million resulted in a net present value savings of $11.1 million. The $90 million in Clean Renewable Energy Bonds will benefit rate payers because of the Federal rebate of up to 70% on interest payments. These rebates are estimated to save net of sequestration $65 million (nominal) over the 25 year term of the bonds.

- The Commission continued its implementation of small, incremental rate increases. In January of 2015, 2016, and April of 2017, the Commission implemented 2.0% average annual rate increases to retail customers. The Commission-adopted budget and forecast has future overall annual rate increases of 2.0% for the foreseeable future. The largest driver of these rate increases is the rising cost to produce power at the Priest Rapids Project. Cost increases are related to the replacement of turbines and generators at the two dams as well as obligations to build parks, construct and operate fish hatcheries, and protect cultural resources as required in the District's federal license. Despite the production costs increases, the Priest Rapids Project remains among the lowest cost generation plants in the United States.

**Electric System Significant Capital Projects:**

- The District began construction work in late 2012 to build a 35.3 mile 230 kV transmission line that spans from the Rocky Ford Substation to the Columbia Substation. This project was completed on schedule and entered service early in 2014 at a cost of $46.2 million. The benefits include significant reduction of transmission costs, an improved ability to deliver power from the District's hydroelectric projects to customers, improved transmission system reliability, and allowing the District to better serve load growth in the central county area.

**The Priest Rapids Project Significant Capital Projects:**

- In 2008, the District determined the final scope and design of a long-term capital improvement project for the Wanapum facilities. A contract was awarded January 5, 2009, to Alstom Hydro US, Inc. (currently doing business as Alstom Power, Inc.) for approximately $150 million to upgrade all ten generators at Wanapum Dam. The on-site construction began in June of 2010 and is scheduled through April of 2020. The existing generators are currently rated at 109.25 megavolt-amperes ("MVA"). The new upgraded generators have a nameplate rating of 128.6 MVA, an increase of 17.7%. As of July 2016, seven of the ten generators have been replaced. The schedule is to replace one generator per year. As of December 31, 2016, the cost of the remaining Wanapum generators to be replaced is estimated at $28.6 million.

- In addition to the Wanapum turbine and generator replacement project, the District has completed most of the design and engineering work on turbine life extension/replacement and generator rewinds for the Priest Rapids Development. Turbine modeling and hydraulic design has been completed and a contract to supply turbines was awarded to Voith Hydro, Inc. in June of 2014 in the amount of $61.6 million. Generator rehabilitation was awarded to Alstom Power, Inc. in June of 2015 in the amount of $87.9 million. Governor replacement was awarded to L&S Electric, Inc. in December of 2014 in the amount of $1.7 million. The first unit upgrade at the Priest Rapids Development began in August of 2016 with a scheduled return to service in November of 2017.

- As part of the Federal Energy Regulatory Commission (FERC) license to operate the Priest Rapids Project, the District is required to make improvements to the Crescent Bar Recreation Area to enhance public access and recreation opportunities. These improvements, which include construction of a new campground, marina, two boat launches, parking area, walking trail, and day use areas, are currently underway and are due to be completed in the spring of 2018. The total cost to the District is estimated at $30 million.

**Slice and Pooling Agreements**

In an effort to increase net revenue stability by improving the predictability of wholesale revenues, the District entered into agreements for the Electric System's 63.3% physical share from the Priest Rapids Project (PRP) to Iberdrola Renewables, Inc. (Iberdrola) and Shell Energy North America (U.S.), L.P. (SENA). The agreements are summarized below.

- **Slice Agreements**: The District has entered into various "slice" sales from its retained 63.3% share. The agreements sell the capacity and inflows (potential) to buyers. The buyer assumes the risk of low precipitation years; the District obtains a stable revenue from the sale. In January of 2015, the District entered into an agreement with Iberdrola for a 10% slice of PRP from July 1, 2015, to June 30, 2018. The SENA agreement for 10% of PRP output was effective July 1, 2013, and terminated June 30, 2016. These agreements are paid in equal monthly installments over the lives of the agreements. The District regularly monitors its exposure with Iberdrola and SENA and retains the right to call for additional assurances at any time. The District has the right to curtail delivery in the event of nonpayment.

- **Pooling Agreement:** The District entered into an Agreement for Pooling of Priest Rapids Project Physical Output (the "Pooling Agreement") with SENA in September 2015. Under the Pooling Agreement, the District provides SENA with a portion of the District's share of the capacity in the Priest Rapids Project, and SENA provides to the District firm power sufficient to meet the Electric System's retail load forecast, adjusted for the portion of Electric System load that is expected to be met with other District resources. In addition, SENA provides certain scheduling services for the District, including managing power schedules, and the District provides certain flexibility to SENA within the District's balancing area authority. The term of the Pooling Agreement expires September 29, 2020.

  The Pooling Agreement provides for the delivery by the District to SENA of 43.3% of the capacity and associated energy of the Priest Rapids Project through June 30, 2016, and 53.3% of the capacity and associated energy from July 1, 2016, through September 29, 2020. The Pooling Agreement greatly reduces the effect of variable water conditions at the Priest Rapids Project on revenues associated with the District's wholesale sales and purchases. Under the Pooling Agreement, SENA has rights to the actual output of a portion of the Priest Rapids Project, which will vary with water conditions, and will provide firm power to meet the District's load forecast regardless of the actual output of the Priest Rapids Project. Over the life of the agreement, the majority of these values will be offsetting and exchanged without cash payment; there will, however, be monthly payments owed by either SENA or the District due to the seasonal differences between capacity and energy amounts and loads. In addition, certain nonhydrological performance metrics were assumed at the beginning of the contract and monthly differences in these metrics will be trued up and payment made by either SENA or the District. Upon entering the agreement, the District does not expect that there will be any significant monthly true-up payments. The amount of monthly payments over the term could vary based upon actual performance versus the estimates at the time the Pooling Agreement was executed.

## PRIEST RAPIDS PROJECT

The Priest Rapids Project consists of the Priest Rapids Dam and the Wanapum Dam.

Priest Rapids consists of a dam and hydroelectric generating station having a nameplate rating of 956,000 kilowatts ("kW"). Priest Rapids is located on the Columbia River in Grant and Yakima Counties about 150 air miles northeast of the City of Portland, 130 air miles southeast of the City of Seattle, and 18 miles downstream of Wanapum.

Wanapum consists of a dam and hydroelectric generating station having a nameplate rating of 1,116,800 kW. Wanapum is located on the Columbia River in Grant and Kittitas Counties about 160 air miles northeast of the City of Portland, 129 air miles southeast of the City of Seattle, and 18 miles upstream of Priest Rapids.

During the year ended December 31, 2016, the Priest Rapids Project provided 9,193,102 net megawatt hours ("MWh") of electric energy at an average cost of $16.14 per MWh. During the year ended December 31, 2015, the Priest Rapids Project provided 8,677,766 net MWh of electric energy at an average cost of $18.04 per MWh. During the year ended December 31, 2014, the Priest Rapids Project provided 7,755,280 net MWh of electric energy at an average cost of $21.61 per MWh.

The timing of the runoff and spill requirements factor into the water available for generation from year to year. Runoff was 98%, 96%, and 103% of average for 2016, 2015, and 2014, respectively. The return of Wanapum to full operation for the majority of 2015 and all of 2016 combined with the decrease in extraordinary expenses and receipt of insurance proceeds associated with the fracture resulted in a 25% decrease in cost per MWh from 2014 to 2016.

## OVERVIEW OF DISTRICT'S FINANCIAL STATEMENTS

This annual financial report consists of a series of financial statements and reflects the self-supporting, proprietary activities of the District funded primarily by the sale of electrical power. The District reports the business-type activities in a manner similar to private business enterprises. The District's financial statements presented in this report consist of the Statements of Net Position, Statements of Revenues and Expenses and Changes in Net Position, Statements of Cash Flows, and the Notes to the Financial Statements.

The Statements of Net Position include all of the District's assets, liabilities, deferred outflows and inflows, and net position and provide information about the nature and amounts of investments in assets and the obligations of the District.

All of the revenues and expenses of the District are accounted for in the Statements of Revenues and Expenses and Changes in Net Position. These statements measure the success of the District's operations over the year and can be used to determine whether the District has successfully recovered all of its costs through rates and other charges.

The primary purpose of the Statements of Cash Flows is to provide information about the District's cash receipts and cash disbursements during the year. These statements report cash receipts, cash payments, and net changes in cash resulting from operating, financing, and investing activities.

The Notes to the Financial Statements provide additional information that is essential for a full understanding of the information provided in the three statements described above.

**CONDENSED COMPARATIVE FINANCIAL INFORMATION**
**(AMOUNTS IN THOUSANDS)**

| Statements of Net Position | 2016 | 2015 | 2014 |
|---|---|---|---|
| **Assets** | | | |
| Current | $ 222,395 | $ 187,141 | $ 185,986 |
| Net utility plant | 1,953,628 | 1,881,265 | 1,804,349 |
| Noncurrent | 410,306 | 402,218 | 374,270 |
| Total assets | 2,586,329 | 2,470,624 | 2,364,605 |
| Deferred outflows of resources | 13,795 | 11,522 | 10,313 |
| Total assets and deferred outflows of resources | $ 2,600,124 | $ 2,482,146 | $ 2,374,918 |
| **Liabilities** | | | |
| Current | $ 151,088 | $ 128,437 | $ 146,246 |
| Noncurrent | 1,450,355 | 1,430,341 | 1,367,732 |
| Total liabilities | 1,601,443 | 1,558,778 | 1,513,978 |
| Deferred inflows of resources - pensions | 926 | 7,837 | 18,796 |
| Total liabilities and deferred inflows of resources | 1,602,369 | 1,566,615 | 1,532,774 |
| Net position | | | |
| Net Investment in capital assets | 638,520 | 613,865 | 578,286 |
| Restricted | 160,550 | 146,705 | 134,619 |
| Unrestricted | 198,685 | 154,961 | 129,239 |
| Total net position | 997,755 | 915,531 | 842,144 |
| Total liabilities, deferred inflows of resources and net position | $ 2,600,124 | $ 2,482,146 | $ 2,374,918 |

**CONDENSED COMPARATIVE FINANCIAL INFORMATION**
**(AMOUNTS IN THOUSANDS)**

| Revenues and Expenses and Changes in Net Position | 2016 | 2015 | 2014 |
|---|---|---|---|
| Operating revenues | $ 286,316 | $ 313,169 | $ 308,665 |
| Operating expenses | 187,574 | 217,077 | 227,003 |
| Net operating income | 98,742 | 96,092 | 81,662 |
| Other revenues (expenses) | (31,017) | (31,568) | (29,660) |
| Contributions in aid of construction | 4,603 | 13,222 | 22,767 |
| Extraordinary loss - Wanapum fracture | 9,896 | (4,359) | (21,269) |
| Change in net position | $ 82,224 | $ 73,387 | $ 53,500 |
| Total net position - beginning of year | $ 915,531 | $ 842,144 | $ 849,965 |
| Cumulative effect of change in accounting principle | - | - | (61,321) |
| Total net position - end of year | $ 997,755 | $ 915,531 | $ 842,144 |

## FINANCIAL ANALYSIS

The following discussion provides comparative financial information for the years ended December 31, 2016, 2015, and 2014.

## ASSETS

Total assets have increased from 2014 to 2015 by 4% and 5% from 2015 to 2016. This mirrors the increases in Net utility plant for the same periods and is driven by the continued investments in the turbines and generators at Wanapum, and other capital improvements in both systems. These investments align with the District's Strategic Plan objectives, which include delivering long term value and reliability to customers.

In 2014, the District recognized its share of the initial pension related deferred outflows of resources of $2.7 million due to the implementation of GASB 68. This balance included contributions to PERS subsequent to the June 30, 2014 measurement date of the net pension liability. Deferred outflows of resources related to pensions increased $5.7 million from 2014 to 2016 due to the District recording its proportionate share of the increase in collective deferred outflows for the PERS plans as provided by the Department of Retirement Systems. This increase in deferred outflows of resources has been partially off-set by the continued amortization of losses on refunding of debt in the amount of $2.2 million from 2014 to 2016.

