Grant County
PUBLIC UTILITY DISTRICT

2014 Annual Report

GRANT COUNTY PUBLIC UTILITY DISTRICT NO. 2

Grant County
PUBLIC UTILITY DISTRICT

2014 | Annual Report letter from the Board

In 2014, Grant PUD dealt with one of the greatest challenges in our 76-year history when a fracture was discovered on the Wanapum Dam Spillway. We were suddenly presented with a number of problems to be solved quickly. We worked to resolve the issues created by the spillway fracture, while also fulfilling our core mission of generating and delivering low-cost, reliable energy for our customers.

While the Wanapum Spillway Response was our top priority in 2014, it was by no means our only accomplishment. In 2014 we improved fish passage in the Priest Rapids Project by making significant progress on a number of hatchery and acclimation facilities as well as improvements installing a new juvenile bypass unit and preparing for new advanced turbines at Priest Rapids Dam. We also made significant progress on a number of recreation improvements along our project lands to fulfill the requirements of our federal operating license. In the same year, we made several important upgrades to our electrical system.

While these large-scale projects are all important to record, it is imperative to point to the day-to-day contributions and expertise of our workers. Grant PUD employees went above and beyond in their response to the Wanapum Spillway. At the same time, they ensured our utility accomplished the thousands of routine tasks required for our mission. Their efforts allowed us to continue to provide outstanding service to our customers while we quickly addressed the emergency associated with the fracture. We believe the Grant PUD team provided the industry with an example of how to respond to an unprecedented crisis on the Columbia River.

We first became aware of the issue with the Wanapum Dam Spillway on February 24 when a worker at the dam noticed some irregular movement on one of the spillway's 13 monoliths. Three days later, a dive team discovered a fracture running along the 65-foot base of monolith No. 4. The fracture had opened by two inches at its widest point. Working with the Federal Energy Regulatory Commission, we reduced the pressure on the monolith by lowering the reservoir behind Wanapum Dam by 26 feet. This drawdown stabilized the monolith so we could begin repairs to the structure, but it also caused a number of concerns that had to be mitigated.

The most pressing concern was upstream fish passage. The lowered reservoir level left Wanapum Dam's fish ladders inoperable, just six weeks from the start of the ESA-listed adult spring Chinook salmon migration. Working with stakeholders, we successfully modified our fish ladders in time to pass a record 800,000 fish during the 2014 upstream migration season.

We also preserved the rich cultural heritage of the reservoir and protected public safety through an emergency closure of the 75 miles of shoreline on the Wanapum Reservoir. During the drawdown, our staff worked to help irrigators affected by the low-water levels to successfully obtain the

ADDRESS PO Box 878
Ephrata, WA 98823
PHONE 509 766 2505
FAX 509 754 6770
grantpud.org

permits they needed to modify their systems. We also used the low water situation to help us prepare for the 2015 recreation season, by accelerating improvements scheduled to boating facilities on the river. Doing the work in the dry conditions reduced environmental impacts and costs. It is significant to note that we continued to safely operate Wanapum Dam, by generating electricity – at a reduced rate – and accommodating river flows, through the entirety of our spillway response.

In December of 2014, we accomplished the necessary work to stabilize the spillway, allowing us to raise the reservoir by 17 feet. We continued with restoration work in early 2015 and then completely refilled the reservoir in March 2015. We expect the work to be completely finished by mid-year of 2015.

The capital expenses and operations and maintenance costs associated with the response to the Wanapum Spillway are estimated at $78.5 million. While this is an unexpected expense, Grant PUD's financial position is strong enough that we will not have to adjust the rate trajectory we adopted in 2013. We are also grateful that our prudent financial practices were affirmed once again with an AA/Stable credit rating from Fitch and S&P, and an Aa3/Stable credit rating from Moody's. These credit ratings provide a savings to our customers in the form of reduced borrowing costs for necessary capital work.

As we reflect on 2014, we are thankful to support a team at Grant PUD that works daily to give their best to those who rely on our services. From our power customers, to the public who has a stake in fish passage and recreation on our project lands, to those who use our high speed communications network, we are committed to providing them with reliable and affordable service for years to come. The challenges of the past reinforce the importance of our work and how it benefits millions of individuals depending on us to deliver in our mission.

While the difficulties of 2014 were nothing that a utility would wish for, we are hopeful that we will use the experiences gained in the past year to propel us toward an even better future.

Sincerely,

Grant PUD Board of Commissioners:
President – Dale Walker
Vice-President – Tom Flint
Secretary – Larry Schaapman
Commissioner – Terry Brewer
Commissioner – Bob Bernd

ADDRESS PO Box 878
Ephrata, WA 98823
PHONE 509 766 2505
FAX 509 754 6770
grantpud.org

Public Utility District No. 2 of Grant County, Washington
Financial Statements
December 31, 2014 and 2013

Independent Auditor's Report

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, 2014 and December 31, 2013, and the related statements of revenues and expenses and changes in net position, cash flows and the related notes to the financial statements for the years then ended.

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.

Auditor's 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 the District at December 31, 2014 and December 31, 2013, 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.

PricewaterhouseCoopers LLP, 805 SW Broadway, Suite 800, Portland, OR 97205-3344
T: (971) 544 4000, F: (971) 544 4100, www.pwc.com/us

Other Matters

The accompanying management's discussion and analysis on pages 3 through 10 are required by accounting principles generally accepted in the United States of America to supplement the basic financial statements. Such information, although not 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 the appropriate operational, economic, or historic 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.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements referred to above. 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 24, 2015

As of December 31, 2014, 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, 2014, 2013, and 2012. Please read it in conjunction with the financial statements, which follow this section.

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, 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.

FINANCIAL HIGHLIGHTS

In February of 2014, a fracture was discovered on the upstream side of Wanapum Dam's Spillway. 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. The reservoir behind Wanapum Dam was lowered for much of 2014 and has been fully restored as of March of 2015. Details of the fracture and the course of action the District followed are discussed in Note 12 of the financial statements.

In October of 2014, the District issued $204.2 million of revenue and refunding bonds, at a net premium of $23.8 million, 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 $119.8 million resulted in a net present value savings of $15.4 million. In November of 2014, the District issued $50 million of revenue bonds associated with the Electric System to finance improvements in the Electric system and to pay issuance costs. In August of 2013, the District issued $100.1 million of revenue bonds, at a net premium of $1.2 million, associated with the Priest Rapids Project to finance improvements at the Priest Rapids Project, to pay issuance costs, and to fund a debt service reserve. In September of 2013, the District issued $67.6 million of revenue refunding bonds, at a net premium of $815 thousand, associated with the Electric System to refund certain bonds previously issued, to pay issuance costs, and to fund a debt service reserve. This refunding allowed the District to restructure debt service so as to obtain a closer alignment and a more fair allocation between the costs of the electric system assets being financed and the enjoyment of the benefits derived from said assets over their useful lives. The debt restructuring was accompanied by moderate retail electric rate increases into the foreseeable future. In May of 2012, the District issued $127.6 million of revenue and refunding bonds, at a net premium of $11.7 million, associated with the Priest Rapids Project to finance improvements at the Priest Rapids Project, to refund certain bonds previously issued, to pay issuance costs, and to fund a debt service reserve. The District had revenue bonds outstanding of $1.25 billion as of December 31, 2014, $1.15 billion as of December 31, 2013, and $1.08 billion as of December 31, 2012. See Note 5.

The Commission implemented rate increases to retail customers in January of 2012, January of 2013, January of 2014, and January of 2015 in the amounts of 8%, 6%, 2%, and 2% respectively. The Commission-adopted budget and forecast has future overall 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.

