

**Washington State Auditor's Office**  
**Financial Statements Audit Report**

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**Public Utility District No. 1 of Clallam  
County**

Audit Period  
January 1, 2007 through December 31, 2007

Report No. 1000264

Issue Date  
**December 15, 2008**



WASHINGTON  
**BRIAN SONNTAG**  
STATE AUDITOR



**Washington State Auditor  
Brian Sonntag**

December 15, 2008

Board of Commissioners  
Public Utility District No. 1 of Clallam County  
Port Angeles, Washington

***Report on Financial Statements***

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

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

In addition to this work, we look at other areas of our audit client's operations for compliance with state laws and regulations. The results of that audit will be included in a separately issued accountability report.

Sincerely,

**BRIAN SONNTAG, CGFM**  
STATE AUDITOR

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January 1, 2007 through December 31, 2007**

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# Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters in Accordance with *Government Auditing Standards*

## **Public Utility District No. 1 of Clallam County January 1, 2007 through December 31, 2007**

Board of Commissioners  
Public Utility District No. 1 of Clallam County  
Port Angeles, Washington

We have audited the basic financial statements of Public Utility District No. 1 of Clallam County, Washington, as of and for the years ended December 31, 2007 and 2006, and have issued our report thereon dated October 14, 2008.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

### ***INTERNAL CONTROL OVER FINANCIAL REPORTING***

In planning and performing our audits, we considered the District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the District's ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the District's financial statements that is more than inconsequential will not be prevented or detected by the District's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

## **COMPLIANCE AND OTHER MATTERS**

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

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

This report is intended for the information and use of management and the Board of Commissioners. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and last name "Sonntag" clearly distinguishable.

**BRIAN SONNTAG, CGFM**  
STATE AUDITOR

October 14, 2008

# Independent Auditor's Report on Financial Statements

## **Public Utility District No. 1 of Clallam County January 1, 2007 through December 31, 2007**

Board of Commissioners  
Public Utility District No. 1 of Clallam County  
Port Angeles, Washington

We have audited the accompanying basic financial statements of Public Utility District No. 1 of Clallam County, Washington, as of and for the years ended December 31, 2007 and 2006, as listed on page 5. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Public Utility District No. 1 of Clallam County, as of December 31, 2007 and 2006, and the changes in financial position and, where applicable, cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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

The management's discussion and analysis on pages 6 through 9 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of

management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and the last name "Sonntag" clearly distinguishable.

**BRIAN SONNTAG, CGFM**  
STATE AUDITOR

October 14, 2008

# Financial Section

## **Public Utility District No. 1 of Clallam County January 1, 2007 through December 31, 2007**

### ***REQUIRED SUPPLEMENTAL INFORMATION***

Management Discussion and Analysis – 2007 and 2006

### ***BASIC FINANCIAL STATEMENTS***

Statement of Net Assets – 2007 and 2006

Statement of Revenues, Expenses and Changes in Net Assets – 2007 and 2006

Statement of Cash Flows – 2007 and 2006

Notes to the Combined Financial Statements – 2007 and 2006

## **PUBLIC UTILITY DISTRICT NO. 1 OF CLALLAM COUNTY, WASHINGTON**

### **MANAGEMENT DISCUSSION & ANALYSIS**

This discussion and analysis is designed to provide an overview of the Clallam County Public Utility District's (District) financial activities for the year ended December 31, 2007 and 2006. This section is intended to be read in conjunction with the basic financial statements and accompanying notes.

#### **Overview of the Financial Statements**

Clallam County P.U.D. is a single enterprise fund with financial activities in the areas of electric, water, and sewer. The operations of the District include the electric system, nine water systems, and three sewer systems. In accordance with Generally Accepted Accounting Principles the District uses full accrual basis accounting where revenues are recognized when earned and expenses when incurred. The basic financial statements include the Statement of Net Assets, the Statement of Revenues, Expenses and Changes in Net Assets, and the Statement of Cash Flows.

The Statement of Net Assets presents the District's assets and liabilities with the difference between them reported as net assets. This statement provides information about the amount of investments in resources (assets) and the obligations to creditors (liabilities). The net assets increase when revenues exceed expenses. This statement provides the basis for evaluating the capital structure, and assessing liquidity and financial flexibility of the District.

The Statement of Revenue, Expenses and Changes in Net Assets reports revenues, expenses, and the change in net assets for the years indicated. This statement measures the success of the District's operations and can be used to evaluate the level of cost recovery from charges for products and services.

The Statement of Cash Flows provides information concerning cash receipts and disbursements resulting from operational, financing, and investing activities. This statement provides insight into the District's ability to generate cash flow and to meet obligations and is an important indicator of the District's liquidity and financial strength.

The Notes to the Financial Statements are presented at the end of the financial statements and provide additional information that is essential to a full understanding of the basic financial statements.

#### **Financial Highlights**

The District has a contract with Bonneville Power Administration (BPA), a federal power-marketing agency, to purchase power through 2011. All of the District's power needs are supplied by BPA with the exception of 1 MW of renewable landfill gas purchased from Klickitat County P.U.D. Every six months BPA has the option to change rates. BPA's average wholesale priority firm rates decreased from \$2.91/kwh at September 30, 2006 to \$2.73/kwh at October 1, 2007. The District's electric retail rates remained unchanged in 2007.