## LIABILITIES

The District had approximately $1.3 billion, $1.3 billion, and $1.25 billion in bonded debt for the years ended December 31, 2016, 2015, and 2014, respectively. In April of 2016, the District issued $50 million of revenue bonds to finance improvements to the Electric System through a direct placement bond held with Bank of America, N.A. In October of 2015, the District issued $90.7 million of revenue and refunding bonds at a net premium of $10.7 million and $90 million in Clean Renewable Energy Bonds, associated with the Priest Rapids Project to refund certain bonds previously issued, to finance improvements at the Priest Rapids Project, to pay issuance costs, and to fund a debt service reserve. The refunding of $97 million resulted in a net present value savings of $11.1 million. The Clean Renewable Energy Bonds have an authorized 70% refund from the Federal Government on interest payments made. In October of 2014, the District issued bonds to finance capital improvements for the Priest Rapids Project. The total par value of the bond offering was $204.2 million and $119.8 million of prior bond issues were refunded. The 2014 bonds were issued at fixed interest rates at a net original issue premium of $23.8 million. In November of 2014, the District issued $50 million in Electric System revenue bonds to finance capital improvements in the Electric System. The 2014 Electric System bonds are Adjusted SIFMA Index Floating Rate Bonds (32 basis points plus SIFMA Index) with a Par Call Date of June 1, 2017.

The implementation of GASB 68 required the District to recognize its share of the unfunded liability of the Public Employees' Retirement System (PERS). 2014 Noncurrent liabilities reflect the initial implementation of GASB 68 and the District's $43 million share of the unfunded liability. In 2015 and 2016, the District's share of the PERS liability increased by $9.5 million and $8.2 million, respectively, due to the changes in the actuarial valuation of the PERS collective net pension liability.

GASB 68 also required the District to recognize deferred inflows of resources related to the District's contributions to PERS. In 2014, the District recognized its share of the initial deferred inflows of resources of $18.7 million. Deferred inflows of resources decreased $17.8 million from 2014 to 2016 due to the District recording its proportionate share of the decrease in collective deferred inflows for the PERS plans as provided by the Department of Retirement Systems.

## NET POSITION

Net position increased by $82.2 million, increased by $73.4 million, and decreased by $7.8 million in 2016, 2015, and 2014, respectively. During 2014, the District was able to make $53.5 million positive contributions to Net position despite the loss of generation due to the Wanapum fracture repairs and related reservoir drawdown, largely due to the fact that 35% of the Electric System's share of the Priest Rapids project was sold at a fixed cost regardless of output, also supported by a $10.8 million increase in Contributions in Aid of Construction over the prior year. Because of the change in accounting principles related to the implementation of GASB 68, the change in Net position showed a net decrease of $7.8 million in 2014. Results in 2015 and 2016 benefited from reduced market purchases, return of normal operations of the Wanapum Dam, and the effect on net wholesale revenues of the slice and pooling agreements mentioned previously.

## STATEMENT OF REVENUES AND EXPENSES

Sales to power purchasers at cost are directly tied to power costs as defined in the long-term power sales contracts (operating expenses – noncash items + debt service – interest earnings). Additional expenses related to compliance with the license and other fish and operational costs have added to the revenues required to cover the cost of production. The extraordinary costs associated with the Wanapum fracture have resulted in a roughly $6.5 million increase in Sales to power purchasers at cost from 2013 to 2014. During 2015 Sales to power purchasers at cost returned to pre-fracture levels. The District saw lower than expected Sales to power purchasers at cost in 2016 due to $9.9 million of net insurance proceeds related to the Wanapum fracture.

Retail energy sales and Sales to other utilities revenues are reflective of the individual ebbs and flows of the economy through power consumption and market forces on wholesale power prices. The increase in operating revenues from 2014 to 2015 is the effect of the rate increases and growth in consumption especially in industrial customers. The decrease in operating revenues from 2015 to 2016 is largely driven by the Shell Pooling Agreement because revenue associated with the agreement is only reported net of firm retail load SENA provides the Electric System. This has decreased gross Sales to other utilities by $20 million and Purchased Power expense by $27 million to effectively zero in 2016 as the District needs to purchase less and less power on the open market to meet the Electric System's retail load. Net wholesale revenues (Sales to other utilities less Purchased power expense) were $28.4 million, $54.4 million and $62.5 million from 2014 to 2016, respectively. Purchased power expense was abnormally high in 2014 due to the lost generation at Wanapum requiring additional market purchases. In 2015 and 2016, Purchased Power Expense has significantly decreased due to the effect of the Pooling agreement and the return of Wanapum to normal operations which has decreased Purchased power expense from $52.7 million in 2014 to zero in 2016.

Most components of Other Revenues (Expenses) remained flat from 2014 to 2016 with the exception of Interest and Other Income which rose substantially from 2014 to 2016 because of improved investment strategy and stronger market conditions.

Contributions In Aid of Construction ("CIAC") were $4.6 million in 2016. CIACs in 2015 and 2014 were much higher, $13.2 million and $22.8 million, respectively, due to the completion of some large contracts with SGL Automotive, Yahoo!, Intergate Quincy, LLC, and Microsoft.

## CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This report is designed to provide the District's customers, bondholders, creditors, and other interested parties with a general overview of the District's finances. If you have questions about this report or need additional information, contact the District's Chief Financial Officer at the Public Utility District No. 2 of Grant County, P.O. Box 878, Ephrata, Washington 98823.

# PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

## STATEMENTS OF NET POSITION
## DECEMBER 31, 2016 AND 2015
## (AMOUNTS IN THOUSANDS)

| ASSETS | 2016 | 2015 |
|---|---|---|
| CURRENT ASSETS | | |
| Cash | $ 742 | $ 261 |
| Investments | 93,719 | 62,237 |
| Restricted funds | | |
| Cash | 40,597 | 5,534 |
| Investments | 45,026 | 71,291 |
| Customer accounts receivable, net of allowance for uncollectible accounts | 23,250 | 28,769 |
| Materials and supplies | 17,582 | 17,418 |
| Other current assets | 1,479 | 1,631 |
| Total current assets | 222,395 | 187,141 |
| NONCURRENT ASSETS | | |
| Investments | 168,640 | 145,643 |
| Restricted funds | | |
| Cash | 1,380 | 985 |
| Investments | 237,476 | 252,887 |
| Conservation loans | 566 | 665 |
| Demand-side management | 1,025 | 1,391 |
| Preliminary expenses | 1,219 | 647 |
| Total other noncurrent assets | 410,306 | 402,218 |
| Utility plant, net of accumulated depreciation and amortization | 1,953,628 | 1,881,265 |
| Total noncurrent assets | 2,363,934 | 2,283,483 |
| TOTAL ASSETS | 2,586,329 | 2,470,624 |
| DEFERRED OUTFLOWS OF RESOURCES | | |
| Deferred outflows of resources - pensions | 8,428 | 5,004 |
| Deferred outflows of resources - losses on refundings | 5,367 | 6,518 |
| Total deferred outflow of resources | 13,795 | 11,522 |
| TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | $ 2,600,124 | $ 2,482,146 |

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

# PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

## STATEMENTS OF NET POSITION
## DECEMBER 31, 2016 AND 2015
## (AMOUNTS IN THOUSANDS)

| LIABILITIES AND NET POSITION | 2016 | 2015 |
|---|---|---|
| CURRENT LIABILITIES | | |
| Trade payable | $ 32,528 | $ 26,624 |
| Wages payable | 11,803 | 11,485 |
| Due to power purchasers | 4,441 | 1,462 |
| Accrued taxes | 6,490 | 6,713 |
| Customer deposits | 11,210 | 7,201 |
| Accrued bond interest | 30,607 | 28,415 |
| Unearned revenue | 6,007 | 628 |
| Habitat liability | 13,287 | 11,405 |
| Other current liabilities | 39 | 40 |
| Current portion of licensing obligations | 2,601 | 3,549 |
| Current portion of long-term debt | 32,075 | 30,915 |
| Total current liabilities | 151,088 | 128,437 |
| NONCURRENT LIABILITIES | | |
| Accrued other postemployment benefits | 2,491 | 2,089 |
| Long-term unearned revenue | 964 | 1,071 |
| Licensing obligations, less current portion | 52,520 | 52,642 |
| Pension obligations | 60,922 | 52,761 |
| Revenue bonds, less current portion | 1,293,030 | 1,275,105 |
| Unamortized bond premium, net of discount | 40,428 | 46,673 |
| Total noncurrent liabilities | 1,450,355 | 1,430,341 |
| TOTAL LIABILITIES | 1,601,443 | 1,558,778 |
| DEFERRED INFLOWS OF RESOURCES | | |
| Deferred inflows of resoureces - pensions | 926 | 7,837 |
| Total deferred inflows of resources | 926 | 7,837 |
| TOTAL LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | 1,602,369 | 1,566,615 |
| NET POSITION | | |
| Net investment in capital assets | 638,520 | 613,865 |
| Restricted | 160,550 | 146,705 |
| Unrestricted | 198,685 | 154,961 |
| Total net position | 997,755 | 915,531 |
| TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND NET POSITION | $ 2,600,124 | $ 2,482,146 |

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

# PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

## STATEMENTS OF REVENUES AND EXPENSES AND CHANGES IN NET POSITION
## YEARS ENDED DECEMBER 31, 2016 AND 2015
## (AMOUNTS IN THOUSANDS)

| | 2016 | 2015 |
|---|---|---|
| OPERATING REVENUES | | |
| Sales to power purchasers at cost | $ 40,001 | $ 51,083 |
| Retail energy sales | | |
| Residential | 40,252 | 39,127 |
| Irrigation | 23,876 | 24,481 |
| Commercial and industrial | 110,604 | 108,273 |
| Governmental and others | 1,066 | 1,034 |
| Sales to other utilities | 62,521 | 82,073 |
| Wholesale fiber optic network sales | 6,170 | 5,338 |
| Other | 1,826 | 1,760 |
| Total operating revenues | 286,316 | 313,169 |
| OPERATING EXPENSES | | |
| Purchased power | - | 27,634 |
| Generation | 28,803 | 27,021 |
| Transmission | 4,634 | 10,843 |
| Distribution | 14,053 | 13,904 |
| Customer and information services | 5,979 | 6,850 |
| Wholesale fiber optic network operations | 1,325 | 1,280 |
| Administrative and general | 37,107 | 35,241 |
| License compliance and related agreements | 18,909 | 21,771 |
| Depreciation and amortization | 61,956 | 56,985 |
| Taxes | 14,808 | 15,548 |
| Total operating expenses | 187,574 | 217,077 |
| NET OPERATING INCOME | 98,742 | 96,092 |
| OTHER REVENUES (EXPENSES) | | |
| Interest and other income | 10,008 | 4,600 |
| Interest on revenue bonds and other, net of capitalized interest | (56,469) | (47,555) |
| Federal rebates on revenue bonds | 10,545 | 8,214 |
| Amortization of debt discount/premium | 5,094 | 4,450 |
| Cost of debt issuance | (195) | (1,277) |
| Total other revenues (expenses) | (31,017) | (31,568) |
| CONTRIBUTIONS IN AID OF CONSTRUCTION | 4,603 | 13,222 |
| EXTRAORDINARY LOSS - WANAPUM FRACTURE | 9,896 | (4,359) |
| CHANGE IN NET POSITION | 82,224 | 73,387 |
| NET POSITION | | |
| Beginning of year | 915,531 | 842,144 |
| Total net position - end of year | $ 997,755 | $ 915,531 |