The Priest Rapids Power Sales Contracts with 17 regional utilities extend to 2052. Each power purchaser is obligated to make payments equal to annual power costs, which include all operating expenses and debt service on the Parity Bonds and debt service coverage less any interest earnings multiplied by the percentage of output or revenue, as applicable, that the purchaser is entitled to that year. In accordance with the FERC Order in the Public Law 83-544 proceeding, the District dedicates 30% of the combined output of the Priest Rapids Project for sales based on market principles. The power purchasers are entitled to receive the net revenues from the sale of the 30% portion to the extent the District does not need the revenues to purchase power to meet the Electric System's firm loads. Since November 1, 2005, the District has been able to meet all of its forecasted firm load requirements with Priest Rapids and Wanapum generation and other benefits derived from the Priest Rapids Project.

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. 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 2019. 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%.

The District completed the long-term turbine upgrade project at Wanapum Dam. In October of 2013, the tenth and final turbine and fourth generator were commissioned and began generating power. The fifth generator was placed in service in June of 2014. In February of 2012, the eighth turbine and second generator were completed. In December of 2012, the ninth turbine and third generator were completed. As of December 31, 2014, the cost of the remaining Wanapum generators to be replaced is estimated at $66.4 million.

In addition to the Wanapum turbine and generator replacement project, the District is initiating 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. On-site work at the Priest Rapids Development is expected to begin in 2016 and be completed by 2026.

In an effort to increase net revenue stability by improving the predictability of wholesale revenues, the District entered into contracts to sell a portion of the Electric System's share from the Priest Rapids Project (PRP) to Iberdrola Renewables, Inc. (Iberdrola) and Shell Energy North America (U.S.), L.P. (Shell). The $104.4 million Iberdrola contract for 12% of PRP output was effective December 1, 2011, and terminated November 30, 2014. The District entered into an additional $20.3 million contract with Iberdrola to extend the 12% slice from December 1, 2014, to June 30, 2015. In January of 2015, the District entered into an $83.1 million agreement with Iberdrola for a 10% slice of PRP from July 1, 2015, to June 30, 2018. The $102.4 million Shell contract for 10% of PRP output was effective July 1, 2013, and terminates June 30, 2016. These contracts are paid in equal monthly installments over the life of the agreement. The District regularly monitors its exposure with Iberdrola and Shell and retains the right to call for additional assurances at any time. The District has the right to curtail delivery in the event of non-payment.

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.

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 1,130,000 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, 2014, the Priest Rapids Project provided 7,755,280 megawatt hours ("MWh") of electric energy at an average cost of $21.61 per MWh. During the year ended December 31, 2013, the Priest Rapids Project provided 8,945,411 MWh of electric energy at an average cost of $16.31 per MWh. During the year ended December 31, 2012, the Priest Rapids Project provided 8,747,538 MWh of electric energy at an average cost of $15.47 per MWh.

The timing of the runoff and spill requirements factor into the water available for generation from year to year. Runoff was 103%, 103% and 120% of average for 2014, 2013 and 2012, respectively. While operating costs have remained generally consistent, the change in average costs per MWh at the Priest Rapids Project from 2012 to 2013 was driven primarily by runoff water available for generation. The fracture of Wanapum spillway discovered in February of 2014 is estimated to have affected generation net of encroachment by 460,000 MWh for 2014. The resulting $18.0 million in extraordinary costs associated with the repair of the spillway and decreased generation resulted in the increased average cost per MWh.

CONDENSED COMPARATIVE FINANCIAL INFORMATION

(AMOUNTS IN THOUSANDS)

Statements of Net Position	**2014**	**2013**	**2012 ***
Assets			
Current	$ 185,986	$ 266,417	$ 228,113
Net utility plant	1,804,711	1,689,361	1,515,539
Noncurrent	374,270	238,845	299,213
Total assets	$ 2,364,967	$ 2,194,623	$ 2,042,865
Deferred outflows of resources	7,616	7,334	7,753
Total assets and deferred outflows of resources	$ 2,372,583	$ 2,201,957	$ 2,050,618
Liabilities			
Current	$ 146,246	$ 150,413	$ 142,025
Noncurrent	1,324,517	1,201,579	1,125,344
Total liabilities	1,470,763	1,351,992	1,267,369
Net position			
Invested in capital assets, net of related debt	578,648	530,428	522,650
Restricted	134,619	107,456	95,051
Unrestricted	188,553	212,081	165,548
Total net position	901,820	849,965	783,249
Total liabilities and net position	$ 2,372,583	$ 2,201,957	$ 2,050,618
Revenues and Expenses and Changes in Net Position			
Operating revenues	$ 308,665	$ 290,427	$ 263,252
Operating expenses	228,648	201,509	176,267
Net operating income	80,017	88,918	86,985
Other revenues (expenses)	(29,660)	(34,168)	(37,531)
Contributions in aid of construction	22,767	11,966	3,848
Extraordinary loss - Wanapum fracture	(21,269)	-	-
Change in net position	$ 51,855	$ 66,716	$ 53,302

* The District's 2012 Statements of Net Position and Statements of Revenues and Expenses and Changes in Net Position were updated for the impacts of the required retroactive implementation of GASB Statement No. 65, "Items Previously Reported as Assets and Liabilities," which became effective for the District in 2013.

FINANCIAL ANALYSIS

The following discussion provides comparative financial information for the years ended December 31, 2014, 2013, and 2012. The year 2012 has been restated to reflect changes in accounting principles per GASB 65.

ASSETS

Current assets from 2012 to 2014 have fluctuated 18%. Materials, supplies and receivables have remained consistent. The majority of the decrease is due to decrease in cash and investments reflective of a move to optimize return by investing in longer term instruments.

Net plant increased 11% from 2012 to 2013 and 7% from 2013 to 2014. These increases reflect the substantial investment in plant in the Electric System, the continued investments in the turbines and generators at Wanapum, and other capital improvements in both systems.

Noncurrent assets have increased 25% between 2012 and 2014. The ebbs and flows of the non-current assets balance are driven primarily by unspent bond proceeds and the movement of short-term investments to long-term investments so as to maintain portfolio balance. Since these proceeds are reserved for construction of plant assets, the timing of bond issues and the subsequent transition to net plant affects the balance from year to year.

Deferred outflows represent the unamortized loss on refunding of debt. These balances have remained fairly static.

LIABILITIES

The District had approximately $1.25 billion, $1.15 billion, and $1.1 billion in bonded debt for the years ended December 31, 2014, 2013, and 2012, respectively. 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. In August of 2013, the District issued bonds to finance capital improvements for the Priest Rapids Project. The total par value of the bond offering was $100.1 million. The bonds were issued at fixed interest rates at an initial offering premium of $1.2 million. In September of 2013, the District issued $67.6 million in Electric System revenue refunding bonds to retire $56.8 million of 2011-I revenue and refunding bonds. The 2013 Electric System bonds were issued at fixed interest rates at a net original issue premium of $815 thousand. This refunding allowed the District to restructure debt service to moderate retail electric rate increases in the foreseeable future. In May of 2012, the District issued bonds to finance capital improvements for the Priest Rapids Project. The total par value of the bond offering was $127.6 million, of which $94.1 million was used to refund prior bond issues. The 2012 bonds were issued at fixed interest rates at a net original issue premium of $11.7

million. The 2012 Priest Rapids Project issue was an opportunity for the District to issue the $42.4 million remaining of its Clean Renewable Energy Bond allocation. The bonds have an authorized 70% refund from the Federal Government on interest payments made.