The District has a contract with the City of Port Angeles to purchase water to serve the needs of 1,548 District water customers out of a total of 4,270 water customers. The District owns other water sources that serve the needs of the rest of the water customers. The City's wholesale water rate increased by 17.5% during 2007. The District's water retail rates remained unchanged in 2006. In April 2007 the District approved a 15% increase in water rates for all systems effective May 1<sup>st</sup>. In December 2007 the District approved a 6.5% increase in water rates effective January 1<sup>st</sup> 2008. Also in December 2007 the District approved a 10% increase in sewer rates effective January 1<sup>st</sup>, 2008.

Between 2006 and 2007 the electric system customers increased by 695 or 2.40%. Gross electric system operating revenue increased by approximately \$5 million, Sales to retail customers increase by approximately \$1.5 million during 2007 or 3.7% Broadband sales increased by \$89,000 or 37% over

2006. The majority of the increase came from an increase in sales to Port Townsend Paper or approximately \$3.4 million. Sales to PTP started in October 2006; therefore 2007 represented the first full year of revenues.

The water systems' customers increased by 66 or 1.57% during 2007. Water system revenues increased by \$110,000 or 5.5% during 2007.

The District ended 2007 with \$21,112,946 unrestricted cash and \$1,168,939 restricted cash. These levels of cash are enough to provide adequate insurance for meeting continuing cash flow needs. The District also is maintaining debt service coverage levels well above the minimum required level of 1.25 in the District's Bond Covenants.

### **Financial Analysis**

The following information provides analysis of the 2007, 2006 and 2005 condensed financial information provided in the following table.

#### **Condensed Statement of Net Assets (000's)**

	<u>2007</u>	<u>2006</u>	<u>Change</u>	<u>% Change</u>	<u>2005</u>
Current Assets	31,407	36,726	-5,319	-14.5%	32,963
Utility Plant, Net	111,279	98,756	12,523	12.7%	90,616
Other Noncurrent Assets	1,634	1,497	137	9.2%	1,821
<b>Total Assets</b>	<b>144,320</b>	<b>136,979</b>	<b>7,341</b>	<b>5.4%</b>	<b>125,400</b>
Current Liabilities	13,418	11,034	2,384	21.6%	7,751
Noncurrent Liabilities	17,774	17,807	-33	-0.2%	15,687
<b>Total Liabilities</b>	<b>31,192</b>	<b>28,841</b>	<b>2,351</b>	<b>8.2%</b>	<b>23,438</b>
Invested in Capital Assets	97,058	83,878	13,180	15.8%	75,699
Restricted for:					
Capital Projects	15	14	1	7.1%	21
Debt Service	1,154	1,144	10	0.9%	1,173
Unrestricted	14,901	23,102	-8,201	-35.5%	25,069
<b>Total Net Assets</b>	<b>113,128</b>	<b>108,138</b>	<b>4,990</b>	<b>4.6%</b>	<b>101,962</b>

#### **Condensed Statement of Revenue, Expenses and Changes in Net Assets (000's)**

	<u>2007</u>	<u>2006</u>	<u>Change</u>	<u>% Change</u>	<u>2005</u>
Operating Revenues	49,416	44,311	5,105	11.5%	41,589
NonOperating Revenues	1,462	1,431	31	2.2%	997
<b>Total Revenues</b>	<b>50,878</b>	<b>45,742</b>	<b>5,136</b>	<b>11.2%</b>	<b>42,586</b>
Operating Expenses	46,787	42,051	4,736	11.3%	37,744
NonOperating Expenses	734	696	38	5.2%	894
<b>Total Expenses</b>	<b>47,521</b>	<b>42,747</b>	<b>4,774</b>	<b>11.2%</b>	<b>38,638</b>
Contributions in Aid	1,633	3,181	-1,548	-48.7%	3,165
Change in Net Assets	4,990	6,176	-1,186	-19.2%	7,113
Net Assets – beginning of year	108,138	101,962	6,176	6.1%	94,849
<b>Net Assets – end of year</b>	<b>113,128</b>	<b>108,138</b>	<b>4,990</b>	<b>4.6%</b>	<b>101,962</b>

## **Assets**

Total assets increase by \$7,341,000 or 5.4% in 2007. This increase was mostly due to a net increase in Capital Assets of \$12,523,000. While current assets decreased by 14.5% or \$5,319,000 in 2007 mostly due to a decrease in cash and inventory. Electric Capital projects included distribution pole replacements, underground replacements, transmission rebuilds and beginning construction of a new substation. Water Net Plant Assets increased by \$624,490 in 2007. The increase in net assets included completion of the new water treatment plant and upgrades to water mains, services and hydrants throughout all water systems.

## **Liabilities**

Total liabilities increased by \$2,320,000 or 8% in 2007, mainly due to an increase in current liabilities. Current liabilities increased because of increased payables accrued at year-end for the new substation construction and a timing difference between warrants issued and redeemed. In 2007, current liabilities increased 21.6% or \$2,384,000 over 2006. Long-term debt decreased \$805,549 from 2006 to 2007. Electric and water debt payments were \$987,900 principal and \$574,512 interest.

## **Net Assets**

The 2007 net assets increased by \$4,990,000 or 4.6% over 2006. This increase was partially from customer contributions of \$1,632,875 in 2007 which were just over half the amount received in the prior year.