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

# PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

## STATEMENTS OF CASH FLOWS
## YEARS ENDED DECEMBER 31, 2016 AND 2015
## (AMOUNTS IN THOUSANDS)

| | 2016 | 2015 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Cash received from retail energy sales | $ 181,168 | $ 165,889 |
| Cash received from sales to power purchasers at cost | 42,210 | 78,309 |
| Cash received from sales to other utilities | 76,994 | 62,534 |
| Other cash receipts | 7,811 | 7,384 |
| Net cash paid for customer deposits | 3,880 | (2,676) |
| Cash paid for purchase of power | (15,091) | (28,851) |
| Cash paid to contractors, suppliers, and employees | (110,516) | (125,494) |
| Cash paid for deposits | 134 | - |
| Taxes paid | (15,020) | (14,560) |
| Cash recovered/(paid) for extraordinary loss | 9,896 | (4,359) |
| Net cash provided by operating activities | 181,466 | 138,176 |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | |
| Principal paid on revenue bonds | (30,915) | (29,589) |
| Interest paid on revenue bonds | (54,276) | (45,819) |
| Federal interest rebates | 10,545 | 8,214 |
| Bond proceeds | 50,000 | 191,515 |
| Payment on refunded debt | - | (101,037) |
| Bond issuance cost | (195) | (1,277) |
| Cash received from contributions in aid of construction | 9,981 | 12,534 |
| Licensing obligation payments | (3,604) | (3,805) |
| Acquisition and construction of plant assets | (125,728) | (146,128) |
| Proceeds on sale of plant assets | 3,493 | 462 |
| Miscellaneous nonoperating income | 912 | 830 |
| Net cash used in capital and related financing activities | (139,787) | (114,100) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of investment securities | (570,954) | (1,258,242) |
| Sale proceeds of investment securities | 516,321 | 1,281,468 |
| Investment income proceeds | 8,794 | 5,863 |
| Net repurchase agreements | 40,000 | (54,000) |
| Net cash received (paid) for conservation loans | 99 | (8) |
| Net cash used in investing activities | (5,740) | (24,919) |
| NET INCREASE (DECREASE) IN CASH | $ 35,939 | $ (843) |

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

# PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

## STATEMENTS OF CASH FLOWS
## YEARS ENDED DECEMBER 31, 2016 AND 2015
## (AMOUNTS IN THOUSANDS)

| | 2016 | 2015 |
|---|---|---|
| CASH AT END OF YEAR | $ 42,719 | $ 6,780 |
| CASH AT BEGINNING OF YEAR | 6,780 | 7,623 |
| NET INCREASE (DECREASE) IN CASH | $ 35,939 | $ (843) |
| OPERATING ACTIVITIES | | |
| Net operating income | $ 98,742 | $ 96,092 |
| Adjustments to reconcile net operating income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 61,956 | 56,985 |
| Accretion expense | 2,533 | 2,826 |
| Earned revenue from deposits | (107) | (107) |
| Provision for uncollectible accounts | 198 | 175 |
| Cash received (paid) for extraordinary loss | 9,896 | (4,359) |
| Cash provided by (used in) changes in operating assets and liabilities: | | |
| Change in habitat funds held in trust | 1,584 | (386) |
| Customer accounts receivable | 6,089 | (7,575) |
| Materials and supplies | (164) | 417 |
| Other current assets | 153 | 193 |
| Trade and wages payables | (3,638) | (6,954) |
| Payable to power purchasers | 2,209 | 5,892 |
| Deferred outflows - Pension | (3,423) | (2,307) |
| Deferred inflows - Pension | (6,910) | (10,959) |
| Pension obligation | 8,161 | 9,545 |
| Accrued taxes | (224) | 975 |
| Customer deposits | 4,009 | (2,658) |
| Accrued other postemployment benefits | 402 | 381 |
| NET CASH PROVIDED BY OPERATING ACTIVITIES | $ 181,466 | $ 138,176 |

| | 2016 | 2015 |
|---|---|---|
| **Supplemental Disclosure** | | |
| Changes in construction costs included in accounts payable | $ 10,567 | $ (15,252) |

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

## 1. ORGANIZATION AND ACCOUNTING POLICIES

Public Utility District No. 2 of Grant County, Washington (the "District") is composed of two operating systems: the Electric System and the Priest Rapids Project. The Priest Rapids Project is operated under Federal Energy Regulatory Commission ("FERC") License, Project No. 2114. The District also maintains a Service System to provide administrative services to the operating systems. Internal transactions, including revenues and expenses between the District's reporting segments and the Service System, have been eliminated in the accompanying financial statements in accordance with accounting principles generally accepted in the United States of America. The District is required by its financing arrangements to maintain separate accounts and to report separately on each operating system. See Note 13. The financing arrangements require maintenance of certain funds and application of accounting procedures prescribed by the State of Washington, which generally conform to those prescribed by FERC and accounting principles generally accepted in the United States of America. The accompanying financial statements are those of the District, which generates, transmits, and distributes electric energy and wholesale fiber optic network services within Grant County, Washington.

The District maintains its accounts in accordance with accounting principles generally accepted in the United States of America for proprietary funds as prescribed by the Governmental Accounting Standards Board ("GASB"). The District's accounting records generally follow the Uniform System of Accounts for public utilities and licensees prescribed by FERC except as it relates to the accounting for Contributions In Aid of Construction ("CIAC"). FERC prescribes for CIAC proceeds to be recorded as a reduction to plant.

In February 2015, GASB issued Statement No. 72, "Fair Value Measurement and Application," this Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The District adopted this Statement in 2016. (Refer to Note 2.)

In June 2015, GASB issued Statement No. 73, "Accounting and Financial Reporting for Pensions and Related Assets that are not within the Scope of GASB 68," the objective of this Statement is to improve the usefulness of information about pensions included in the general purpose external financial reports of state and local governments for making decisions and assessing accountability. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. The District is currently evaluating the financial statement impact of adopting these statements.

In June 2015, GASB issued Statement No. 74, “Financial Reporting for Postemployment Benefit Plans other than Pension Plans” and Statement No. 75, “Accounting and Financial Reporting for Postemployment Benefits other than Pensions.” The primary objective of these statements is to improve both the usefulness of information about postemployment benefits other than pensions (OPEB) included in the external financial reports of state and local OPEB plans and the accounting and financial reporting by state and local governments for OPEB. The statements replace Statement No. 43, “Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,” Statement No. 57, “OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans” and Statement No. 45, “Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.” These statements establish standards for measuring and recognizing liabilities, deferred outflows and deferred inflows of resources and expenses. For defined benefit OPEB, these statements identify the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined OPEB are also addressed. Statements No. 74 and No. 75 are effective for fiscal years 2017 and 2018, respectively. The District is currently evaluating the financial statement impact of adopting these statements.

In June 2015, GASB issued Statement No. 76, “The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments.” The statement identifies the hierarchy of accounting principles used to prepare financial statements of state and local governments in conformity with generally accepted accounting principles. The adoption of this statement did not have a material effect on the District’s financial statements.

In August 2015, GASB issued Statement No. 77, “Tax Abatement Disclosures.” The statement establishes financial reporting standards for tax abatement agreements entered into by state and local governments. The District is currently evaluating the financial statement impact of adopting this statement.

In December 2015, GASB issued Statement No. 78 “Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans” The statement establishes accounting and financial reporting standards for defined benefit pensions provided to the employees of state or local governmental employers through a cost-sharing multiple-employer defined benefit pension plan meeting certain criteria. The District is currently evaluating the financial statement impact of adopting this statement.

In December 2015, GASB issued Statement No. 79, "Certain External Investment Pools and Pool Participants." The statement establishes accounting and financial reporting standards for qualifying external investment pools that elect to measure for financial reporting purposes all of their investments at amortized cost, as well as for state and local governments that participate in such a qualifying external investment pool. The District does not participate in any of the investment pools as defined by this statement; therefore, the pronouncement has no impact to the District's financials.

In January 2016, GASB issued Statement No. 80, "Blending Requirements for Certain Component Units-an amendment of GASB Statement No. 14." This Statement's objective is to improve financial reporting by clarifying the financial statement presentation requirements for certain component units. The District is currently evaluating the financial statement impact of adopting this statement.

In March 2016, GASB issued Statement No. 81, "Irrevocable Split Interest Agreements." The objective of this statement is to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations where a government is a beneficiary of the agreement. The District has evaluated the financial statement impact of adopting this statement and determined it will not have a material impact on the District's financial statements.

In March 2016, GASB issued Statement No. 82, "Pension Issues-an amendment of GASB Statements No. 67, No. 68, and No. 73." The purpose of this statement is to address certain issues that have been raised with respect to Statement No. 67, No. 68 and No. 73. Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The requirements of Statement 82 are effective for reporting periods after June 15, 2017. The District is currently evaluating the financial statement impact of adopting this statement.

In November 2016, GASB issued Statement No. 83, "Certain Asset Retirement Obligations." An asset retirement obligation (ARO) is a legally enforceable liability associated with the retirement of a tangible capital asset. GASB Statement 83 establishes guidance for determining the timing and pattern of recognition for liabilities and corresponding deferred outflow of resources related to AROs. The requirements of Statement 83 are effective for reporting periods beginning after June 15, 2018, with earlier application encouraged. The District is currently evaluating the financial statement impact of adopting this statement.

***Revenue Recognition –*** The District recognizes revenues associated with power sales to its retail and wholesale customers when the power is delivered, which includes an estimate of revenue earned but not billed to customers as of year-end.

Revenues associated with power sales from the Priest Rapids Project under the Power Sales Contracts described in Note 6 are recorded on a cost-based formula specified in the contracts which include operation and maintenance costs, 115% of debt service, and adjustments related to other factors. Depreciation, amortization, charges paid by the Renewal, Replacement and Contingency Fund, and Construction Funds are not considered costs of producing and delivering power for this purpose.

***SENA Pooling Agreement –*** With the implementation of the SENA Pooling Agreement (2016 was the first full year with the agreement in effect), the volume of open market power purchases required by the District has dropped dramatically because SENA provides firm power sufficient to meet the Electric System's retail load. All activity for the agreement (sales, purchases and other contractual monthly true-up payments) are presented net in either the "Sales to other utilities" or "Purchased power expense" line items on the Statement of Revenues and Expenses and Changes in Net Position. For 2016 and 2015 the agreement resulted in a net sale for the District. Additionally, in 2016, the District has changed its method of presenting certain financial benefits of the Priest Rapids Project in the Statements of Cash Flows as "Cash received from sales to other utilities" rather than as an offset to "Cash paid for purchase of power," due to the economic impact the SENA Pooling Agreement has on the District. This change in presentation has no impact on the net cash flows from operating activities.

***Allowance for Uncollectible Accounts –*** Management reviews accounts receivable on a regular basis to determine if any receivables will potentially be uncollectible. The allowance for uncollectible accounts includes amounts due from specific customers for which collection is in question. Such estimates are developed based on historical experience. For 2016 and 2015, the allowance for uncollectible accounts was $211,000 and $409,000, respectively.

***Contributions in Aid of Construction –*** A portion of the District's utility plant is financed through contributions from customers in accordance with the District's Line Extension Policy. Additionally, a portion of utility plant may be financed through contributions from other sources, such as other governmental organizations. The District recognizes capital contributions from these sources as nonoperating revenue at the point at which it becomes nonrefundable. The District recognized $4.6 million and $13.2 million of contributions in aid of construction for the years ended December 31, 2016 and 2015, respectively.

***Capitalized Interest* –** Interest costs incurred to finance major construction projects are capitalized as part of the cost of the project. The composite interest rate for calculating capitalized interest was 2.20% and 4.26% for 2016 and 2015, respectively. Interest capitalized during 2016 and 2015 was $5.2 million and $12.2 million, respectively.

***Utility Plant* –** Utility plant assets are recorded at cost including an allocation of internal payroll and other administrative and general costs associated with construction of the assets. Depreciation is determined by the straight-line method over the estimated life of the asset. The District's asset lives used for computing depreciation range from five to 100 years, with an average rate of 2.25% and 2.19% for 2016 and 2015, respectively. When utility plant assets are retired, their original cost, together with removal costs, less salvage, are charged to accumulated depreciation.