In August of 2013, Standard and Poor's raised its long-term rating and underlying rating to AA/stable from AA-/stable for the Electric System, Priest Rapids, Wanapum, and the Priest Rapids Project System's bonds and reaffirmed that rating in October of 2014. The previous rating had been in effect since March of 2010. The rationale for the raise included very strong operations, strong availability, extremely low production costs, and improved liquidity for the Priest Rapids Project and the Electric System's benefit from increasing industrial loads, willingness to increase rates, an extremely low-cost power supply, lack of additional debt needs, and strong financial and risk management practices. In October of 2014, Fitch Ratings reaffirmed their AA/stable rating which has been in effect since 2005 on all District bonds based on low-cost power, ample generation capacity, favorable risk-management practices, and cash reserves to manage volatility. In the same month, Moody's reaffirmed their Aa3/stable rating which has been in effect since 2010 on all District bonds citing competitive hydro generation, low retail rates, strong liquidity, and forecasted financial performance.

NET POSITION

Net position increased by $51.8 million, $66.7 million, and $53.3 million in 2014, 2013, and 2012, respectively. This is reflective of ample generation and surplus power sales due largely to above average river flows of 103% of average for 2013 and 120% for 2012. The District was able to make 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 is 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.

STATEMENT OF REVENUES AND EXPENSES

Sales to power purchasers at cost is directly tied to power costs (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.

Retail energy sales and Sales to other utilities revenues, on the other hand, 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 2013 to 2014 is the effect of the rate increases and growth in consumption especially in industrial customers. The increase in operating revenues from 2012 to 2013 is primarily due to the retail rate increase and the $20 million increase in Sales to other utilities, much of which is attributed to the slice sale to Shell Energy which was in place for the last six months of 2013. Operating expenses increased by $27 million between 2013 and 2014, of which $22 million of this increase was in the area of Purchased power part of which is attributable to the need to cover lost generation resulting from the Wanapum Fracture.

Operating expenses increased from 2012 to 2013 by $25 million, of which $12 million of this increase is related to Purchased Power. This increase was expected and generally relates to covering the slice sales related to Shell Energy and Iberdrola which help to reduce water risk and wholesale market price exposure for the District. Other operating expense increases included distribution, administrative and general, license compliance, depreciation and amortization, and taxes ranging from 5% to 15% increase from 2012.

Most components of Other revenues (expenses) remained flat from 2012 to 2014 with the exception of Interest and Other income which has risen substantially because of improved investment strategy and stronger market conditions.

Contributions In Aid of Construction ("CIAC") for 2014 and 2013 were $22.8 million and $12.0 million, respectively, with SGL Automotive and Microsoft making up the majority of the contributions.

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, 2014 AND 2013
(AMOUNTS IN THOUSANDS)

ASSETS	2014	2013
CURRENT ASSETS		
Cash	$ 2,123	$ 15,227
Investments	65,812	146,766
Restricted funds		
Cash	3,901	8,450
Investments	68,691	56,941
Customer accounts receivable, net of allowance for uncollectible accounts	21,369	18,431
Materials and supplies	17,835	18,880
Due from power purchasers	4,430	-
Other current assets	1,825	1,722
Total current assets	185,986	266,417
NONCURRENT ASSETS		
Investments	122,473	56,228
Restricted funds		
Cash	1,599	9,353
Investments	246,401	168,627
Conservation loans	658	722
Demand-side management	1,804	2,563
Preliminary expenses	1,335	1,352
Total other noncurrent assets	374,270	238,845
Utility plant, net of accumulated depreciation and amortization	1,804,711	1,689,361
Total noncurrent assets	2,178,981	1,928,206
TOTAL ASSETS	2,364,967	2,194,623
DEFERRED OUTFLOWS OF RESOURCES	7,616	7,334
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	$ 2,372,583	$ 2,201,957

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, 2014 AND 2013
(AMOUNTS IN THOUSANDS)

LIABILITIES AND NET POSITION	2014	2013
CURRENT LIABILITIES		
Accounts payable		
Trade	$ 45,084	$ 30,654
Wages payable	12,391	12,509
Power purchasers	-	845
Accrued taxes	5,739	5,627
Customer deposits	9,853	11,521
Accrued bond interest	26,687	27,770
Unearned revenue	1,317	11
Habitat liability	12,264	12,417
Other current liabilities	39	10,324
Current portion of licensing obligations	3,402	3,445
Current portion of long-term debt	29,470	35,290
Total current liabilities	146,246	150,413
NONCURRENT LIABILITIES		
Accrued other postemployment benefits	1,707	1,472
Long-term unearned revenue	1,179	1,286
Licensing obligations, less current portion	53,748	54,350
Revenue bonds, less current portion	1,222,305	1,117,450
Unamortized (discount) premium, net	45,578	27,021
Total noncurrent liabilities	1,324,517	1,201,579
Total liabilities	1,470,763	1,351,992
NET POSITION		
Invested in capital assets, net of related debt	578,648	530,428
Restricted	134,619	107,456
Unrestricted	188,553	212,081
Total net position	901,820	849,965
TOTAL LIABILITIES AND NET POSITION	$ 2,372,583	$ 2,201,957

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
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(AMOUNTS IN THOUSANDS)

	2014	2013
OPERATING REVENUES		
Sales to power purchasers at cost	$ 61,099	$ 55,641
Retail energy sales		
Residential	39,845	39,491
Irrigation	23,026	20,873
Commercial and industrial	95,769	88,107
Governmental and others	1,034	1,033
Sales to other utilities	81,078	79,363
Wholesale fiber optic network sales	5,101	4,404
Other	1,713	1,515
Total operating revenues	308,665	290,427
OPERATING EXPENSES		
Purchased power	52,663	30,634
Generation	25,531	23,384
Transmission	6,905	7,924
Distribution	14,625	15,272
Customer and information services	7,110	7,318
Wholesale fiber optic network operations	1,298	1,470
Administrative and general	30,564	30,591
License compliance and related agreements	22,277	20,711
Depreciation and amortization	53,896	50,474
Taxes	13,779	13,731
Total operating expenses	228,648	201,509
NET OPERATING INCOME	80,017	88,918
OTHER REVENUES (EXPENSES)		
Interest and other income	7,432	(236)
Interest on revenue bonds and other, net of capitalized interest	(46,125)	(43,796)
Federal rebates on revenue bonds	7,770	7,712
Amortization of debt discount/premium	3,078	3,559
Cost of debt issuance	(1,815)	(1,407)
Total other revenues (expenses)	(29,660)	(34,168)
CONTRIBUTIONS IN AID OF CONSTRUCTION	22,767	11,966
EXTRAORDINARY LOSS - WANAPUM FRACTURE	(21,269)	-
CHANGE IN NET POSITION	51,855	66,716
NET POSITION		
Beginning of year	849,965	783,249
End of year	$ 901,820	$ 849,965

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

PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(AMOUNTS IN THOUSANDS)

	TWELVE MONTHS ENDED DECEMBER 31, 2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from retail energy sales	$ 158,616	$ 148,135
Cash received from sales to power purchasers at cost	44,051	51,091
Cash received from sales to other utilities	78,506	83,471
Other cash receipts	6,622	5,605
Cash (paid) received for customer deposits	(1,632)	7,654
Cash paid for purchase of power	(40,662)	(24,725)
Cash paid to contractors, suppliers, and employees	(99,420)	(97,911)
Taxes paid	(13,677)	(13,457)
Cash paid out for extraordinary loss	(17,947)	-
Net cash provided by operating activities	114,457	159,863
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Principal paid on revenue bonds	(35,290)	(38,855)
Interest paid on revenue bonds	(47,211)	(43,482)
Federal interest rebates	7,770	7,712
Bond proceeds	323,500	169,685
Payment on refunded debt	(122,323)	(62,107)
Bond issuance cost	(1,815)	(1,417)
Cash received from contributions in aid of construction	14,439	22,344
Licensing obligation payments	(3,489)	(3,564)
Acquisition and construction of plant assets	(163,048)	(228,067)
Proceeds on sale of plant assets	423	579
Miscellaneous nonoperating income	600	466
Net cash used in capital and related financing activities	(26,444)	(176,706)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of investment securities	(648,906)	(471,871)
Sale proceeds of investment securities	539,546	448,593
Investment income proceeds	3,876	1,900
Net repurchase agreement	(8,000)	45,999
Cash paid for conservation loans	64	69
Net cash (used in) provided by investing activities	(113,420)	24,690
NET (DECREASE) INCREASE IN CASH	$ (25,407)	$ 7,847