## **Operating Revenues**

The 2006 operating revenues increased by 6.5% over 2005, an increase of \$2,722,000. In 2007, operating revenues increased by 11.5% or \$5,105,000 over 2006. The District electric customers increased by 581 in 2006 and 695 in 2007. Water customers increased by 132 in 2006 and 66 in 2007.

## **Operating Expenses**

Operating expenses increased \$4,307,000 or 11.4% in 2006. Operating expenses in 2007 increased \$4,736,000 or 11.3%. Increases in purchased power, purchased water and maintenance of the system were primarily responsible for the increase in operating expenses. Purchased power increased due to an additional load as a result of the supplemental power contract with Port Townsend Paper.

## **Capital Assets and Long Term Debt Activity**

Electric Net Plant Assets increased by \$5,674,769 in 2006 and \$11,910,750 in 2007. The main capital projects included distribution pole replacements, underground replacements, transmission rebuilds and beginning construction of a new substation. Water Net Plant Assets increased by \$2,480,969 in 2006 and \$624,490 in 2007. The increase in Water net assets in 2006 included construction of the new water treatment plant and upgrades to water mains, services and hydrants throughout all water systems. The increase in 2007 Water Net Plant Assets included completion of the Water Treatment Plant and upgrades to water mains, services and hydrants through all water systems.

No new Electric debt was issued in 2006 or 2007. Payments made to the Electric Revenue and Refunding bond of 2001 consisted of \$535,850 in interest and \$720,000 in principal in 2006; and \$502,775 in interest and \$750,000 in principal in 2007. The electric debt service coverage ratio was 5.12 in 2006 and 6.63 in 2007. The bond covenant requires a minimum of 1.25. The District paid \$41,593 interest and \$56,726 principal to the 2003 Water revenue loan and \$6,500 principal and \$580 interest to the 1991 Bond Series LUD 10 in 2006 and paid \$14,581 interest to the State of Washington Drinking Water State Revolving Fund Loan. In 2006, the District borrowed an additional \$1,887,500, bringing the total funds borrowed to \$3,187,330 from the State of Washington Drinking Water State Revolving Fund Loan. In 2007, the District paid the final principal of \$2,500 to the 1991 Bond Series LUD 10. The District paid \$39,100 in interest and \$59,219 in principal to the 2003 Water Revenue Loan and \$32,637 in interest

and \$178,681 in principal to the State of Washington Drinking Water Revolving Loan Fund. The District borrowed an additional \$207,600 in 2007 bringing the total borrowed to \$3,394,930 from this revolving loan. The District closed out the loan in 2007 and did not borrow the total available of \$3,535,000. The water debt service coverage for 2007 is 6.16 and in 2006 was 3.51. The water bond covenant requires a minimum of 1.25. The District maintained compliance with its required bond covenants.

**Public Utility District No. 1 of Clallam County, Washington**  
**Statement of Net Assets**  
**Year Ended December 31, 2007 and 2006**

<b>Assets</b>	<b>2007</b>	<b>2006</b>
<b>CURRENT ASSETS</b>		
Cash, Including Temp. Investments	\$21,112,946	\$25,464,675
Accts. Receivable, Net of Provision for Uncollectible Accounts of \$60,535 and \$57,804 (Note 2)	3,158,591	3,212,273
Accounts Receivable - Other	1,117,243	996,710
Materials & Supplies, at Aver. Cost	4,731,379	5,576,651
Prepayments	1,113,763	1,203,920
Accrued Interest Receivable	173,322	271,789
<b>TOTAL CURRENT ASSETS</b>	<b>31,407,244</b>	<b>36,726,018</b>
<b>NONCURRENT ASSETS</b>		
<b>RESTRICTED ASSETS</b>		
Bond Funds Cash & Invest. (Note 1)	126,298	131,372
Funds Held by Fiscal Agent	1,027,950	1,012,325
Construction Fund 2001/2003	14,691	13,954
<b>TOTAL RESTRICTED ASSETS</b>	<b>1,168,939</b>	<b>1,157,651</b>
<b>UTILITY PLANT, at Cost</b>		
Plant in Service (Note 1)	152,375,981	141,211,330
Construction Work in Progress	16,725,649	10,282,755
<b>TOTAL UTILITY PLANT</b>	<b>169,101,630</b>	<b>151,494,085</b>
Less: Accumulated Depreciation	57,823,179	52,738,131
<b>NET UTILITY PLANT</b>	<b>111,278,451</b>	<b>98,755,954</b>
Assessments Receivable	4,648	6,787
Deferred Charges	460,703	332,902
<b>TOTAL NONCURRENT ASSETS</b>	<b>112,912,741</b>	<b>100,253,294</b>
<b>TOTAL ASSETS</b>	<b>\$144,319,985</b>	<b>\$136,979,312</b>