The costs of maintenance and repairs are charged to operations as incurred. Renewals, replacements, and betterments are capitalized. The District assesses its assets for obsolescence and possible impairment on a periodic basis. Once an asset has been identified as impaired due to a significant and unexpected decline in usable capacity, it is written down to reflect its current service utility and the associated impairment loss is charged either to operations or an extraordinary item depending on its nature.

***Energy Conservation and Demand-Side Management ("DSM") Programs* –** The District's expenditures for regional conservation programs and other DSM programs which benefit future periods by reducing energy supply requirements have historically been capitalized and amortized over the expected useful lives of the programs. During 2009, the District began expensing DSM costs as Customer information and services expense. The balances accumulated prior to the change in accounting are being amortized over the original useful lives of the programs.

***Cash* –**The District classifies only amounts held in demand deposit accounts as cash.

***Investments* –** All investments are presented at fair value (refer to Note 2 for additional details). Discounts and premiums on investments are amortized as adjustments to interest income over the remaining term of the investments using the constant yield method.

Short-term investments are defined as investments with a maturity of less than one year. The purchase and maturity of investment instruments are reported on a gross basis in the Statements of Cash Flows, with the exception of repurchase agreements, which are reported on a net basis.

Realized and unrealized gains and losses on investments are included in Interest and other income on the Statements of Revenues and Expenses and Change in Net Position.

***Materials and Supplies –*** Materials and supplies consist of hydroelectric generation, transmission, and distribution assets as well as fiber optic cable and fiber-related supplies. All inventory amounts are recorded at average cost.

***Due to Power Purchasers –*** This balance represents estimated power costs received by the Priest Rapids Project from power purchasers in excess of actual power costs, which will be paid to the power purchasers.

***Debt Discounts, Premiums, and Issuance Costs –*** Debt discounts and premiums relating to the sale of bonds are amortized over the lives of the related bonds using the constant yield method. Debt issuance costs are recognized in the period incurred.

***Refunds of Debt –*** The gain or loss on refunding of debt is amortized over the remaining life of the refunded or newly issued bond, whichever is shorter. If debt is extinguished using the District's own reserves, any resulting gain or loss is recognized during the current period and recorded as a deferred inflow or outflow.

***Unearned Revenue –*** Contributions In Aid of Construction that are refundable are recorded as unearned revenue. Additionally, the District has two long-term exchange contracts under which the District received collective prepayments of $2 million that are being amortized into revenue on a straight-line basis over the life of these agreements.

***Revenue Taxes –*** Utility revenue-based taxes assessed by governmental entities are accounted for as a separate cost collected from customers for remittance to those governmental entities. Therefore, revenue taxes paid to the taxing authorities are accounted for as an operating expense on the Statements of Revenues and Expenses and Changes in Net Position. Taxes collected from customers on behalf of other governmental entities are included in Retail energy sales in the Statements of Revenues and Expenses and Changes in Net Position.

***Net Position –*** The District classifies its net position into three components – Net investment in capital assets; Restricted; and Unrestricted. These classifications are defined as follows:

- *Net investment in capital assets* – This component of net position consists of capital assets, net of accumulated depreciation reduced by the outstanding debt balances, net of unamortized debt expenses, and related unspent project and debt service funds.

- *Restricted* – This component of net position consists of assets with constraints placed on their use. Constraints include those imposed by debt trust indentures, grants or laws and regulations of other governments, or by law through constitutional provisions or enabling legislation.

- *Unrestricted* – This component of net position consists of net assets and liabilities that do not meet the definition of "restricted" or "net investment in capital assets."

***Significant Risk and Uncertainties* –** The District is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include weather and natural-disaster-related disruptions, collective bargaining labor disputes, fish and other Endangered Species Act ("ESA") issues, Environmental Protection Agency regulations, federal government regulations or orders concerning the operation, maintenance and/or licensing of hydroelectric facilities, and the changes to the regulatory environment of the electrical utility industry.

The District self-insures for general and auto liability for amounts below an excess liability policy, and the District carries aircraft, foreign and employment policies below excess liability policies. The District is involved in litigation in the ordinary course of business with results that are uncertain but the risk to the District at this time is considered immaterial.

***Personal Leave Benefit* –** Employees of the District accrue a personal leave benefit based upon a years of service schedule. Personal leave may be used for vacation, sick leave, or other employee absences. The District records personal leave as an expense and a liability as earned. Unused personal leave may be accumulated up to a maximum of 1,200 hours for employees who began service prior to April 1, 2011. For employees hired on or after April 1, 2011, the maximum amount of accrued personal leave is 700 hours.

***Use of Estimates* –** The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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. Actual results could differ from these estimates. The District has used significant estimates in determination of unbilled revenue, Licensing obligations, allowance for uncollectible accounts, Accrued other postemployment benefits, and depreciable lives of utility plant.

***Energy Risk Management –*** The District's power marketing activities are limited to sales and purchases to meet surplus and deficits of expected forecasted load at the best available price. To mitigate risk in the portfolio, the District has: 1) established the Enterprise Risk Management Committee, 2) adopted the Energy Risk Management and Reporting Policy to structure ongoing monitoring and review of power transactions, and 3) entered into a five year transaction with SENA that largely removes the District from trading activities. The policy outlines the parameters for transactions, trader and counterparty exposure, and serves as a formal communication to all District employees performing power marketing functions. Although the District is entering into fewer physical purchases for load requirements during the term of the SENA Pooling Agreement, it will continue to meet the evolving demands of retail customers which include the pursuit of alternatively sourced power and environmental attributes beyond the requirements of the State of Washington.

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

## 2. CASH AND INVESTMENTS

The District's cash deposits at December 31, 2016 and 2015, were either entirely covered by federal depository insurance or protected against loss by being on deposit with financial institutions recognized as qualified public depositories of the State of Washington under the Revised Code of Washington ("RCW") Chapter 39. Subject to specific bond resolution limitations, management is permitted to invest as provided under the laws of the State of Washington.

Unspent cash, and associated investments, received in connection with bond offerings are maintained in funds as required by the District's bond indentures. Restricted assets represent funds that are restricted by bond covenants or third party contractual agreements. Funds that are allocated by Commission resolution are considered to be board-designated funds. Board designated funds are a component of unrestricted assets as their use may be redirected at any time by Commission approval.

As of December 31, the District's unrestricted, board designated, and restricted assets included on the Statement of Net Position as Cash and Investments, including accrued interest, consisted of the following:

| (AMOUNTS IN THOUSANDS) | 2016 | 2015 |
|---|---|---|
| **Unrestricted assets:** | | |
| Unrestricted funds: | | |
| Revenue and Service System funds | $ 136,227 | $ 83,838 |
| Board designated funds: | | |
| Electric System Reserve and Contingency fund | 125,820 | 123,243 |
| Self-Insurance Reserve fund | 1,054 | 1,060 |
| Total board designated funds | 126,874 | 124,303 |
| Total unrestricted funds | 263,101 | 208,141 |
| Restricted: | | |
| Construction funds | 107,793 | 131,834 |
| Bond Sinking funds | 128,297 | 113,564 |
| Debt Service Reserve funds | 61,143 | 59,808 |
| Renewal, Replacement and Contingency fund | 12,133 | 12,016 |
| Habitat funds | 13,387 | 11,732 |
| Quincy Chute Renewal and Replacement fund | 1,726 | 1,743 |
| Total restricted funds | 324,479 | 330,697 |
| Total | $ 587,580 | $ 538,838 |

***Interest Rate Risk –*** The District has adopted a formal investment policy and an investment oversight committee which monitors its investment position limitations as a means of managing its exposure to fair value losses arising from increasing interest rates. To further mitigate risk of selling investments early to meet unexpected cash flow needs, a minimum of 20% of the total portfolio will be comprised of investments maturing within one year.

***Credit Risk –*** The District has adopted a formal investment policy that specifies minimal credit rating acceptability criteria of potential investment issuers as well as both a wholesale and retail electric power customer credit risk management program as a means of managing the District's exposure to credit risk. Pursuant to the investment policy, the minimum credit rating requirement at the time of investment purchase is one of the three highest credit ratings of a nationally recognized rating agency.

***Custodial Credit Risk –*** The District's investment policy requires that securities purchased are held by a master custodian or other entity legally allowed to act as an independent third party on behalf of the District within that entity's trust department.

***Concentration of Credit Risk –*** The District's adopted investment policy states that with the exception of direct U.S. Government obligations, repurchase agreements collateralized by the same, and the state investment pool, no more than fifty percent (50%) of the total portfolio par value will be invested in government sponsored agencies, supranational institutions or municipal bonds, and no more than twenty-five percent (25%) of the total portfolio par value will be invested in corporate bonds and commercial paper. Credit concentration of the District's investment portfolio is actively monitored by the investment oversight committee as required by the District's adopted investment policy.

The investment oversight committee actively monitors portfolio composition and seeks to ensure prudent diversification is maintained. The following are the concentrations of risk greater than 5%, in either year. The credit ratings listed are from Standard and Poor's as of December 31, 2016. TSY refers to U.S. Treasury securities and N/R means not rated.

| Investments by Issuer | Credit Rating | 2016 | 2015 |
|---|---|---|---|
| U.S. Treasuries | TSY | 31% | 38% |
| Federal Home Loan Bank | AA+ | 5% | 4% |
| Federal National Mortgage Assoc. | AA+ | 4% | 8% |

The District's investments at December 31, 2016 and 2015, as identified on the Statements of Net Position, are shown below by investment type. All investments are either issued or registered in the name of the District or are held by the District or by the District's agent in the District's name. The difference between the totals shown in the previous table and table below is accrued interest of $3.2 million and $2.6 million for 2016 and 2015, respectively.

During 2016 and 2015, the District realized $9.3 million and $6.3 million of interest earnings and realized gains from investments, respectively. The unrealized net gain/loss on investments held at December 31, 2016 and 2015, was a $2.4 million net loss and a $2.6 million net loss, respectively. Investments are made in investment types authorized by Washington State law. The types are 1) Obligations of the U.S. Government and its agencies, 2) Repurchase agreements collateralized by U.S. Government obligations, 3) Supranational institutions, 4) Money market funds that have holdings of or are backed by U.S. Government obligations 5) Municipal bonds and 6) Corporate bonds and commercial paper. Investments by type at December were as follows:

| **(AMOUNTS IN THOUSANDS)** | **2016** | **2015** |
|---|---|---|
| U.S. Treasuries | $ 182,624 | $ 205,842 |
| Municipal Bonds | 184,588 | 133,586 |
| U.S. Agencies | 102,972 | 107,564 |
| Repurchase Agreements | 28,000 | 68,000 |
| Commercial Paper | 28,071 | 14,482 |
| Supranational Institutions | 15,423 | - |
| Total investments | 541,678 | 529,474 |
| Cash | 42,719 | 6,780 |
| Total cash and investments | $ 584,397 | $ 536,254 |

**Fair Value Measurements -** The District's investments have been adjusted to reflect fair value measurements as of December 31, 2016, obtained from available financial industry valuation sources. The District categorizes its fair value measurements within the fair value hierarchy established by GASB Statement No. 72 "Fair Value Measurement and Application," which has been adopted in 2016. The hierarchy is based on the valuation inputs used to measure the fair value of the assets. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. In particular, the District valued its US Treasuries using quoted prices in active markets. Debt securities classified in Level 2 of the fair value hierarchy are valued using a matrix pricing technique. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices. Below are the District's fair value measurements as of December 31, 2016 and 2015:

| (AMOUNTS IN THOUSANDS) | Total 12/31/2016 | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Investments by fair value level | | | | |
| Debt Securities | | | | |
| Municipal Bonds | $ 184,588 | $ - | $ 184,588 | $ - |
| U.S. Treasuries | 182,624 | 182,624 | - | - |
| U.S. Agencies | 102,972 | - | 102,972 | - |
| Commercial Paper | 28,071 | - | 28,071 | - |
| Repurchase Agreements | 28,000 | - | 28,000 | - |
| Supranational Institutions | 15,423 | - | 15,423 | - |
| Total investments by fair value level | $ 541,678 | $ 182,624 | $ 359,054 | $ - |

| (AMOUNTS IN THOUSANDS) | Total 12/31/2015 | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Investments by fair value level | | | | |
| Debt Securities | | | | |
| U.S. Treasuries | $ 205,842 | $ 205,842 | $ - | $ - |
| Municipal Bonds | 133,586 | - | 133,586 | - |
| U.S. Agencies | 107,564 | - | 107,564 | - |
| Repurchase Agreements | 68,000 | - | 68,000 | - |
| Commercial Paper | 14,482 | - | 14,482 | - |
| Total investments by fair value level | $ 529,474 | $ 205,842 | $ 323,632 | $ - |