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

PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(AMOUNTS IN THOUSANDS)

	TWELVE MONTHS ENDED DECEMBER 31, 2014	TWELVE MONTHS ENDED DECEMBER 31, 2013
CASH AT END OF YEAR	$ 7,623	$ 33,030
CASH AT BEGINNING OF YEAR	33,030	25,183
NET (DECREASE) INCREASE IN CASH	$ (25,407)	$ 7,847
OPERATING ACTIVITIES		
Net operating income	$ 80,017	$ 88,918
Adjustments to reconcile net operating income to net cash provided by (used in) operating activities:		
Depreciation and amortization	53,896	50,474
Accretion expense	2,843	2,475
Earned revenue from deposits	(107)	(107)
Provision for uncollectible accounts	(11)	(79)
Cash provided by (used in) changes in operating assets and liabilities:		
Change in Habitat funds held in trust	(20)	800
Customer accounts receivable	(3,576)	2,601
Materials and supplies	1,045	336
Other current assets	(103)	275
Trade and wages payables	4,872	5,620
Payable to power purchasers, net	(5,135)	356
Accrued taxes	112	275
Customer deposits	(1,665)	7,687
Accrued other postemployment benefits	236	232
Cash paid for extraordinary loss	(17,947)	-
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 114,457	$ 159,863

Supplemental Disclosure (Amounts in Thousands)	2014	2013
Changes in construction costs included in accounts payable	$ (7,976)	$ 6,457

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.

GASB Statement No. 67, *Financial Reporting for Pension Plans – an amendment of GASB Statement No. 25*, GASB Statement No. 69, *Government Combinations and Disposal of Government Operations* and GASB Statement No. 70, *Accounting and Reporting for Nonexchange Financial Guarantees* were all effective for the District beginning in fiscal year 2014. Implementation of these statements did not have a material impact to the District's financial results.

In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*. The primary objective of Statement No. 68 is to improve accounting and financial reporting by state and local governments for pensions. This statement establishes standards for measuring and recognizing liabilities, deferred outflows and deferred inflows of resources, and expenses. For defined benefit pension plans, this statement identifies the methods and assumptions that should 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. This Statement will require the District to account for its proportional share of multi-employer plans, including the State pension fund. Note disclosure and required supplementary information about pensions are also addressed. Statement No. 68 is effective for the District beginning in fiscal year 2015. 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.

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 2014 and 2013, the allowance for uncollectible accounts was $234,000 and $245,000, 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 non-operating revenue at the point at which it becomes nonrefundable. The District recognized $22.8 million and $12.0 million of contributions in aid of construction for the years ended December 31, 2014 and 2013, 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 4.23% for 2014 and 2013. Interest capitalized during 2014 and 2013 was $11.3 million and $10.4 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 a composite rate of 2.27% and 2.31% for 2014 and 2013, respectively. When utility plant assets are retired, their original cost, together with removal costs, less salvage, are charged to accumulated depreciation. The District does not collect costs of disposal through rates. Such costs 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 – Investments with maturities of more than twelve months are presented at fair value. Fair values are based on quoted market prices for those investments. All other investments are presented at amortized cost in accordance with GASB No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* on the basis that their amortized cost approximates fair value for these instruments of shorter maturity. 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.

Changes in unrealized gains and losses on investments with maturities held for more than one year and realized gains and losses during the current year 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 from (to) Power Purchasers – This balance represents actual power costs in excess (deficit) of estimated power costs received by the Priest Rapids Project from power purchasers to be collected from, or due 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 resources, 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 – Invested in capital assets, net of related debt; Restricted; and Unrestricted. These classifications are defined as follows:

- *Invested in capital assets, net of related debt* – 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 "invested in capital assets, net of related debt."

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 deregulation of the electrical utility industry.

With regard to liability risk, the District has elected self-insurance for general and auto liability up to $500,000 per incident. The District has historically had minimal liability claims activity, and estimated claims incurred but not reported are not significant as of December 31,

2014. The District is involved in litigation 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 restricted to meeting the District's load requirements in excess of expected generation from the Priest Rapids Project and selling power excess to the District's needs at the best available price. To mitigate risk associated with power marketing activities, the District established the Risk Oversight Committee and adopted the Energy Risk Management Policies and Procedures to provide greater ongoing monitoring and review of power transactions. The Energy Risk Management Policy and Procedures outlines the parameters for transactions, trader and counterparty exposure, and serves as a formal communication to all District employees performing power marketing functions. The District believes that the Energy Risk Management Policy and Procedures, coupled with the Risk Oversight Committee, limits the risk of any substantial financial loss resulting from the District's power supply management activities.

2. CASH AND INVESTMENTS

The District's cash deposits at December 31, 2014 and 2013, 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)	2014	2013
Unrestricted assets:		
Unrestricted funds:		
Revenue and Service System funds	$ 67,538	$ 97,009
Board designated funds:		
Electric System Reserve and Contingency fund	121,783	120,111
Self-Insurance Reserve fund	1,087	1,101
Total board designated funds	122,870	121,212
Total unrestricted funds	190,408	218,221
Restricted:		
Construction funds	134,759	70,822
Bond Sinking funds	60,922	58,028
Debt Service Reserve funds	58,960	47,897
Bond Interest funds	39,683	27,791
Renewal, Replacement and Contingency fund	11,952	24,626
Habitat funds	12,586	12,496
Quincy Chute Renewal and Replacement fund	1,730	1,711
Total restricted funds	320,592	243,371
Total	$ 511,000	$ 461,592

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.

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.

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 or municipal bonds, and no more than twenty-five percent (25%) of the total portfolio par value will be invested in 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 District's investments at December 31, 2014 and 2013, 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 $1.7 million and $1.4 million for 2014 and 2013, respectively.

During 2014 and 2013, the District realized $4.0 million and $2.0 million of interest earnings and realized gains from investments, respectively. The unrealized net gain/loss on investments held at December 31, 2014 and 2013, was a $2.6 million net gain and a $2.8 million net loss, respectively.

Investments are made in investment types authorized by the RCW. The types are 1) Obligations of the U.S. Government and its agencies, 2) Repurchase agreements collateralized by U.S. Government obligations, 3) Money market funds that have holdings of or are backed by U.S. Government obligations and 4) Municipal bonds. Investments by type at December were as follows:

(amounts in thousands)	2014	2013
U.S. Agencies	$ 224,133	$ 162,470
U.S. Treasuries	133,735	175,447
Money Market Funds	50,216	55,467
Repurchase Agreements	14,000	6,000
Commercial Paper	29,325	-
Municipal Bonds	50,292	27,815
Total investments	501,701	427,199
Cash	7,623	33,030
Total cash and investments	$ 509,324	$ 460,229

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, 2014. TSY refers to U.S. Treasury securities and N/R means not rated.