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

# Public Utility District No. 1 of Clallam County, Washington

## Statement of Net Assets

Year Ended December 31, 2007 and 2006

<b>Liabilities and Net Assets</b>	<b>2007</b>	<b>2006</b>
<b>CURRENT LIABILITIES</b>		
Accounts Payable	\$9,987,871	\$7,858,830
Customer Deposits	1,120,842	1,096,630
Accrued Taxes Payable	1,192,798	1,188,349
Other Payables	1,116,565	890,030
<b>TOTAL CURRENT LIABILITIES</b>	<b>13,418,076</b>	<b>11,033,839</b>
<b>PAYABLES FROM RESTRICTED ASSETS</b>		
Insurance Fund (Note 11)		
Accrued Interest Payable	260,290	277,201
Current Maturities/Long-Term Debt	1,023,001	984,489
<b>TOTAL PAYABLES FROM RESTRICTED ASSETS</b>	<b>1,283,291</b>	<b>1,261,690</b>
<b>NONCURRENT LIABILITIES</b>		
Revenue Bonds Payable(Note 4)	13,087,612	13,893,161
Customer Advances for Construction	2,783,571	2,032,153
Miscellaneous Deferred Credits	619,126	620,715
<b>TOTAL NONCURRENT LIABILITIES</b>	<b>16,490,309</b>	<b>16,546,029</b>
<b>NET ASSETS</b>		
Invested in Capital Assets, Net of Related Debt	97,057,938	83,878,304
Restricted For		
Capital Projects	14,691	13,954
Debt Service	1,154,248	1,143,697
Unrestricted	14,901,432	23,101,799
<b>TOTAL NET ASSETS</b>	<b>113,128,309</b>	<b>108,137,754</b>
<b>TOTAL LIABILITIES &amp; NET ASSETS</b>	<b>\$144,319,985</b>	<b>\$136,979,312</b>

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

**Public Utility District No. 1 of Clallam County, Washington**  
**Statement of Revenue, Expenses, and Changes in Net Assets**  
**Year Ended December 31, 2007 and 2006**

	2007	2006
<b>OPERATING REVENUES</b>	<b>\$49,416,493</b>	<b>\$44,310,795</b>
<b>OPERATING EXPENSES</b>		
Operations		
Purchased Power (Note 8)	25,453,398	22,406,708
Purchased Water (Note 8)	254,723	240,662
Other Expenses	10,177,439	9,124,917
Maintenance	3,265,548	3,260,034
General Taxes	2,555,237	2,413,382
Depreciation and Amortization	5,080,375	4,605,234
<b>TOTAL OPERATING EXPENSES</b>	<b>46,786,720</b>	<b>42,050,937</b>
<b>NET OPERATING INCOME</b>	<b>2,629,773</b>	<b>2,259,858</b>
<b>NONOPERATING REVENUES AND EXPENSES</b>		
<b>NONOPERATING REVENUES</b>		
Interest Income	1,208,651	1,278,802
Miscellaneous Nonoperating Income	253,729	152,005
<b>TOTAL NONOPERATING REVENUES</b>	<b>1,462,380</b>	<b>1,430,807</b>
<b>NONOPERATING EXPENSES</b>		
Interest Expense	558,959	582,427
Misc Non-Operating Expenses	175,514	113,564
<b>TOTAL NONOPERATING EXPENSES</b>	<b>734,473</b>	<b>695,991</b>
<b>NET NONOPERATING INCOME</b>	<b>727,907</b>	<b>734,816</b>
<b>CONTRIB. IN AID OF CONSTR.</b>	(Note 1) 1,632,875	3,181,430
<b>CHANGE IN NET ASSETS</b>	<b>4,990,555</b>	<b>6,176,104</b>
Net Assets, January 1	108,137,754	101,961,650
<b>NET ASSETS, December 31</b>	<b>113,128,309</b>	<b>108,137,754</b>

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

# Public Utility District No. 1 of Clallam County, Washington

## Statement of Cash Flow

Year Ended December 31, 2007 and 2006

	2007 Total	2006 Total
<b>CASH FLOW FROM OPER. ACTIVITIES</b>		
Cash Received from Customers and Others	49,245,278	45,258,018
Other Cash Receipts	319,448	268,040
Cash Paid to Suppliers and Employees	(38,458,081)	(36,753,121)
Other Cash Payments	(272,253)	(157,532)
<b>Net Cash Provided From Operating Activities</b>	<b>10,834,392</b>	<b>8,615,405</b>
<b>CASH FLOW FROM CAPITAL &amp; RELATED FINANCING ACTIVITIES</b>		
Acquisition and Construction of Capital Assets	(17,570,981)	(12,713,561)
Capital Contributions	2,445,561	3,855,253
LUD Assessment Payments	2,139	12,492
Proceeds from Revenue Bond	207,600	1,887,500
Principal & Interest Paid on Capital Debt	(1,566,269)	(1,376,587)
<b>Net Cash Used by Capital &amp; Related Financing Activities</b>	<b>(16,481,950)</b>	<b>(8,334,903)</b>
<b>CASH FLOW FROM INVESTING ACTIVITIES</b>		
Interest Income	1,307,117	1,226,308
<b>Net Cash Provided by Investing Activities</b>	<b>1,307,117</b>	<b>1,226,308</b>
<b>NET INCREASE (DECREASE) IN CASH</b>	<b>(4,340,441)</b>	<b>1,506,810</b>
<b>Cash Balances - Beginning of the Year</b>	<b>26,622,326</b>	<b>25,115,516</b>
<b>Less Restricted Cash</b>	<b>(1,168,939)</b>	<b>(1,157,651)</b>
<b>Unrestricted Cash Balances - End of the Year</b>	<b>21,112,946</b>	<b>25,464,675</b>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Operating Income (Loss)	2,629,773	2,259,858
<b>Adjustments to reconcile Operating Income To Net Cash Provided by Operating Activities</b>		
<b>Add:</b>		
Depreciation	5,080,375	4,605,234
Other Non-Operating (Receipts) Payments	78,217	38,440
<b>Changes in Assets and Liabilities</b>		
(Increase) Decrease in Accounts Receivable	53,151	(336,525)
(Increase) Decrease in Other Receivables	(181,270)	519,260
(Increase) Decrease in Materials	845,272	(1,981,858)
(Increase) Decrease in Prepayments	90,157	(330,913)
(Increase) Decrease in Deferred Charges	(143,930)	232,579
(Increase) Decrease in Other Assets	0	
Increase (Decrease) in Accounts Payable	2,129,040	2,591,928
Increase (Decrease) in Customer Deposits	24,212	487,401
Increase (Decrease) in Accrued Taxes	4,449	59,293
Increase (Decrease) in Other Payables	226,535	130,263
Increase (Decrease) in Restricted Assets	0	(52,723)
Increase (Decrease) in Deferred Credits	(1,589)	393,168
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>10,834,392</b>	<b>8,615,405</b>