## 3. UTILITY PLANT

Utility plant of the District as of December 31, 2016, and December 31, 2015, is summarized as follows:

| (AMOUNTS IN THOUSANDS) | Balance 2015 | Additions | Retirements/ Transfers | Balance 2016 |
|---|---|---|---|---|
| Distribution facilities | $ 494,080 | $ 10,738 | $ (280) | $ 504,538 |
| Transmission facilities | 240,843 | 297 | - | 241,140 |
| Hydro facilities | | | | |
| Power plant structures | 73,227 | 62,789 | (1,156) | 134,860 |
| Reservoirs, dams, waterways | 495,941 | | - | 495,941 |
| Power plant equipment | 567,504 | 11,946 | (408) | 579,042 |
| General facilities | | | | |
| Quincy Chute (Note 6) | 17,771 | - | - | 17,771 |
| Potholes East Canal (Note 6) | 16,450 | - | - | 16,450 |
| Other generation | 30 | - | - | 30 |
| General plant | 408,709 | 67,542 | (402) | 475,849 |
| FERC License | 119,355 | - | - | 119,355 |
| Other intangible assets | 27,769 | 6,228 | - | 33,997 |
| Total | 2,461,679 | 159,540 | (2,246) | 2,618,973 |
| Accumulated depreciation and amortization | (870,451) | (61,874) | 1,716 | (930,609) |
| Subtotal | 1,591,228 | 97,666 | (530) | 1,688,364 |
| Land and land rights | 24,618 | - | - | 24,618 |
| Construction in progress | 265,419 | 134,669 | (159,442) | 240,646 |
| Total net utility plant | $ 1,881,265 | $ 232,335 | $ (159,972) | $ 1,953,628 |

| (AMOUNTS IN THOUSANDS) | Balance 2014 | Additions | Retirements/ Transfers | Balance 2015 |
|---|---|---|---|---|
| Distribution facilities | $ 472,631 | $ 21,735 | $ (286) | $ 494,080 |
| Transmission facilities | 228,683 | 12,435 | (275) | 240,843 |
| Hydro facilities | | | | |
| Power plant structures | 74,845 | 126 | (1,744) | 73,227 |
| Reservoirs, dams, waterways | 410,252 | 83,945 | 1,744 | 495,941 |
| Power plant equipment | 543,586 | 25,057 | (1,139) | 567,504 |
| General facilities | | | | |
| Quincy Chute (Note 6) | 17,771 | - | - | 17,771 |
| Potholes East Canal (Note 6) | 16,450 | - | - | 16,450 |
| Other generation | 30 | - | - | 30 |
| General plant | 351,970 | 56,739 | - | 408,709 |
| FERC License | 119,335 | 20 | - | 119,355 |
| Other intangible assets | 24,670 | 3,099 | - | 27,769 |
| Total | 2,260,223 | 203,156 | (1,700) | 2,461,679 |
| Accumulated depreciation and amortization | (815,038) | (57,113) | 1,700 | (870,451) |
| Subtotal | 1,445,185 | 146,043 | - | 1,591,228 |
| Land and land rights | 24,618 | - | - | 24,618 |
| Construction in progress | 334,546 | 132,365 | (201,492) | 265,419 |
| Total net utility plant | $ 1,804,349 | $ 278,408 | $ (201,492) | $ 1,881,265 |

## 4. LICENSING

The Priest Rapids Project is operated under a 44-year FERC license that expires in 2052. Costs associated with the relicensing efforts, totaling $62.2 million, were recorded as an intangible asset included in Utility plant and are being amortized over the term of the license. Accumulated amortization related to the relicensing efforts totaled $19.1 million and $16.4 million as of December 31, 2016 and 2015, respectively.

Under the license, the District is committed to numerous obligations related to fish and habitat protection which require payments to other organizations using funds provided by the District. The present value of these obligations totaled $55.1 million as of December 31, 2016, of which approximately $2.6 million is expected to be paid within one year. The present value of the obligations was $56.1 million as of December 31, 2015. These amounts are the FERC Licensing Obligations reflected as liabilities in the Statement of Net Position. The elements of these obligating payments, comprising the Salmon and Steelhead Agreement, Part A (Hatchery Renovation) and Part B (Resident Fish Monitoring and Trout Purchase), are further discussed in Note 7.

## 5. REVENUE BONDS

In April of 2016, the District issued $50 million of revenue bonds to finance improvements to the Electric System through a direct placement bond held with Bank of America, N.A. In October of 2015, the District issued $90.7 million of revenue and refunding bonds at a net premium of $10.7 million and $90 million in Clean Renewable Energy Bonds, associated with the Priest Rapids Project to refund certain bonds previously issued, to finance improvements at the Priest Rapids Project, to pay issuance costs, and to fund a debt service reserve. The refunding of $97 million resulted in a net present value savings of $11.1 million. The Clean Renewable Energy Bonds have an authorized 70% refund from the Federal Government on interest payments made.

The District’s total outstanding bonds of $1.3 billion are mostly comprised of fixed rate debt and are secured by a pledge of the net revenues of the District and are on parity with each other.

The District’s variable rate outstanding bonds total $100 million and are secured by a pledge of the net revenues of the District of which $50 million is on parity with the senior fixed rate bonds and $50 million is subordinated junior lien bonds.

The District's outstanding revenue bonds as of December 31 were as follows:

| (AMOUNTS IN THOUSANDS) | 2016 | 2015 |
|---|---|---|
| Electric System, interest rates of .84% to 5.0%, maturing through 2044 | $ 244,795 | $ 194,795 |
| Priest Rapids Project, interest rates of 1.79% to 5.83%, maturing through 2044 | 1,080,310 | 1,111,225 |
| Total revenue bonds outstanding | $ 1,325,105 | $ 1,306,020 |

Scheduled debt service requirements for the District's bonds are as follows:

| (AMOUNTS IN THOUSANDS) | Principal | Interest | Total |
|---|---|---|---|
| 2017 | $ 32,075 | $ 61,319 | $ 93,394 |
| 2018 | 31,610 | 59,941 | 91,551 |
| 2019 | 93,590 | 57,918 | 151,508 |
| 2020 | 45,655 | 55,603 | 101,258 |
| 2021 - 2025 | 189,655 | 246,224 | 435,879 |
| 2026 - 2030 | 264,410 | 187,389 | 451,799 |
| 2031 - 2035 | 247,165 | 124,230 | 371,395 |
| 2036 - 2040 | 319,865 | 66,415 | 386,280 |
| 2041 - 2044 | 101,080 | 6,412 | 107,492 |
| Total | $ 1,325,105 | $ 865,451 | $ 2,190,556 |

For the years ending December 31, 2016 and 2015, the District is in compliance with all financial covenants related to the outstanding bonds, which includes a minimum debt service coverage of 1.15x and 1.25x for the Priest Rapids Project bonds and Electric System bonds, respectively.

During the years ended December 31, the following changes occurred in the District's long-term debt:

| (AMOUNTS IN THOUSANDS) | Balance 2015 | Additions | Reductions | Balance 2016 | Due Within One Year |
|---|---|---|---|---|---|
| Revenue bonds payable | $ 1,306,020 | $ 50,000 | $ (30,915) | $ 1,325,105 | $ 32,075 |
| Unamortized premiums and discounts, net | 46,673 | - | (6,245) | 40,428 | - |
| Total | $ 1,352,693 | $ 50,000 | $ (37,160) | $ 1,365,533 | $ 32,075 |

| (AMOUNTS IN THOUSANDS) | Balance 2015 | Additions | Reductions | Balance 2016 | Due Within One Year |
|---|---|---|---|---|---|
| Revenue bonds payable | $ 1,251,775 | $ 180,720 | $ (126,475) | $ 1,306,020 | $ 30,915 |
| Unamortized premiums and discounts, net | 45,578 | 10,675 | (9,580) | 46,673 | - |
| Total | $ 1,297,353 | $ 191,395 | $ (136,055) | $ 1,352,693 | $ 30,915 |

## 6. POWER PURCHASER COMMITMENTS

### Priest Rapids Project

Under the Priest Rapids Power Sales Contracts, the amount of net power costs incurred by the District in serving its load changes on an annual basis in relation to its firm power requirements. The District incurred 73.4% and 67.4% of Priest Rapids Project power costs with power purchasers funding 26.6% and 32.6% for 2016 and 2015, respectively. Each purchaser is obligated to pay its share of the cost (excluding depreciation and amortization) of producing and delivering power, plus 115% of its share of the amounts required for debt service payments.

### Bonneville Power Administration (BPA)

The District is a statutory preference customer of BPA. The District signed a BPA preference contract during 2008 to serve its Grand Coulee load of approximately 5 average megawatts ("aMW") that expires September 30, 2028. The District has purchased from BPA the transmission required to deliver the power associated with this load through September 30, 2028. In 2009, the District entered into a five-year agreement for 150 MW of Long-Term Firm (LTF) transmission, and this agreement expired on December 31, 2015. This 150 MW of transmission is no longer needed due to the completion of the new Columbia/Rocky Ford 230 kV line in February 2014. The District has 12 MW of transmission for the delivery of power from the Nine Canyon Wind Project with a term expiring on October 1, 2030.

District management estimates the District's minimum commitments to BPA for the next five years are as follows:

**Estimated BPA Contractual Payments**
**(AMOUNTS IN THOUSANDS)**

| | |
|---|---|
| 2017 | $ 973 |
| 2018 | 1,026 |
| 2019 | 1,440 |
| 2020 | 2,519 |
| 2021 | 2,538 |

**Nine Canyon Wind Power Purchase Agreement**

The District participates in a power purchase agreement with Energy Northwest for Phase I of the Nine Canyon Wind Project (the "Project") which consists of 37 wind turbines with an aggregate generating capacity of approximately 48 MW. Energy Northwest is a municipal corporation and a joint operating agency of the State of Washington (formerly known as the Washington Public Power Supply System). The District does not participate in the two other phases of the Project which comprise additional generation capacity of approximately 48 MW. The phases are operated together as a single project under an amended power purchase agreement.

The District is one of nine public agencies participating in the original project power purchase agreement for Phase I of the Project. The District's purchaser share of Phase I of the project output was 25% of output up to a maximum of 12 MW. Since the District did not participate in either Phase II or Phase III of the Project, its share of the combined Project is 12.54%. In exchange for the output, the District pays its proportionate share of certain Project costs and its 25% share of Phase I debt service.

Scheduled debt service requirements, inclusive of principal and interest, for the District's 25% share of the bonds as well as certain other Project costs are estimated at $2 million annually.

**Yakama Nation Agreement**

In 2007, the District entered into an agreement with the Yakama Nation that provides mutual benefits to both parties. In exchange for physical benefits from the Priest Rapids Project, the Yakama Nation works collaboratively with the District on environmental issues affecting the project and in the development of new generation resources. The Yakama Nation is responsible to pay the costs associated with producing the benefit received.

A primary consideration for the agreement is an allocation of the benefit from the Priest Rapids Project to the Yakama Nation. The financial equivalent of 15 aMW was paid during 2010-2015 less the associated power costs. Per the agreement, the financial benefit will be 10 aMW net of cost of production from 2016 to the remainder of the agreement. The net payments to the Yakama Nation totaled $75,649 and $468,733 during 2016 and 2015, respectively. The agreement expires at the end of the FERC license term (2052). The projected annual cost for this agreement is listed in the table below.