	Credit Rating	2014	2013
U.S. Treasuries	TSY	27%	38%
Federal National Mortgage Assoc.	AA+	10%	8%
Federal Home Loan Mortgage Corp.	AA+	6%	7%
Money Market Funds	N/R	10%	13%
Federal Home Loan Bank	AA+	20%	13%
Federal Farm Credit Bank	AA+	7%	11%

3. UTILITY PLANT

Utility plant of the District as of December 31, 2014, is summarized as follows:

(amounts in thousands)	Balance 2013	Additions	Retirements/ Transfers	Balance 2014
Distribution facilities	$ 462,045	$ 10,742	$ (156)	$ 472,631
Transmission facilities	170,215	59,293	(825)	228,683
Hydro facilities				
Power plant structures	61,140	17,026	(3,321)	74,845
Reservoirs, dams, waterways	410,252	-	-	410,252
Power plant equipment	508,779	36,087	(1,280)	543,586
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	308,196	43,774	-	351,970
FERC License	119,335	-		119,335
Other intangible assets	19,508	5,524	-	25,032
Total	2,093,721	172,446	(5,582)	2,260,585
Accumulated depreciation and amortization	(763,664)	(53,634)	2,260	(815,038)
Subtotal	1,330,057	118,812	(3,322)	1,445,547
Land and land rights	24,618	-	-	24,618
Construction in progress	334,686	167,310	(167,450)	334,546
Total net utility plant	$ 1,689,361	$ 286,122	$ (170,772)	$ 1,804,711

(amounts in thousands)	Balance 2012	Additions	Retirements/ Transfers	Balance 2013
Distribution facilities	$ 441,068	$ 21,258	$ (281)	$ 462,045
Transmission facilities	162,114	8,101	-	170,215
Hydro facilities				
Power plant structures	57,208	3,932	-	61,140
Reservoirs, dams, waterways	411,469	527	(1,744)	410,252
Power plant equipment	464,031	47,257	(2,509)	508,779
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	297,766	10,430	-	308,196
FERC License	110,646	8,689	-	119,335
Other intangible assets	5,667	13,841	-	19,508
Total	1,984,220	114,035	(4,534)	2,093,721
Accumulated depreciation and amortization	(715,183)	(50,537)	2,056	(763,664)
Subtotal	1,269,037	63,498	(2,478)	1,330,057
Land and land rights	24,577	-	41	24,618
Construction in progress	221,925	214,177	(101,416)	334,686
Total net utility plant	$ 1,515,539	$ 277,675	$ (103,853)	$ 1,689,361

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 $57.1 million, were recorded as an intangible asset included in Utility plant and are being amortized over the term of the license.

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 $57.1 million as of December 31, 2014, of which approximately $3.5 million is expected to be paid within one year. The present value of the obligations was $57.8 million as of December 31, 2013. These amounts are included in the FERC license balance and are 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 October of 2014, the District issued $204.2 million of revenue and refunding bonds at a premium of $23.8 million, associated with the Priest Rapids Project, to finance improvements at the Priest Rapids Project, to refund certain bonds previously issued, to pay issuance costs, and to fund debt service reserved. The refunded portion of $119.8 million will yield a net present value savings of $15.4 million. In November of 2014, the District issued $50 million of revenue bonds to finance improvement of the Electric System. In August of 2013, the District issued $100.1 million of revenue bonds associated with the Priest Rapids Project. The bonds were issued at an initial offering premium of $1.2 million. The bonds were issued to finance improvements at the Priest Rapids Project, to pay issuance costs, and to fund a debt service reserve. In September of 2013, the District issued $67.6 million in Electric System revenue refunding bonds to retire $56.8 million of 2011-I revenue and refunding bonds. The 2013 Electric System bonds were issued at fixed interest rates at a net original issue premium of $815 thousand. The District realized a $1.7 million and $1.3 million refunding loss associated with unamortized discounts/premiums for 2014 and 2013, respectively.

The 2014 bond issue of the Electric system accrues interest based on a variable SIFMA INDEX. All other outstanding District bond issues are fixed rate obligations. All District bond issues are secured by a pledge of the net revenues of the District and are on parity with each other. See Note 13.

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

(amounts in thousands)	2014	2013
Electric System, interest rates of .36% to 5.0%, maturing through 2044	$ 195,745	$ 151,340
Priest Rapids Project, interest rates of .38% to 5.83%, maturing through 2044	1,056,030	1,001,400
Total revenue bonds outstanding	$ 1,251,775	$ 1,152,740

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

(amounts in thousands)	Principal	Interest	Total
2015	$ 29,470	$ 56,367	$ 85,837
2016	30,915	58,537	89,452
2017	32,075	57,158	89,233
2018	31,680	55,731	87,411
2019	43,640	53,938	97,578
2020 - 2024	208,430	236,569	444,999
2025 - 2029	252,820	181,020	433,840
2030 - 2034	243,350	115,085	358,435
2035 - 2039	229,975	57,983	287,958
2040 - 2044	149,420	11,396	160,816
Total	$ 1,251,775	$ 883,784	$ 2,135,559

For the years ending December 31, 2014 and 2013, the District is in compliance with all debt 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 2013	Additions	Reductions	Balance 2014	Due Within One Year
Revenue bonds payable	$ 1,152,740	$ 254,165	$ (155,130)	$ 1,251,775	$ 29,470
Unamortized premiums and discounts, net	27,021	23,835	(5,278)	45,578	-
Total	$ 1,179,761	$ 278,000	$ (160,408)	$ 1,297,353	$ 29,470

(amounts in thousands)	Balance 2012	Additions	Reductions	Balance 2013	Due Within One Year
Revenue bonds payable	$ 1,080,675	$ 167,695	$ (95,630)	$ 1,152,740	$ 35,290
Unamortized premiums and discounts, net	34,351	1,990	(9,320)	$ 27,021	-
Total	$ 1,115,026	$ 169,685	$ (104,950)	$ 1,179,761	$ 35,290

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 64% and 61% of Priest Rapids Project power costs with power purchasers funding 36% and 39% for 2014 and 2013, 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.

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 MW 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) power. Rollover rights were included as part of this agreement. The District chose not to exercise the rollover rights by the December 31, 2014 deadline, and this transmission agreement will expire 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. In 2010, the District exercised rollover rights associated with 12 MW of transmission for the delivery of power from the Nine Canyon Wind Project in order to extend the term of the reservation to October 1, 2030. In 2011, the District entered into a 2-year contract with BPA for 250 MW of transmission that expired on September 30, 2013, and is no longer needed due to the completion of the new Columbia/Rocky Ford 230 kV line in February 2014.

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)		
2015	$	2,947
2016		930
2017		1,015
2018		1,078
2019		1,503

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 $2.1 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 will work 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.

The net payments to the Yakama Nation totaled $2,288,984 and $2,266,513 during 2014 and 2013, respectively. The projected annual cost for this agreement for 2015 is $2.2 million and for 2016 to 2020 is $1.6 million. The agreement expires at the end of the FERC license term (2052).

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 fiber design/build, mobile radio replacement, electrical system upgrades, multiple transformer purchases, power cable purchases, and substation and distribution line construction projects over the next few years totaling approximately $25.5 million as of December 31, 2014.

The District's improvement programs for the Priest Rapids Project include restoration or replacement of generators, construction and upgrades to project support buildings, construction of a fish bypass project, 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 $183.3 million as of December 31, 2014.

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, 2014, and December 31, 2013, equaled $3.5 million and $3.4 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, 2014, representing required contributions through the New License term.