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

PUBLIC UTILITY DISTRICT NO. 1 OF CLALLAM COUNTY, WASHINGTON  
NOTES TO THE COMBINED FINANCIAL STATEMENTS  
2007 and 2006

NOTE 1 ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization

Public Utility District No. 1 of Clallam County, Washington ("District") is a single enterprise fund with financial activities in the areas of electric, water, and sewer. The District was voted into existence on November 5, 1940, and became live at 11:00 am on July 15, 1944. In 1945, the District began providing water to the Gales Addition area. On November 5, 1990, the voters authorized the District to provide sewer services.

The District is comprised of an electric system, nine (9) water systems, and three (3) sewer systems. The accompanying financial statements for 2007 and 2006 include the financial position of the Electric System, the Water Systems, and the Sewer Systems and the results of their operations. These statements include all inter-department transactions and report the obligations owing at December 31, 2007, and December 31, 2006.

The Electric System provides certain services to the Water and Sewer Systems, which are recorded as inter-department charges. The financing arrangements provide for the maintenance of specific funds and the District is required to follow accounting procedures prescribed by the State of Washington, under the authority of Chapter 43.09 RCW.

Basis of Accounting Procedures

The accounting policies of Public Utility District No. 1 of Clallam County conform to generally accepted accounting principles as applicable to proprietary funds of governments. Accounts are maintained in accordance with the Uniform System of Accounts for Public Utilities and Licenses as published by the Federal Energy Regulatory Commission (FERC). The District uses the full accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Fixed assets are capitalized and long-term liabilities are accounted for in the appropriate funds. The District implemented GASB 34 in 2003, requiring the Balance Sheet to be restated in terms of Statement of Net Assets. Also a Management's Discussion and Analysis precedes the financial statements as required supplementary information under GASB 34.

Revenue Recognition

Revenues are based only on monthly cyclical billings to customers. This system of billing results in earned but unbilled revenues at year-end which are not included in the financial statements. Estimated earned but unbilled revenues at December 31, 2007, 2006, and 2005 were \$1,752,032, \$1,675,418, and \$1,575,162, respectively. The net cumulative effect on revenues at December 31, 2007 and 2006 was (\$76,614) and (\$100,256), respectively.

Cash and Cash Equivalents

For purposes of reporting cash flows, the District considers cash equivalents as short-term, highly liquid investments that are both readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates.

As required by state law, all monies of the District are invested in obligations of the U. S. Government or deposited in Washington state banks or savings and loan institutions, which have been approved by the Washington Public Protection Commission. The District records all investments at cost as cash equivalents. Short-term investments, less than a year, are invested in local banks in the form of Certificates of Deposit that are held to maturity and do not fluctuate in value. As required by GASB

Statement No. 31, the District records all other investments at fair value based on quoted market rates, with changes in unrealized gains and losses reported as investment income unless the difference is immaterial. The District's intention and practice is to hold all investments until maturity. Total investments comprised of Time Deposits, at cost, were \$20,143,416 in 2006 and \$15,561,264 in 2007.

#### Allowance for Accounts Receivable

Management reviews accounts receivable and provides for estimated uncollectible accounts. Accounts deemed uncollectible are transferred to the provision for uncollectible accounts on a monthly basis.

#### Inventories

Materials and supplies inventories are valued at average cost.

#### Utility Plant

Utility Plant Assets are stated at cost. The provision for depreciation is determined by the straight-line method over the estimated useful life. Composite rates are used for groups of assets and, accordingly, no gain or loss is recorded on the retirement of an asset unless it represents a major retirement. The cost of maintenance and repairs is expensed as incurred; renewals, replacements, and betterments are capitalized. The estimated useful life of assets range from 5 to 50 years for the Electric Distribution System, Water Systems, and Sewer Systems assets. See Note 3 on page 8 for more information.

#### Preliminary Survey Charges

Preliminary survey charges incurred for proposed projects are deferred pending construction of the facility. Charges relating to projects ultimately constructed are transferred to utility plant; charges relating to projects abandoned are charged to expense.

#### Unamortized Debt Expense

Costs relating to the sale of bonds and bond discounts are amortized over the lives of the various bond issues by the straight-line method.