**Estimated Yakama Nation Contractual Payments**
**(AMOUNTS IN THOUSANDS)**

| | | |
|---|---|---|
| 2017 | $ | 671 |
| 2018 | | 465 |
| 2019 | | 497 |
| 2020 | | 628 |
| 2021 | | 678 |
| 2022 | | 843 |

### Other Sources

Pursuant to agreements with three irrigation districts, the District constructed, operates, and maintains both the Quincy Chute and Potholes East Canal hydroelectric generation facilities in return for the right to all output from the projects. The construction costs of Quincy Chute and Potholes East Canal are included in Net utility plant and are being amortized over the terms of the agreements, which expire October 1, 2025, and September 1, 2030, respectively. The irrigation districts hold title to the project facilities.

## 7. NONPOWER COMMITMENTS

### Capital Projects

The District has contractual commitments relating to several Electric System capital improvement projects including electrical system upgrades, multiple transformer purchases, power cable purchases, and substation and distribution line construction projects over the next few years totaling approximately $23.8 million as of December 31, 2016.

The District's improvement programs for the Priest Rapids Project include restoration or replacement of generators, turbine upgrades, construction and upgrades to project support buildings, development of Crescent Bar recreation area, construction and renovation of hatcheries, construction of recreation facilities, supplying GSU transformers and supplying trunnion cylindrical bearings for spillway gates. The District intends to, or has committed by contract to, fulfill these programs, which are projected to be substantially complete by 2026. The contractually committed amount on future Priest Rapids Project work to be performed on these major capital programs is approximately $304.5 million as of December 31, 2016.

### Other Commitments

In 2006, the District entered into a Salmon and Steelhead Settlement Agreement with the United States Department of Interior, the U.S. Fish and Wildlife Service, the National Marine Fisheries Service of the National Oceanic and Atmospheric Administration (NOAA), the Washington Department of Fish and Wildlife, the Yakama Nation, and the Confederated Tribes of the Colville Reservation for the purpose of resolving all issues between the District and the other signatories related to anadromous salmonid fish species. This agreement is intended to constitute a comprehensive and long-term adaptive management program for the protection, mitigation, and enhancement of anadromous fish (both listed and not listed species under the Endangered Species Act) which pass or may be affected by the Priest Rapids Project.

Under the Salmon and Steelhead Settlement Agreement, the District is obligated to establish a habitat conservation account and a no-net-impact fund (referred herein as “Habitat funds”) into which the District deposits payments for further distribution in accordance with the requirements of the Salmon and Steelhead Agreement. The purpose of the Habitat funds are two-fold: (1) to establish and shepherd a habitat restoration program that promotes the rebuilding of self-sustaining and harvestable populations of anadromous species and to mitigate for a portion (2%) of unavoidable losses resulting from the Priest Rapids Project operations and (2) to provide near-term compensation for annual survivals that are less than the survival objectives in the performance standards for the Priest Rapids Project for spring Chinook, steelhead, summer Chinook, and sockeye. The parties that oversee the distribution of these funds include the signatories to the Priest Rapids Salmon and Steelhead Settlement Agreement (U.S. Fish and Wildlife Service, NOAA Fisheries, Washington Department of Fish and Wildlife, Confederated Colville Tribes, Yakama Nation, and the District).

In addition to the Habitat funds discussed above, the District is obligated to establish a habitat account into which the District deposits payments for further distribution in accordance with the requirements of the NOAA Fisheries 2008 Biological Opinion (“2008 BiOp”) for the Priest Rapids Project. Funds from this account are used for habitat actions that directly benefit Upper Columbia River (“UCR”) spring-run Chinook salmon and UCR steelhead. The parties identified above and the Confederated Tribes of the Umatilla Reservation have been identified in the 2008 BiOp as responsible for overseeing distribution of these funds.

The Habitat funds are restricted and cannot be spent without unanimous consent. Interest earned by the Habitat funds increases the balance of these funds and is not recognized as income by the District. Expenditures of these funds are made in accordance with the Salmon and Steelhead Settlement Agreement and the 2008 NOAA Fisheries BiOp for the protection and restoration of habitats along the mainstem and tributaries within the UCR watershed including the Okanogan, Methow, Entiat, and Wenatchee watersheds. The District anticipates funding these accounts up to and through the term of its FERC license.

In October of 2006, the District filed a request for a 401 Water Quality Certification ("401 WQC") from the Washington State Department of Ecology ("Ecology"), pursuant to the provisions of section 401 of the Clean Water Act. A 401 WQC for the operation of the Priest Rapids Project was issued by Ecology on April 3, 2007, and amended on March 6, 2008.

In order to fulfill requirements of the 401 WQC related to native resident fish, the District is required to provide funds to track native resident fish species diversity and provide mitigation for impacts to and loss of resident fish and harvest opportunities by compliance with Parts A and B as described below.

To remain in compliance under Part A ("Hatchery Renovation"), the District is required to provide funds (not to exceed $1.5 million) to renovate the existing Columbia Basin Hatchery facility to ensure stable operations at current capacity for the term of the license. Current capacity is 60,000-70,000 pounds of trout annually, which shall be credited to the District as mitigation for reduced recreational fishing opportunities occurring on native resident fish species. Under Part B ("Resident Fish Monitoring and Trout Purchase"), the District is obligated to establish and administer a fund for resident fish monitoring and fish purchase. Funds from Part B are specifically directed toward the monitoring of native resident fish species within the Priest Rapids Project area. The District is required to make contributions to the fund annually on or before February 15 of each year in the amount of $100,000 per year, based upon 2003 dollars and annually adjusted for inflation.

In a FERC Order (issued on August 31, 2010) approving the Wildlife Habitat Management Plan (Article 409), the District is required to assist the Washington Department of Fish and Wildlife in fire suppression by contributing $40,000 annually to an account. Funds from the account are to be designated for: 1) revegetating burned areas; 2) revegetating areas known to burn frequently with species carrying lesser fuel loads; 3) creating fire breaks in appropriate locations; and 4) paying for firefighting activities.

The District's total contributions to these Habitat funds for the years ended December 31, 2016, and December 31, 2015, equaled $2.6 million and $3.5 million, respectively. These contributions reduced the Licensing obligations, as discussed in Note 4.

The following table shows the District's estimate of the remaining fixed contributions to the Habitat funds as of December 31, 2016, representing required contributions through the FERC License term (2052).

**Estimated Fixed Habitat Funding Commitments**
**(AMOUNTS IN THOUSANDS)**

| | |
|---|---|
| 2017 | $ 2,717 |
| 2018 | 2,762 |
| 2019 | 2,809 |
| 2020 | 1,721 |
| 2021 | 1,750 |
| 2022 and thereafter | 68,516 |
| Total | $ 80,275 |

*Northwest Open Access Network, Inc. D.B.A. NoaNet* – The District withdrew its membership in NoaNet in July of 2014, but remains a participant with respect to certain debt of NoaNet. NoaNet, a Washington non-profit mutual corporation, was established in 2000 and is currently comprised of 9 Washington State Public Utility Districts and Energy Northwest. NoaNet provides a broadband communications backbone, over Public Benefit Fibers leased from BPA, throughout the State of Washington to assist its members in the efficient management of load, conservation, and acquisition of electric energy as well as other purposes.

In 2001, NoaNet issued $27 million in bonds to finance, among other things, the acquisition and construction of necessary facilities and systems. In 2011, NoaNet issued $13.2 million to refund most of the NoaNet 2001 bonds. The Electric System had previously guaranteed the repayment of up to approximately $1.43 million of NoaNet's remaining 2011 bonds. As of December 2016, these bonds were completely paid.

In addition, NoaNet had an outstanding $5 million loan with a commercial lender, of which the District previously guaranteed 17.57% of the outstanding balance in the event of NoaNet's revenues being insufficient. This loan was refinanced in 2016 (subsequent to the District withdrawing its membership in 2014) effectively discharging the District's guarantee.

## 8. PENSION / RETIREMENT PLANS

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

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

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

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

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

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

Industries. PERS 1 members were vested after the completion of five years of eligible service. The plan was closed to new entrants on September 30, 1977.

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

| **PERS Plan 1**<br>**Actual Contribution Rates:** | **Employer** | **Employee** |
|---|---|---|
| PERS Plan 1 | 6.23% | 6.00% |
| PERS Plan 1 UAAL | 4.77% | 6.00% |
| Administrative Fee | 0.18% | |
| Total | 11.18% | 12.00% |

The District's actual contributions to the plan were $2,976,853 and $2,503,192 for the years ended December 31, 2016 and 2015, respectively.

**PERS Plan 2/3** provide 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 nonduty disability payments, a cost-of-living allowance (based on the CPI), capped at three percent annually and a one-time duty related death benefit, if found eligible by the Department of Labor and Industries. PERS 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service if 12 months of that service are earned after age 44.

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

**Contributions**

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

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

The District's actual contributions to the plan were $3,752,850 and $3,025,799 for the years ended December 31, 2016 and 2015, respectively.

### Actuarial Assumptions

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

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

- **Inflation:** 3% total economic inflation; 3.75% salary inflation

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

- Investment rate of return: 7.5%

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

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

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

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

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

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

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

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

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

### Estimated Rates of Return by Asset Class

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

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

### Sensitivity of NPL

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

| (AMOUNTS IN THOUSANDS) | 1% Decrease 6.5% | Current Discount Rate (7.5%) | 1% Increase (8.5%) |
|---|---|---|---|
| PERS 1 | $ 33,996 | $ 28,191 | $ 23,196 |
| PERS 2/3 | 60,264 | 32,731 | (17,038) |

### Pension Plan Fiduciary Net Position

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

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

At June 30, 2016 and 2015, respectively, the District reported a total pension liability of $60,922,127 and $52,760,651 for its proportionate share of the net pension liabilities as follows:

| **Liability (AMOUNTS IN THOUSANDS)** | **2016** | **2015** |
|---|---|---|
| PERS 1 | $ 28,191 | $ 28,490 |
| PERS 2/3 | 32,731 | 24,271 |
| Total | $ 60,922 | $ 52,761 |

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

| | **Proportionate Share 6/30/2015** | **Proportionate Share 6/30/2016** | **Change in Proportion** |
|---|---|---|---|
| PERS 1 | 0.544648% | 0.524928% | -0.019720% |
| PERS 2/3 | 0.679264% | 0.650080% | -0.029184% |

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

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

## Pension Expense

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

| Pension Expenswe (AMOUNTS IN THOUSANDS) | 2016 | 2015 |
|---|---|---|
| PERS 1 | $ 432 | $ (49) |
| PERS 2/3 | 3,893 | 3,042 |
| Total | $ 4,325 | $ 2,993 |

## Deferred Outflows of Resources and Deferred Inflows of Resources

At December 31, 2016 and 2015, respectively, the District recognized deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

| | 2016 | | 2015 | |
|---|---|---|---|---|
| (AMOUNTS IN THOUSANDS) | Deferred Outflows of Resources | Deferred Inflows of Resources | Deferred Outflows of Resources | Deferred Inflows of Resources |
| **PERS Plan 1** | | | | |
| Net difference between projected and actual investment earnings on pension plan investments | $ 710 | $ - | $ - | $ 1,512 |
| Contributions subsequent to measurement date | 1,488 | - | 48 | - |
| Total | $ 2,198 | $ - | $ 48 | $ 1,512 |

| (AMOUNTS IN THOUSANDS) | 2016 Deferred Outflows of Resources | 2016 Deferred Inflows of Resources | 2015 Deferred Outflows of Resources | 2015 Deferred Inflows of Resources |
|---|---|---|---|---|
| **PERS Plan 2/3** | | | | |
| Differences between expected and actual experience | $ 1,743 | $ 1,080 | $ - | $ - |
| Net difference between projected and actual investment earnings on pension plan investments | 4,005 | - | 2,580 | 6,479 |
| Changes of assumptions | 338 | - | 39 | (154) |
| Changes in proportion and differences between contributions and proportionate share of contributions | (1,807) | (154) | (870) | - |
| Contributions subsequent to measurement date | 1,951 | - | 3,207 | - |
| Total | $ 6,230 | $ 926 | $ 4,956 | $ 6,325 |

Deferred outflows of resources related to pensions resulting from the District's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2016.