Estimated Fixed Habitat Funding Commitments (amounts in thousands)		
2015	$	3,509
2016		3,574
2017		3,642
2018		3,710
2019		3,780
2020 and thereafter		79,331
Total	$	97,546

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 nonprofit 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 $13,165,000 to refund most of the NoaNet 2001 bonds. The Electric System has guaranteed the repayment of up to approximately $1.43 million of NoaNet's remaining 2011 bonds (which amount includes a potential 25% step up if another member defaults) plus accrued interest. As of December 2016, these bonds should be completely paid. In addition, NoaNet has an outstanding $5 million loan with a commercial lender in order to finance capital expenditures and network upgrades. The District has guaranteed the repayment of up to 17.57% of the outstanding balance to the extent NoaNet's revenues are insufficient to pay the loans. This loan must be repaid in full by December of 2017. No contributions by the District were required for 2013 or 2014.

The NoaNet financial report is the responsibility of NoaNet. The independent auditor for the District has not audited or examined any information in the financial report, and accordingly, does not express an opinion or any other form of assurance with respect thereto.

8. PENSION / RETIREMENT PLAN

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 retirement plans. 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 98504-8380; or it may be downloaded from the DRS website at www.drs.wa.gov.

Public Employees' Retirement System (PERS) Plans 1, 2, and 3

Plan Description

The Legislature established PERS in 1947. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior courts; employees of legislative committees; employees of district and municipal courts; and employees of local governments. Membership also includes higher education employees not participating in higher education retirement programs. Approximately 49 percent of PERS salaries are accounted for by state employment. PERS retirement benefit provisions are established in Chapters 41.34 and 41.40 RCW and may be amended only by the State Legislature.

PERS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a defined benefit plan with a defined contribution component.

PERS members who joined the system by September 30, 1977 are Plan 1 members. Those who joined on or after October 1, 1977 and by either, February 28, 2002 for state and higher education employees, or August 31, 2002 for local government employees, are Plan 2 members unless they exercised an option to transfer their membership to Plan 3. PERS members joining the system on or after March 1, 2002 for state and higher education employees, or September 1, 2002 for local government employees have the irrevocable option of choosing membership in either PERS Plan 2 or Plan 3. The option must be exercised within 90 days of employment. Employees who fail to choose within 90 days default to Plan 3.

PERS is comprised of and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members, and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits

for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of this Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

PERS Plan 1 and Plan 2 retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Employee contributions to the PERS Plan 1 and Plan 2 defined benefit plans accrue interest at a rate specified by the Director of DRS. During DRS' Fiscal Year 2013, the rate was five and one-half percent compounded quarterly. Members in PERS Plan 1 and Plan 2 can elect to withdraw total employee contributions and interest thereon, in lieu of any retirement benefit, upon separation from PERS-covered employment.

PERS Plan 1 members are vested after the completion of five years of eligible service.

PERS Plan 1 members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with 25 years of service, or at age 60 with at least 5 years of service. Plan 1 members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits.

The monthly benefit is 2 percent of the average final compensation (AFC) per year of service, but the benefit may not exceed 60 percent of the AFC. The AFC is the monthly average of the 24 consecutive highest-paid service credit months.

PERS Plan 1 retirement benefits are actuarially reduced to reflect the choice, if made, of a survivor option.

Plan 1 members may elect to receive an optional COLA that provides an automatic annual adjustment based on the Consumer Price Index. The adjustment is capped at 3 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 1 provides duty and non-duty disability benefits. Duty disability retirement benefits for disablement prior to the age of 60 consist of a temporary life annuity. The benefit amount is $350 a month, or two-thirds of the monthly AFC, whichever is less. The benefit is reduced by any workers' compensation benefit and is payable as long as the member remains disabled or until the member attains the age of 60, at which time the benefit is converted to the member's service retirement amount.

A member with five years of covered employment is eligible for non-duty disability retirement. Prior to the age of 55, the benefit amount is 2 percent of the AFC for each year of service reduced by 2 percent for each year that the member's age is less than 55. The total benefit is limited to 60 percent of the AFC and is actuarially reduced to reflect the choice of a survivor option. Plan 1 members may elect to receive an optional COLA amount (based on

the Consumer Price Index), capped at 3 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 2 members are vested after the completion of five years of eligible service. Plan 2 members are eligible for normal retirement at the age of 65 with five years of service. The monthly benefit is 2 percent of the AFC per year of service. The AFC is the monthly average of the 60 consecutive highest-paid service months. There is no cap on years of service credit; and a cost-of-living allowance is granted (based on the Consumer Price Index), capped at 3 percent annually.

PERS Plan 2 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 reduced benefit. The benefit is reduced by an early retirement factor (ERF) that varies according to age, for each year before age 65.

PERS Plan 2 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions, if hired prior to May 1, 2013:

- With a benefit that is reduced by 3 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 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of 5 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.

PERS Plan 2 retirement benefits are actuarially reduced to reflect the choice, if made, of a survivor option.

PERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component and member contributions finance a defined contribution component. As established by Chapter 41.34 RCW, employee contribution rates to the defined contribution component range from 5 percent to 15 percent of salaries, based on member choice. Members who do not choose a contribution rate default to a 5 percent rate. There are currently no requirements for employer contributions to the defined contribution component of PERS Plan 3.

PERS Plan 3 defined contribution retirement benefits are dependent upon the results of investment activities. Members may elect to self-direct the investment of their contributions. Any expenses incurred in conjunction with self-directed investments are paid by members. Absent a member's self-direction, PERS Plan 3 contributions are invested in the Retirement Strategy Fund that assumes the member will retire at age 65.

For DRS' Fiscal Year 2013, PERS Plan 3 employee contributions were $99.0 million, and plan refunds paid out were $69.4 million.

The defined benefit portion of PERS Plan 3 provides members a monthly benefit that is 1 percent of the AFC per year of service. The AFC is the monthly average of the 60 consecutive highest-paid service months. There is no cap on years of service credit, and Plan 3 provides the same cost-of-living allowance as Plan 2.

Effective June 7, 2006, PERS 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 twelve months of that service are earned after age 44; or after five service credit years earned in PERS Plan 2 by June 1, 2003. Plan 3 members are immediately vested in the defined contribution portion of their plan.
Vested Plan 3 members are eligible for normal retirement at age 65, or they may retire early with the following conditions and benefits:

- If they have at least ten service credit years and are 55 years old, the benefit is reduced by an ERF that varies with age, for each year before age 65.

- If they have 30 service credit years and are at least 55 years old, and were hired before May 1, 2013, they have the choice of a benefit that is reduced by 3 percent for each year before age 65; or a benefit with a smaller (or no) reduction factor (depending on age) that imposes stricter return-to-work rules.

- If they have 30 service credit years, are at least 55 years old, and were hired after May 1, 2013, they have the option to retire early by accepting a reduction of 5 percent for each year before age 65.

PERS Plan 3 benefits are actuarially reduced to reflect the choice, if made, of a survivor option.

PERS Plan 2 and Plan 3 provide disability benefits. There is no minimum amount of service credit required for eligibility. The Plan 2 monthly benefit amount is 2 percent of the AFC per year of service. For Plan 3, the monthly benefit amount is 1 percent of the AFC per year of service. These disability benefit amounts are actuarially reduced for each year that the member's age is less than 65, and to reflect the choice of a survivor option. There is no cap on years of service credit, and a cost-of-living allowance is granted (based on the Consumer Price Index) capped at 3 percent annually.

PERS members meeting specific eligibility requirements have options available to enhance their retirement benefits. Some of these options are available to their survivors.

A one-time duty-related death benefit is provided to the beneficiary or the estate of a PERS member who dies as a result of injuries sustained in the course of employment, or if the death

resulted from an occupational disease or infection that arose naturally and proximately out of the member's covered employment, if found eligible by the Department of Labor and Industries.