#### Contribution in Aid of Construction

Contributions, from customers, for construction of capital plant were accounted for as equity for many years. Governmental Accounting Standards Board (GASB) Statement No. 33 addresses accounting for non-exchange transactions. Beginning in 2001, the District changed accounting for contributions, in accordance with Statement No. 33, to a revenue transaction.

For the year ended December 31, 2007 and 2006 the District reported Contributions in Aid of Construction of \$1,632,875 and \$3,181,430, respectively. For 2007 contributions reported in the Electric System were \$870,099, Water Systems were \$753,339, and Sewer Systems were \$9,436. For 2006 contributions reported to the Electric System were \$2,142,295, Water Systems were \$990,655, and Sewer Systems were \$48,480.

#### Allowance for Funds Used During Construction

An allowance for funds used during construction is capitalized as a component of cost of construction projects and is credited to interest charges. This allowance represents the cost to finance construction. The allowance totaled \$0 and \$379 for 2007 and 2006, respectively.

### Reclassifications

Certain financial statement amounts have been reclassified from the previous year with no effect on the change in net assets.

### NOTE 2 ACCOUNTS RECEIVABLE

The customers accounts receivable contain credit balances as a result of advance payments from the Average Payment Plan residential customers. The total dollar amount of the credit balances were approximately \$263,320 at December 31, 2007, and \$226,379 at December 31, 2006. All customer meters are read and billed monthly. Management reviews accounts receivable and provides for estimated uncollectible accounts on a monthly basis. Customer accounts receivable is presented in the statement of net assets net of uncollectible balance.

### NOTE 3 UTILITY PLANT

The District has a capitalization policy for purchases over \$1,000 with a useful life of greater than one year. Property, plant and equipment are depreciated using the straight-line method over estimated useful lives ranging from 5 to 50 years. Disposal recordings are booked to accumulated depreciation. A gain or loss is recorded for any significant disposals. There were no significant disposals in 2007 or 2006.

Utility plant activity for the year ended December 31, 2007, was as follows:

<u>Electric Plant Assets</u>	<u>2006 Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>2007 Balance</u>
Utility Plant-Non Depreciable				
Franchises	\$ 32,933	\$ 4,412		\$ 37,345
Construction Work In Progress	6,450,452	6,179,059		12,629,511
Land & Land Rights	<u>2,456,931</u>	<u>-561,664</u>		<u>1,895,267</u>
Total Non-Depreciable	<u>\$ 8,940,316</u>	<u>\$ 5,621,807</u>		<u>\$ 14,562,123</u>
Utility Plant-Depreciable				
Organization	\$ 14,502			\$ 14,502
Generators	5,292			5,292
Transmission	11,682,813	\$ 1,495,818	\$ 37,964	13,140,667
Distribution	91,332,719	8,696,777	262,662	99,766,834
General Plant	<u>19,250,395</u>	<u>1,094,722</u>	<u>260</u>	<u>20,344,857</u>
Total Depreciable	<u>\$122,285,721</u>	<u>\$11,287,317</u>	<u>\$ 300,886</u>	<u>\$133,272,152</u>
Total Electric Plant	\$131,226,037	\$16,909,124	\$ 300,886	\$147,834,275
Less Accumulated Depreciation	<u>48,187,515</u>	<u>4,697,488</u>		<u>52,885,003</u>
Net Electric Plant	<u>\$ 83,038,522</u>	<u>\$12,211,636</u>	<u>\$ 300,886</u>	<u>\$ 94,949,272</u>
<u>Water Plant Assets</u>	<u>2006 Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>2007 Balance</u>
Utility Plant-Non Depreciable				
Franchise & Consent	\$ 14,271			\$ 14,271
Land & Land Rights	233,694			233,694
Construction Work in Progress	<u>3,832,303</u>	<u>\$ 260,529</u>		<u>4,092,832</u>
Total Non-Depreciable	<u>\$ 4,080,268</u>	<u>\$ 260,529</u>		<u>\$ 4,340,797</u>
Utility Plant-Depreciable				
Transmission & Distribution	\$ 15,062,132	\$ 703,701	\$ 20,714	\$ 15,745,119
General	<u>546,449</u>	<u>51,582</u>		<u>598,031</u>
Total Depreciable	<u>\$ 15,608,581</u>	<u>\$ 755,283</u>	<u>\$ 20,714</u>	<u>\$ 16,343,150</u>
Total Water Plant	\$ 19,688,849	\$ 1,015,812	\$ 20,714	\$ 20,683,947
Less Accumulated Depreciation	<u>4,380,076</u>	<u>416,802</u>	<u>46,194</u>	<u>4,750,684</u>
Net Water Plant	<u>\$ 15,308,773</u>	<u>\$ 599,010</u>	<u>\$(25,480)</u>	<u>\$ 15,933,263</u>
<u>Sewer Plant Assets</u>	<u>2006 Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>2007 Balance</u>
Utility Plant-Non Depreciable				
Land & Land Rights	\$ 31,105			\$ 31,105
Construction Work in Progress	<u>0</u>	<u>\$ 3,306</u>		<u>3,306</u>
Total Non-Depreciable	<u>\$ 31,105</u>	<u>\$ 3,306</u>		<u>\$ 34,411</u>
Utility Plant-Depreciable				
General	<u>\$ 548,094</u>	<u>\$ 903</u>		<u>\$ 548,997</u>
Total Sewer Plant	579,199	4,209		583,408
Less Accumulated Depreciation	<u>170,540</u>	<u>16,952</u>		<u>187,492</u>
Net Sewer Plant	<u>\$ 408,659</u>	<u>\$ (12,743)</u>		<u>\$ 395,916</u>