## 9. POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS ("OPEB")

### Plan Description

The District administers a single-employer defined benefit premium program ("the retiree subsidy plan"). The plan provides a subsidy that covers a portion of healthcare insurance for retirees ages 59½ to 65 and their spouses. The retiree subsidy plan may be amended through collective bargaining (for bargaining unit employees) and ratified by the District's Commission, or changed without bargaining for nonunit employees. The retiree subsidy plan does not issue a publicly available financial report.

### Funding Policy

The District pays a percentage of the medical premiums based upon years of service of the retirees. At the age of 59½, the retiree is eligible for a subsidy of 3% of their premium cost for each year of service up to 30 years (years x 3% x retiree premium). The subsidy cannot be more than the premium amount paid for active employees and is effective until the retiree turns 65. For the years ended December 31, 2016 and 2015, the District paid approximately $142,000 and $188,000 in retiree subsidies, respectively.

### Annual OPEB Cost and Net Obligation

The District's annual OPEB cost (expense) is calculated based on the annual required contribution ("ARC") of the employer. The District's ARC and related information is based upon an actuarial valuation as required by GASB Statement No. 45. As of year-end, the net OPEB obligation represents the cumulative difference in ARC and payments made through the plan since actuarial accounting began in 2007. The following table shows the components of the District's annual OPEB cost for the years ended December 31, 2016 and 2015:

| (AMOUNTS IN THOUSANDS) | 2016 | 2015 |
|---|---|---|
| Normal cost with interest | $ 350 | $ 375 |
| Amortization amount with interest | 194 | 194 |
| Annual required contribution | $ 544 | $ 569 |
| Annual OPEB cost | $ 544 | $ 569 |
| Less: benefit payments | (142) | (188) |
| Increase in net OPEB obligation | 402 | 381 |
| Net OPEB obligation at beginning of year | 2,088 | 1,707 |
| Net OPEB obligation at end of year | $ 2,490 | $ 2,088 |

### Funded Status and Funding Progress

As of December 31, 2016 and 2015, the District's Actuarial Accrued Liability ("AAL") was $6.2 million and $5.8 million, respectively, all of which was unfunded. The District has no plans at this time to fund the obligation using an irrevocable trust. The AAL is being amortized over a 30-year period and the increase in net OPEB obligation is accrued each year and is split between the District systems, based on current labor allocations. For 2016 and 2015, the covered payroll (annual payroll of active employees covered by the plan) was $54 million and $56 million, respectively, and the ratio of the unfunded obligation to the covered payroll was 11.5% and 10.3%, respectively.

The projection of future benefit payments for an ongoing plan involves 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 annual required 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.

### Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of the valuation and the sharing of benefit costs between the employer and plan members in effect at the time of the valuation which was December 31, 2015. The Entry Age Normal method is used to develop an Annual Required Contribution and an Actuarial Accrued Liability. The UAAL amortization was changed to a level percentage of payroll over 30 years instead of a level dollar.

The following are the significant assumptions related to the plan's actuarial liability:

***Retirement age for active employees –*** Based on assumptions used by the Office of the State Actuary in Olympia, Washington but adjusted to reflect expected future rates of retirement based on current experience of the District.
***Mortality –*** Rates of mortality are the same that were used for PERS participants in the June 30, 2015, actuarial valuation published by the Office of the State Actuary.
***Medical trends –*** Premium increases of 7.7% in 2017, decreasing to 5.2% in 2018, and declining percentages in future years. It is assumed that the monthly premium and maximum employer subsidy amounts will increase at a slower rate than future claims in the immediate future.
***Discount rate –*** The discount rate of 3.5% was used in the valuation to reflect expected investment returns. This rate is used because the Plan is "unfunded" and the District's assets would be used to pay benefits.

## 10. CONTINGENCIES

On July 28, 2015, the District's Board of Commissioners approved a settlement that resolves the dispute with Crescent Bar Island residents concerning the use of real property on District land. The settlement allows 80 percent of the Crescent Bar area previously under lease to be made fully available to the public. FERC approved the leases in November of 2016, which have a term from the effective date of December 1, 2016, through April 1, 2052. The District has the right beginning April 1, 2042, to provide five years' written notice to the lessees to notify them of termination (i.e. earliest termination could occur April 1, 2047). The leases require the residents to pay fair-market rent to the District retroactive to 2012 and would also require them to pay for necessary wastewater treatment capital upgrades and fire-safety infrastructure. The settlement does not require any financial payment from the District to the Crescent Bar Island residents.

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

## 11. SUPPLEMENTAL DISCLOSURE OF TELECOMMUNICATION ACTIVITIES

The District is installing a wholesale fiber optic network in its service area. This fiber optic network is interconnected with multiple regional and national telecommunications carriers, including NoaNet's fiber optic network. The wholesale fiber optic network is available to retail providers of Internet, telephone, and video services. The District has also recently implemented a wholesale wireless network which is available to retail wireless providers.

The following is a summary of the results of operations of the wholesale fiber optic and wireless networks, and the related utility plant balances and related additions, as of and for the years ended December 31:

| (AMOUNTS IN THOUSANDS) | 2016 | 2015 |
|---|---|---|
| Operating revenues | | |
| Wholesale fiber services | $ 5,663 | $ 4,972 |
| Dark fiber revenue | 447 | 349 |
| Wireless fiber revenue | 60 | 17 |
| Wholesale fiber optic network sales | $ 6,170 | $ 5,338 |
| Operating expenses | | |
| Administrative and general | $ 276 | $ 443 |
| Repairs and maintenance | 1,049 | 837 |
| Depreciation | 7,049 | 6,483 |
| Total operating expenses | $ 8,374 | $ 7,763 |
| Nonoperating revenues | | |
| Contributions in aid of construction | $ 14 | $ 313 |
| Utility plant | | |
| Additions to utility plant | $ 5,363 | $ 7,082 |
| Utility plant, net of accumulated depreciation | 87,547 | 89,185 |

## 12. EXTRAORDINARY LOSS – WANAPUM FRACTURE

On February 27, 2014, a horizontal fracture was discovered on the upstream side of Wanapum Dam's Spillway Monolith Number 4. The fracture ran the length of the 65-foot-wide monolith and was two inches tall at its widest point. A spillway monolith, and its associated pier, is the structure that supports the spillway gates. There are 13 spillway monoliths and 12 spillway gates at Wanapum Dam. Each monolith is independent of the others. Eleven of the monoliths are 65 feet wide and the two end ones are half monoliths. Wanapum Dam is 8,637 feet wide.

After consulting FERC, the District began to draw down the elevation of the Wanapum reservoir by 26 feet to reduce pressure on the monolith. A survey of the structure on March 4, 2014, showed that the fracture had closed and the monolith was stable. An examination of the upstream face of the dam found no other fractures similar to the fracture found on Monolith No. 4.

Following an 11-week investigation, it was determined that a mathematical error during the pre-construction design of Wanapum Dam was the primary contributing factor to the fracture. When engineers recalculated the original design formulas, they found that additional concrete or reinforced steel should have been included in the construction of Monolith No. 4 and all of the other 12 monoliths on Wanapum Dam. No other mathematical errors were discovered by the experts performing the investigation.

Repair work began within 8 weeks of the discovery of the fracture. The District has repaired the fracture in Monolith No. 4 and anchored all 13 monoliths. Anchoring included installing additional steel reinforcements from the top of the monoliths, through the concrete, and into bedrock below the dam. As of April 1, 2015, all anchors have been installed.

Repairs and additional capital work were completed before the summer recreation season of 2015. During the repair, Wanapum Dam continued to operate and the District continued to meet its obligations with regard to fish passage, flood-control, irrigation, cultural resource protection, public safety, and electric generation. Recreational activities were modified to reflect water elevation and safety and culture concerns. At its lowest levels, Wanapum Dam was capable of generating electricity at between 50 to 60 percent of capacity. As of March 21, 2015, the water level behind Wanapum Dam was restored to a normal operating range of 560 to 571.5 feet above sea level.

The financial impact of the fracture has been manageable for the District. An Extraordinary loss of $21.3 million was recognized in 2014 of which $18 million is associated with repairs and additional operating costs associated with the fracture. The remaining $3.3 million relates to a noncash permanent write down of the original spillway cost to comply with Governmental Accounting Standards Board Statement No. 42 related to asset impairment.

During 2015, the remaining repairs were completed at an additional cost of $7.1 million and insurance proceeds of $2.7 million were received resulting in the extraordinary loss of $4.4 million. During 2016 the District received $10.5 million of insurance proceeds and incurred final clean-up expenses of $0.6 million resulting in the $9.9 million extraordinary gain for the year. The District concluded that expenses incurred related to restoration of the fracture were not a part of the normal life cycle of the dam and therefore met the definition of an extraordinary item as the event was both unusual and infrequent in nature. In order to correct the original design error in the structure incremental capital costs were incurred to properly anchor the dam into the bedrock with additional steel and concrete reinforcements. The total capital expenditures for these structural improvements were $62.4 million. The District does not anticipate any further costs or recoveries related to the fracture

## 13. SEGMENTS

The District has outstanding revenue bonds used to finance the Electric System and the Priest Rapids Project hydroelectric production facilities. As described in Note 5, all the outstanding bond issues, which are on parity with each other, are secured by a pledge of the net revenues of the District. The Electric System has committed to cover, without limitation, any costs incurred by the Priest Rapids Project that are not covered by purchasers other than the District.

Each system has an external requirement to be accounted for separately. The following condensed financial statements of the operating segments of the District include the Electric System and the Priest Rapids Project. The District's Service System, as well as eliminating internal transactions, is presented as "Other" in order to reconcile to the combined District's results. "Other" is not considered a segment of the District.

**CONDENSED STATEMENT OF NET POSITION**

| (AMOUNTS IN THOUSANDS) | Electric System | Priest Rapids Project | Other | Total |
|---|---|---|---|---|
| ASSETS | | | | |
| Current assets | $ 174,269 | $ 114,520 | $ (66,394) | $ 222,395 |
| Net utility plant | 571,248 | 1,382,380 | - | 1,953,628 |
| Noncurrent | 285,619 | 197,658 | (72,971) | 410,306 |
| TOTAL ASSETS | 1,031,136 | 1,694,558 | (139,365) | 2,586,329 |
| Deferred outflows of resources | 19,920 | 10,307 | (16,432) | 13,795 |
| TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | $ 1,051,056 | $ 1,704,865 | $ (155,797) | $ 2,600,124 |
| LIABILITIES | | | | |
| Current | $ 50,675 | $ 122,762 | $ (22,349) | $ 151,088 |
| Noncurrent | 277,664 | 1,289,680 | (116,989) | 1,450,355 |
| TOTAL LIABILITIES | 328,339 | 1,412,442 | (139,338) | 1,601,443 |
| Deferred Inflows of resources | 375 | 16,984 | (16,433) | 926 |
| TOTAL LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | 328,714 | 1,429,426 | (155,771) | 1,602,369 |
| NET POSITION | | | | |
| Net investment in capital assets | 336,417 | 184,089 | 118,014 | 638,520 |
| Restricted | 20,317 | 138,401 | 1,832 | 160,550 |
| Unrestricted | 365,608 | (47,051) | (119,872) | 198,685 |
| TOTAL NET POSITION | 722,342 | 275,439 | (26) | 997,755 |
| TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND NET POSITION | $ 1,051,056 | $ 1,704,865 | $ (155,797) | $ 2,600,124 |