From January 1, 2007 through December 31, 2007, judicial members of PERS were given the choice to elect participation in the Judicial Benefit Multiplier (JBM) Program enacted in 2006. Justices and judges in PERS Plan 1 and Plan 2 were able to make an irrevocable election to pay increased contributions that would fund a retirement benefit with a 3.5 percent multiplier. The benefit would be capped at 75 percent of AFC. Judges in PERS Plan 3 could elect a 1.6 percent of pay per year of service benefit, capped at 37.5 percent of AFC.

Newly elected or appointed justices and judges who chose to become PERS members on or after January 1, 2007, or who had not previously opted into PERS membership, were required to participate in the JBM Program.

There are 1,176 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of June 30, 2013[1]:

Retirees and Beneficiaries Receiving Benefits	85,328
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	31,047
Active Plan Members Vested	150,706
Terminated Plan Members Nonvested	101,191
Total	368,272

Funding Policy

Each biennium, the state Pension Funding Council adopts PERS Plan 1 employer contribution rates, PERS Plan 2 employer and employee contribution rates, and PERS Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at 6 percent for state agencies and local government unit employees, and at 7.5 percent for state government elected officials. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. Under PERS Plan 3, employer contributions finance the defined benefit portion of the plan and member contributions finance the defined contribution portion. The Plan 3 employee contribution rates range from 5 percent to 15 percent.

[1] GASB does not require the number of participating employers and members to be presented in the notes to the financial statements. The information has been provided here so it can be included in the notes if desired.

As a result of the implementation of the Judicial Benefit Multiplier Program in January 2007, a second tier of employer and employee rates was developed to fund, along with investment earnings, the increased retirement benefits of those justices and judges that participate in the program

The methods used to determine the contribution requirements are established under state statute in accordance with Chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of current-year covered payroll, as of December 31, 2014, are as follows:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
Employer*	9.21%**	9.21%**	9.21%***
Employee	6.00%****	4.92%****	*****

* The employer rates include the employer administrative expense fee currently set at 0.18%.
** The employer rate for state elected officials is 13.73% for Plan 1 and 9.21% for Plan 2 and Plan 3.
*** Plan 3 defined benefit portion only.
**** The employee rate for state elected officials is 7.50% for Plan 1 and 4.92% for Plan 2.
***** Variable from 5.0% minimum to 15.0% maximum based on rate selected by the PERS 3 member.

Both the District and the employees made the required contributions. The District's required contributions for the years ended December 31, were as follows:

(amounts in thousands)	PERS Plan 1	PERS Plan 2	PERS Plan 3
2014	$ 101	$ 4,408	$ 1,161
2013	246	3,843	1,018
2012	356	3,269	854

Deferred Compensation Plan – The District has an Internal Revenue Code Section 457 (b) deferred compensation program covering eligible employees as defined in the plan document. Participants may contribute and defer, up to defined limits, a portion of their current year's salary. The deferred compensation is held in trust and is not available to employees until termination, retirement, death, or unforeseeable emergency. The program includes a loan provision in accordance with IRS guidelines. All plan assets are held in trust for the exclusive benefit of participants and their beneficiaries and therefore are not included in the District's financial statements.

Additionally, the District administers the Public Utility District No. 2 of Grant County's 401(a) Governmental Money Purchase Plan and Trust (fixed and variable plan). Eligible employees can elect to either contribute to the Section 457 deferred compensation plan (variable) or the 401(a) defined contribution plan (fixed). The District's matching employer contributions (50 cents per one dollar of employee contributions) are deposited into the 401(a) plan. The District's match is capped at 2% of straight-time employee wages for the pay period. The District made matching contributions of $923,435 and $898,327 in 2014 and 2013, respectively.

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 non-unit 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, 2014 and 2013, the District paid approximately $226,000 and $234,000 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, 2014 and 2013:

(amounts in thousands)	2014	2013
Normal cost with interest	$ 194	$ 198
Amortization amount with interest	268	268
Annual required contribution	$ 462	$ 466
Annual OPEB cost	$ 462	$ 466
Less: benefit payments	(226)	(234)
Increase in net OPEB obligation	236	232
Net OPEB obligation at beginning of year	1,472	1,240
Net OPEB obligation at end of year	$ 1,708	$ 1,472

Funded Status and Funding Progress

As of December 31, 2014 and 2013, the District's Actuarial Accrued Liability ("AAL") was $4.5 million and $4.1 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 2014 and 2013, the covered payroll (annual payroll of active employees covered by the plan) was $54.7 million and $54.4 million, respectively, and the ratio of the unfunded obligation to the covered payroll was 8.2% and 7.6%, 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, 2013. The Entry Age Normal method is used to develop an Annual Required Contribution and an Actuarial Accrued Liability. Use of the EAN Level Percent of Pay method for the OPEB Plan is a change from the prior year valuation, which used the Projected Unit Cost method to value OPEB benefits. This change in method resulted in a 1% increase in Accrued Liabilities.

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, 2012, actuarial valuation published by the Office of the State Actuary.

Medical trends **–** Premium increases of 7.5% in 2014 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 5.0% that was used in the valuation represents the District's current long term borrowing rate. This rate is used because the Plan is "unfunded" and the District's assets would be used to pay benefits.

10. CONTINGENCIES

On April 14, 2015 the District's Board of Commissioners approved an agreement that will lead to settlement of a federal lawsuit with Crescent Bar Island residents concerning the use of real property on District land. The settlement would allow 80 percent of the Crescent Bar area previously under lease to be made fully available to the public. The residents will be allowed to remain on the island through at least 2047 under new leases, which will be subject to FERC approval. The agreement would 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. As the settlement will be entered subsequent to December 31, 2014, no amounts have been recorded related to the proposed settlement in the District's financial statements for the current period. Furthermore, 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 fiber optic distribution system in its service area. As of December 31, 2014, the build out is 68% complete. This fiber optic distribution system is interconnected with multiple regional and national telecommunications carriers, including NoaNet's fiber optic network. The District has made capacity on this system available to providers of high speed Internet services and telephone services, among others. The District has also recently implemented wireless internet capacity which will be made available to internet providers.

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

(amounts in thousands)	**2014**	**2013**
Operating revenues		
Wholesale fiber services	$ 4,702	$ 4,027
Dark fiber revenue	399	377
Wholesale fiber optic network sales	$ 5,101	$ 4,404
Operating expenses		
Administrative and general	$ 476	$ 431
Repairs and maintenance	812	1,038
Depreciation	5,863	5,499
Total operating expenses	$ 7,151	$ 6,968
Nonoperating revenues		
Contributions in aid of construction	$ 396	$ 274
Utility plant		
Additions to utility plant	$ 10,025	$ 11,254
Utility plant, net of accumulated depreciation	$ 87,772	$ 83,576

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 is working to repair the fracture in Monolith No. 4 and to anchor all 13 monoliths. Anchoring includes 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 are expected to be complete before the summer recreation season of 2015. During the repair, Wanapum Dam continues to operate and the District continues to meet its obligations with regard to fish passage, flood-control, irrigation, cultural resource protection, public safety, and electric generation. Recreational activities have been 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 has been recognized in 2014 of which $18.0 million is associated with repairs and additional operating costs associated with the fracture. The remaining $3.3 million relates to a non-cash permanent write down of the original spillway cost to comply with Governmental Accounting Standards Board Statement 42 related to asset impairment. 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. Incremental capital requirements are

driven almost exclusively by the structural improvement costs, most of which are comprised of the anchoring of the dam with additional steel reinforcements. Gross incremental capital costs to repair the fracture and to correct the design error throughout the structure are estimated to be $57 million of which $40.2 million was spent as of December 31, 2014. The District continues to work with its insurers on potential recovery of a portion of the loss.