<u>Combined Plant Assets</u>	<u>2006 Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>2007 Balance</u>
Utility Plant-Non Depreciable				
Franchises	\$ 47,204	\$ 4,412		\$ 51,616
Construction Work In Progress	10,282,755	6,442,894		16,725,649
Land & Land Rights	<u>2,721,730</u>	<u>(561,664)</u>		<u>2,160,066</u>
Total Non-Depreciable	<u>\$ 13,051,689</u>	<u>\$ 5,885,642</u>		<u>\$ 18,937,331</u>
Utility Plant-Depreciable				
Organization	\$ 14,502			\$ 14,502
Generators	5,292			5,292
Transmission	11,682,813	\$ 1,495,818	\$ 37,964	13,140,667
Distribution	106,394,851	9,400,478	283,376	115,511,953
General Plant	<u>20,344,938</u>	<u>1,147,207</u>	<u>260</u>	<u>21,491,885</u>
Total Depreciable	<u>\$138,442,396</u>	<u>\$12,043,503</u>	<u>\$321,600</u>	<u>\$150,164,299</u>
Total Combined Plant	\$151,494,085	\$17,929,145	\$321,600	\$169,101,630
Less Accumulated Depreciation	<u>52,738,131</u>	<u>5,131,242</u>	<u>46,194</u>	<u>57,823,179</u>
Net Combined Plant	<u>\$ 98,755,954</u>	<u>\$12,797,903</u>	<u>\$275,406</u>	<u>\$111,278,451</u>

#### NOTE 4 LONG-TERM DEBT

Long-term debt obligations of the District are payable as follows:

<u>Electric System</u>	<u>2007</u>	<u>2006</u>
2001 Electric Revenue Refunding Bonds		
4.50% - 5.50% due 2003-2017	\$ 9,800,000	\$10,550,000
Unauthorized Loss/Premiums on Bonds	<u>242,443</u>	<u>226,680</u>
TOTAL ELECTRIC	<u>\$10,042,443</u>	<u>\$10,776,680</u>
<u>Water System</u>		
1991 LUD#10 Bonds		
6.15% - 7.25% due 2006		\$ 2,500
2003 Water Revenue Bond		
4.36% due 2018	\$ 851,920	911,139
2005 Drinking Water Loan		
1% Due 2025	<u>3,216,250</u>	<u>3,187,330</u>
TOTAL WATER	<u>\$ 4,068,170</u>	<u>\$ 4,100,969</u>
TOTAL LONG-TERM DEBT	<u>\$14,110,613</u>	<u>\$14,877,649</u>

The annual requirement to amortize all debts outstanding as of December 31, 2007, including interest, are as follows:

Years Ending <u>December 31</u>	Electric System		Water System		<u>Total</u>
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	
2008	\$ 785,000	\$ 466,275	\$ 240,133	\$ 68,472	\$ 1,559,880
2009	825,000	427,056	243,346	63,879	1,559,281
2010	865,000	386,919	246,196	59,242	1,557,357
2011	905,000	343,750	249,172	54,479	1,552,401
2012	950,000	297,375	252,279	49,585	1,549,239
2013-2017	5,470,000	741,663	1,313,018	169,501	7,694,182
2018-2022			987,984	55,276	1,043,260
2023-2026			<u>536,042</u>	<u>9,853</u>	<u>545,895</u>
TOTALS	<u>\$9,800,000</u>	<u>\$2,663,038</u>	<u>\$4,068,170</u>	<u>\$530,287</u>	<u>\$17,061,495</u>

The District has \$1,154,248 in restricted assets held in reserve for payment of the District's long-term obligations as required by bond indentures. Also, the Water System has \$14,691, in Construction Fund money from recent bond proceeds. One requirement of the indentures is for the District to maintain a minimum of 1.25 ratio of operating revenues to debt service. As of year end, the District was in compliance with all requirements of the Bond Covenants.

#### Electric Debt

The District issued \$13,245,000 in Electric System Revenue & Refunding Bonds dated September 15, 2001, with interest rates varying from 4.50% and 5.50% over 15 years. The money was borrowed to refund \$5,000,000 borrowed from a Line of Credit with Bank of America and to partially refund the outstanding \$3,415,000 principal amount of the Electric Revenue & Refunding Bonds, Series 1992. In addition, the proceeds of the Electric System Revenue Refunding Bond, 2001, reimbursed the Electric Operating Fund for previously constructed capital projects and provided funds for future capital improvements of the Electric System.

In lieu of maintaining a Bond Reserve Fund, it was decided to purchase a Bond Insurance Policy through Financial Security Assurance, Inc. The Bond Insurance Policy guarantees the scheduled payment of principal and interest on the bonds.

#### Water Debt

The District issued \$1,079,000 in Water System Revenue and Refunding Bonds dated October 6, 2003, with an interest rate of 4.36% over 15 years. The money was borrowed to refund \$195,238.61 borrowed from a line of credit with Bank of America and to refund the outstanding \$440,000 principal amount of the Water Revenue and Refunding Bonds, 1993.