(Internal transactions are eliminated based on Generally Accepted Accounting Principles)

**SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET POSITION**

| (AMOUNTS IN THOUSANDS) | Electric System | Priest Rapids Project | Other | Total |
|---|---|---|---|---|
| OPERATING REVENUES | $ 246,315 | $ 148,397 | $ (108,396) | $ 286,316 |
| OPERATING EXPENSES | | | | |
| Depreciation and amortization | 33,614 | 28,342 | - | 61,956 |
| Other operating expenses | 158,997 | 75,017 | (108,396) | 125,618 |
| Total operating expenses | 192,611 | 103,359 | (108,396) | 187,574 |
| NET OPERATING INCOME | 53,704 | 45,038 | - | 98,742 |
| OTHER REVENUES (EXPENSES) | | | | |
| Interest and other income | 7,561 | 5,887 | (3,440) | 10,008 |
| Interest on revenue bonds and other, net of capitalized interest | (7,654) | (52,357) | 3,542 | (56,469) |
| Federal rebates on revenue bonds | - | 10,545 | - | 10,545 |
| Amortization of debt discount/premium | 1,332 | 3,860 | (98) | 5,094 |
| Cost of debt issuance | (167) | (28) | - | (195) |
| Total other revenues (expenses) | 1,072 | (32,093) | 4 | (31,017) |
| CONTRIBUTIONS IN AID OF CONSTRUCTION | 4,603 | - | - | 4,603 |
| EXTRAORDINARY LOSS - WANAPUM FRACTURE | - | 9,896 | - | 9,896 |
| CHANGE IN NET POSITION | 59,379 | 22,841 | 4 | 82,224 |
| NET POSITION | | | | |
| Beginning of year | 662,963 | 252,598 | (30) | 915,531 |
| End of year | $ 722,342 | $ 275,439 | $ (26) | $ 997,755 |

(Internal transactions are eliminated based on Generally Accepted Accounting Principles)

**CONDENSED SCHEDULE OF CASH FLOWS**

| (AMOUNTS IN THOUSANDS) | Electric System | Priest Rapids Project | Other | Total |
|---|---|---|---|---|
| Net cash provided by operating activities | $ 88,088 | $ 90,604 | $ 2,774 | $ 181,466 |
| Net cash provided by (used) in capital and related financing activities | 12,425 | (119,457) | (32,755) | (139,787) |
| Net cash (used in) provided by investing activities | (97,350) | 62,197 | 29,413 | (5,740) |
| NET INCREASE (DECREASE) IN CASH | $ 3,163 | $ 33,344 | $ (568) | $ 35,939 |
| CASH AT END OF YEAR | $ 4,085 | $ 39,722 | $ (1,088) | $ 42,719 |
| CASH AT BEGINNING OF YEAR | 923 | 6,378 | (521) | 6,780 |
| NET INCREASE (DECREASE) IN CASH | $ 3,162 | $ 33,344 | $ (567) | $ 35,939 |

**CONDENSED STATEMENT OF NET POSITION**

| (AMOUNTS IN THOUSANDS) | Electric System | Priest Rapids Project | Other | Total |
|---|---|---|---|---|
| ASSETS | | | | |
| Current assets | $ 113,854 | $ 85,585 | $ (12,298) | $ 187,141 |
| Net utility plant | 557,598 | 1,323,667 | - | 1,881,265 |
| Noncurrent | 244,487 | 231,013 | (73,282) | 402,218 |
| TOTAL ASSETS | 915,939 | 1,640,265 | (85,580) | 2,470,624 |
| Deferred outflows of resources | 2,288 | 9,234 | - | 11,522 |
| TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | $ 918,227 | $ 1,649,499 | $ (85,580) | $ 2,482,146 |
| LIABILITIES | | | | |
| Current | $ 26,045 | $ 105,171 | $ (2,779) | $ 128,437 |
| Noncurrent | 226,014 | 1,287,098 | (82,771) | 1,430,341 |
| TOTAL LIABILITIES | 252,059 | 1,392,269 | (85,550) | 1,558,778 |
| Deferred inflows of resources | 3,205 | 4,632 | - | 7,837 |
| TOTAL LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | 255,264 | 1,396,901 | (85,550) | 1,566,615 |
| NET POSITION | | | | |
| Net investment in capital assets | 362,497 | 167,577 | 83,791 | 613,865 |
| Restricted | 20,055 | 125,561 | 1,089 | 146,705 |
| Unrestricted | 280,411 | (40,540) | (84,910) | 154,961 |
| TOTAL NET POSITION | 662,963 | 252,598 | (30) | 915,531 |
| TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND NET POSITION | $ 918,227 | $ 1,649,499 | $ (85,580) | $ 2,482,146 |

(Internal transactions are eliminated based on Generally Accepted Accounting Principles)

**SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET POSITION**

| (AMOUNTS IN THOUSANDS) | Electric System | Priest Rapids Project | Other | Total |
|---|---|---|---|---|
| OPERATING REVENUES | $ 262,086 | $ 156,587 | $ (105,504) | $ 313,169 |
| OPERATING EXPENSES | | | | |
| Depreciation and amortization | 32,242 | 24,743 | - | 56,985 |
| Other operating expenses | 191,072 | 74,524 | (105,504) | 160,092 |
| Total operating expenses | 223,314 | 99,267 | (105,504) | 217,077 |
| NET OPERATING INCOME | 38,772 | 57,320 | - | 96,092 |
| OTHER REVENUES (EXPENSES) | | | | |
| Interest and other income | 4,349 | 2,190 | (1,939) | 4,600 |
| Interest on revenue bonds and other, net of capitalized interest | (6,206) | (43,283) | 1,934 | (47,555) |
| Federal rebates on revenue bonds | - | 8,214 | - | 8,214 |
| Amortization of debt expense, discount, and premium | 1,163 | 3,296 | (9) | 4,450 |
| Cost of debt issuance | (7) | (1,270) | - | (1,277) |
| Total other revenues (expenses) | (701) | (30,853) | (14) | (31,568) |
| CONTRIBUTIONS IN AID OF CONSTRUCTION | 13,222 | - | - | 13,222 |
| EXTRAORDINARY LOSS - WANAPUM FRACTURE | - | (4,359) | - | (4,359) |
| CHANGE IN NET POSITION | 51,293 | 22,108 | (14) | 73,387 |
| NET POSITION | | | | |
| Beginning of year | 611,670 | 230,490 | (16) | 842,144 |
| End of year | $ 662,963 | $ 252,598 | $ (30) | $ 915,531 |

(Internal transactions are eliminated based on Generally Accepted Accounting Principles)

**CONDENSED SCHEDULE OF CASH FLOWS**

| (AMOUNTS IN THOUSANDS) | Electric System | Priest Rapids Project | Other | Total |
|---|---|---|---|---|
| Net cash provided by operating activities | $ 45,487 | $ 106,081 | $ (13,392) | $ 138,176 |
| Net cash used in capital and related financing activities | (34,923) | (46,618) | (32,559) | (114,100) |
| Net cash (used in) provided by investing activities | (13,308) | (55,830) | 44,219 | (24,919) |
| NET (DECREASE) INCREASE IN CASH | $ (2,744) | $ 3,633 | $ (1,732) | $ (843) |
| CASH AT END OF YEAR | $ 923 | $ 6,378 | $ (521) | $ 6,780 |
| CASH AT BEGINNING OF YEAR | 3,667 | 2,745 | 1,211 | 7,623 |
| NET (DECREASE) INCREASE IN CASH | $ (2,744) | $ 3,633 | $ (1,732) | $ (843) |

# PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

## REQUIRED SUPPLEMENTARY INFORMATION (UNAUDITED)
## FOR THE YEAR ENDED DECEMBER 31, 2016

**Schedule of the District's Proportionate Share of the Net Pension Liability**
**(AMOUNTS IN THOUSANDS)**

| | PERS 1 | | PERS 2/3 | |
|---|---|---|---|---|
| | **2016** | **2015** | **2015** | **2015** |
| **Measurement Date Ended June 30** | | | | |
| Proportion of the net pension liability | 0.524928% | 0.544648% | 0.650080% | 0.679264% |
| Proportionate share of the net pension liability | $ 28,191 | $ 28,490 | $ 32,731 | $ 24,271 |
| Covered-employee payroll | 913 | 956 | 58,869 | 60,273 |
| Proportionate share of the net pension liability as a percentage of its covered-employee payroll | 3087.73% | 2980.13% | 55.60% | 40.27% |

**Schedule of the District's Contributions**

**(AMOUNTS IN THOUSANDS)**

| | PERS 1 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Fiscal Year Ended June 30** | **2016** | **2015** | **2014** | **2013** | **2012** | **2011** | **2010** | **2009** | **2008** | **2007** |
| Contractually Required Contribution | $ 102 | $ 86 | $ 114 | $ 112 | $ 163 | $ 128 | $ 164 | $ 267 | $ 211 | $ 185 |
| Contributions in Relation to the Contractually Required Contribution Subtotal | (102) | (86) | (114) | (112) | (163) | (128) | (164) | (267) | (211) | (185) |
| Contribution Deficiency (Excess) | $ - | $ - | $ - | $ - | $ - | $ - | $ - | $ - | $ - | $ - |
| Covered-Employee Payroll | $ 913 | $ 956 | $ 1,277 | $ 1,586 | $ 2,382 | $ 2,578 | $ 3,398 | $ 3,693 | $ 3,889 | $ 4,768 |
| Contributions as a Percentage of covered Employee Payroll | 11.17% | 9.00% | 8.93% | 7.06% | 6.84% | 4.97% | 4.83% | 7.23% | 5.43% | 3.88% |

| | PERS 2/3 | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Fiscal Year Ended June 30** | **2016** | **2015** | **2014** | **2013** | **2012** | **2011** | **2010** | **2009** | **2008** | **2007** |
| Contractually Required Contribution | $ 3,685 | $ 3,026 | $ 2,984 | $ 2,756 | $ 3,923 | $ 3,001 | $ 2,934 | $ 4,200 | $ 2,824 | $ 1,952 |
| Contributions in Relation to the Contractually Required Contribution Subtotal | (3,685) | (3,026) | (2,984) | (2,756) | (3,923) | (3,001) | (2,934) | (4,200) | (2,824) | (1,952) |
| Contribution Deficiency (Excess) | $ - | $ - | $ - | $ - | $ - | $ - | $ - | $ - | $ - | $ - |
| Covered-Employee Payroll | $ 58,869 | $ 60,273 | $ 60,446 | $ 58,703 | $ 55,948 | $ 58,289 | $ 55,851 | $ 52,138 | $ 47,568 | $ 45,655 |
| Contributions as a Percentage of covered Employee Payroll | 6.26% | 5.02% | 4.94% | 4.69% | 7.01% | 5.15% | 5.25% | 8.06% | 5.94% | 4.28% |
| PERS Plan 1 UAAL* | $ 2,898 | $ 2,417 | $ 2,428 | $ 1,383 | $ - | $ - | $ - | $ - | $ - | $ - |

**Notes to Schedules**

Grant County PUD #2 implemented GASB 68 for the year ended June 30, 2015.

*DRS allocates a certain portion of contributions from PERS Plan 2/3 to PERS Plan 1 in order to fund its unfunded actuarial accrued liability (UAAL)

**Schedule of Funding Progress for Postretirement Health Benefits Program**

**(AMOUNTS IN THOUSANDS)**

| Fiscal Year Ended | Actuarial Value of Assets | Actuarial Accrued Liability | Unfunded Actuarial Accrued Liabilities (UAAL) | Funded Ratio Ratio |
|---|---|---|---|---|
| 12/31/2009 | $ - | $ 5,182 | $ 5,182 | 0% |
| 12/31/2011 | - | 4,168 | 4,168 | 0% |
| 12/31/2013 | - | 4,127 | 4,127 | 0% |
| 12/31/2015 | - | 5,808 | 5,808 | 0% |


TEREX

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**PUBLIC UTILITY DISTRICT**

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