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.

NOTE 13 - SEGMENTS
DECEMBER 31, 2014

CONDENSED STATEMENT OF NET POSITION

(AMOUNTS IN THOUSANDS)	Electric System	Priest Rapids Project	Other	Total
ASSETS				
Total current assets	$ 99,992	$ 78,894	$ 7,100	$ 185,986
Net utility plant	548,475	1,256,236	-	1,804,711
Noncurrent	223,305	192,144	(41,179)	374,270
TOTAL ASSETS	871,772	1,527,274	(34,079)	2,364,967
Deferred outflows of resources	536	7,080	-	7,616
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	$ 872,308	$ 1,534,354	$ (34,079)	$ 2,372,583
LIABILITIES				
Current	$ 30,554	$ 104,365	$ 11,327	$ 146,246
Noncurrent	205,855	1,164,052	(45,390)	1,324,517
TOTAL LIABILITIES	236,409	1,268,417	(34,063)	1,470,763
NET POSITION				
Invested in capital assets, net of related debt	382,781	150,367	45,500	578,648
Restricted	20,939	113,790	(110)	134,619
Unrestricted	232,179	1,780	(45,406)	188,553
TOTAL NET POSITION	635,899	265,937	(16)	901,820
TOTAL LIABILITIES AND NET POSITION	$ 872,308	$ 1,534,354	$ (34,079)	$ 2,372,583

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

PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

NOTE 13 - SEGMENTS
FOR THE YEAR ENDED DECEMBER 31, 2014

SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

(AMOUNTS IN THOUSANDS)	Electric System	Priest Rapids Project	Other	Total
OPERATING REVENUES	$ 247,566	$ 167,588	$ (106,489)	$ 308,665
OPERATING EXPENSES				
Depreciation and amortization	30,713	23,183	-	53,896
Other operating expenses	212,407	68,834	(106,489)	174,752
Total operating expenses	243,120	92,017	(106,489)	228,648
NET OPERATING INCOME	4,446	75,571	-	80,017
OTHER REVENUES (EXPENSES)				
Interest and other income	3,091	4,559	(218)	7,432
Interest on revenue bonds and other, net of capitalized interest	(5,196)	(41,131)	202	(46,125)
Federal rebates on revenue bonds	-	7,770	-	7,770
Amortization of debt discount/premium	940	2,138	-	3,078
Cost of debt issuance	(357)	(1,458)	-	(1,815)
Total other revenues (expenses)	(1,522)	(28,122)	(16)	(29,660)
CONTRIBUTIONS IN AID OF CONSTRUCTION	22,767	-	-	22,767
EXTRAORDINARY LOSS - WANAPUM FRACTURE	-	(21,269)	-	(21,269)
CHANGE IN NET POSITION	25,691	26,180	(16)	51,855
NET ASSETS				
Beginning of year	610,208	239,757	-	849,965
End of year	$ 635,899	$ 265,937	$ (16)	$ 901,820

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

NOTE 13 - SEGMENTS
FOR THE YEAR ENDED DECEMBER 31, 2014

CONDENSED SCHEDULE OF CASH FLOWS

(AMOUNTS IN THOUSANDS)	Electric System	Priest Rapids Project	Other	Total
Net cash provided by operating activities	$ 44,467	$ 61,717	$ 8,273	$ 114,457
Net cash provided by (used in) capital and related financing activities	8,555	(41,320)	6,321	(26,444)
Net cash used in provided by investing activities	(67,170)	(25,598)	(20,652)	(113,420)
NET DECREASE IN CASH	$ (14,148)	$ (5,201)	$ (6,058)	$ (25,407)
CASH AT END OF PERIOD	$ 3,667	$ 2,745	$ 1,211	$ 7,623
CASH AT BEGINNING OF YEAR	17,815	7,946	7,269	33,030
NET DECREASE IN CASH	$ (14,148)	$ (5,201)	$ (6,058)	$ (25,407)

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

PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

NOTE 13 - SEGMENTS
DECEMBER 31, 2013

CONDENSED STATEMENT OF NET POSITION

(AMOUNTS IN THOUSANDS)	Electric System	Priest Rapids Project	Other	Total
ASSETS				
Total current assets	$ 237,027	$ 83,042	$ (53,652)	$ 266,417
Net utility plant	534,790	1,154,571	-	1,689,361
Noncurrent	81,615	156,729	501	238,845
TOTAL ASSETS	853,432	1,394,342	(53,151)	2,194,623
Deferred outflows of resources	1,035	6,299	-	7,334
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	$ 854,467	$ 1,400,641	$ (53,151)	$ 2,201,957
LIABILITIES				
Current	$ 86,004	$ 117,560	$ (53,151)	$ 150,413
Noncurrent	158,253	1,043,326	-	1,201,579
TOTAL LIABILITIES	244,257	1,160,886	(53,151)	1,351,992
NET ASSETS				
Invested in capital assets, net of related debt	373,716	156,712	-	530,428
Restricted	24,465	82,991	-	107,456
Unrestricted	212,029	52	-	212,081
TOTAL NET ASSETS	610,210	239,755	-	849,965
TOTAL LIABILITIES AND NET ASSETS	$ 854,467	$ 1,400,641	$ (53,151)	$ 2,201,957

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

PUBLIC UTILITY DISTRICT NO. 2 OF GRANT COUNTY, WASHINGTON

NOTE 13 - SEGMENTS
DECEMBER 31, 2013

SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

(AMOUNTS IN THOUSANDS)	Electric System	Priest Rapids Project	Other	Total
OPERATING REVENUES	$ 234,786	$ 142,168	$ (86,527)	$ 290,427
OPERATING EXPENSES				
Depreciation and amortization	29,612	20,862	-	50,474
Other operating expenses	171,552	66,010	(86,527)	151,035
Total operating expenses	201,164	86,872	(86,527)	201,509
NET OPERATING (LOSS) INCOME	33,622	55,296	-	88,918
OTHER REVENUES (EXPENSES)				
Interest and other income	(96)	(140)	-	(236)
Interest on revenue bonds and other, net of capitalized interest	(4,725)	(39,071)	-	(43,796)
Federal rebates on revenue bonds	-	7,712	-	7,712
Amortization of debt expense, discount, and premium	1,917	235	-	2,152
Total other revenues (expenses)	(2,904)	(31,264)	-	(34,168)
CONTRIBUTIONS IN AID OF CONSTRUCTION	11,966	-	-	11,966
CHANGE IN NET POSITION	42,684	24,032	-	66,716
NET POSITION				
Beginning of year	567,524	215,725	-	783,249
End of year	$ 610,208	$ 239,757	$ -	$ 849,965

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

NOTE 13 - SEGMENTS
DECEMBER 31, 2013

CONDENSED SCHEDULE OF CASH FLOWS

(AMOUNTS IN THOUSANDS)	Electric System	Priest Rapids Project	Other	Total
Net cash provided by operating activities	$ 66,412	$ 76,200	$ 17,251	$ 159,863
Net cash used in capital and related financing activities	(57,072)	(119,068)	(566)	(176,706)
Net cash (used in) provided by investing activities	(5,257)	35,480	(5,533)	24,690
NET INCREASE (DECREASE) IN CASH	$ 4,083	$ (7,388)	$ 11,152	$ 7,847
CASH AT END OF PERIOD	$ 17,815	$ 7,946	$ 7,269	$ 33,030
CASH AT BEGINNING OF YEAR	13,732	15,334	(3,883)	25,183
NET INCREASE (DECREASE) IN CASH	$ 4,083	$ (7,388)	$ 11,152	$ 7,847

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