In addition, the proceeds of the Water System Revenue and Refunding Bond, 2003, reimbursed the Water Operating Fund for previously constructed capital projects and provided funds for future capital improvement of the Water System.

The District entered into a loan agreement in 2003 for a State of Washington Drinking Water State Revolving Fund Loan in the amount of \$1,825,290 at 1.5% interest. This agreement was renegotiated in 2005 in the amount of \$3,535,000 at 1% interest. The term of the loan would not exceed 20 years with the final payment due on October 1, 2025. The first payment was due October 1, 2006, for interest only. In 2006, the District borrowed \$1,887,500, bringing the total funds borrowed to \$3,187,330 on this loan. In 2007 the District borrowed an additional \$207,600 bringing the total funds borrowed to \$3,394,930 on this loan. The District closed out the loan in 2007 and did not borrow the total available of \$3,535,000. The money was borrowed to replace an existing Water Treatment Plant with new and better technology.

## NOTE 5 PENSION PLANS

Substantially all District full-time and qualifying part-time employees participate in one of the statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer public employee defined benefit and defined contribution retirement plans. The 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. The following disclosures are made pursuant to GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers*.

### PUBLIC EMPLOYEES' RETIREMENT SYSTEM (PERS) PLANS 1, 2, AND 3

#### Plan Description

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.

Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior courts (other than judges currently in a judicial retirement system); employees of legislative committees; community and technical colleges, college and university employees not participating in national higher education retirement programs; judges of district and municipal courts; and employees of local governments.

PERS participants 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 exercise an option to transfer their membership to Plan 3. PERS participants 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 PERS Plan 3. The option must be exercised within 90 days of employment. An employee is reported in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to PERS Plan 3.

PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PERS retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

Plan 1 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement at any age after 30 years of service or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2 percent of the average final compensation per year of service, capped at 60 percent. The average final compensation is based on the greatest compensation during any 24 eligible consecutive compensation months. Plan 1 retirements from inactive status prior to the age of 65 may receive actuarially-reduced benefits. The benefit is actuarially reduced to reflect the choice of survivor option. A cost-of-living allowance (COLA) is granted at age 66 based upon years of service times the (COLA) amount, increased by 3 percent annually. Plan 1 members may also elect to receive an additional COLA amount (indexed to the Seattle Consumer Price Index), capped at 3 percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

Plan 2 members are vested after the completion of five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of 2 percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Plan 2 retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial

reduction will apply. The benefit is also actuarially reduced 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 (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit portion provides a benefit calculated at 1 percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Effective June 7, 2006, Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service; or after five service credit years earned in PERS Plan 2 prior to June 1, 2003. Vested Plan 3 members are eligible to retire with full benefits at 65, or at age 55 with 10 years of service. Retirements prior to the age of 65 received reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit, and Plan 3 provides the same cost-of-living allowance as Plan 2.

The defined contribution portion can be distributed in accordance with an option selected by the member, either as a lump sum or pursuant to other options authorized by the Employee Retirement Benefits Board.

There are 1,188 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of September 30, 2006:

Retirees and Beneficiaries Receiving Benefits	70,201
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	25,610
Active Plan Members Vested	105,215
Active Plan Members Nonvested	<u>49,812</u>
TOTAL	<u>250,838</u>

Funding Policy

Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and 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 officers. 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. All employers are required to contribute at the level established by the Legislature. Under PERS Plan 3, employer contributions finance the defined benefit portion of the plan, and member contributions finance the defined contribution portion of the plan. The Employee Retirement Benefits Board sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee's age. 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, 2007, were as follows:

	<u>PERS Plan 1</u>	<u>PERS Plan 2</u>	<u>PERS Plan 3</u>
Employer*	6.13%	6.13%	6.13%**
Employee	6.00%	4.15%	***

\*The employer rates include the employer administrative expense fee currently set at 0.16%.

\*\*Plan 3 defined portion only.

\*\*\*Variable from 5.0% minimum to 15.0% maximum based on rate selected by the PERS 3 member.

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

	<u>PERS Plan 1</u>	<u>PERS Plan 2</u>	<u>PERS Plan 3</u>
2007	\$ 40,179	\$378,405	\$73,882
2006	\$ 30,752	\$190,047	\$27,927
2005	\$ 18,494	\$100,888	\$13,792

**NOTE 6 SELF INSURANCE**

The District is a member of the Public Utility Risk Management Services (PURMS) Self-Insurance fund. There are currently 19 members of PURMS. The fund consists of three pools for liability, property, and Health and Welfare coverage. The District is a participant in all three pools.

The pools are fully funded by its current and former members. Members file claims with the administrator, Pacific Underwriters in Seattle, Washington, which has been contracted to provide claims adjustment and loss prevention services.

The pools are governed by a Board of Directors comprised of one designated representative from each participating member. The administrator and elected Administrative Committee conduct the business of the pools.

Members that withdraw from the fund are still responsible for their share of the assessments for occurrences while they were members. Likewise terminated members continue to receive coverage for the time they were members.

PURMS Liability Pool is presently composed of nineteen (19) members. The Fund self insures each incident for the first \$1,000,000 and has purchased excess General Comprehensive Liability Insurance coverage of \$35,000,000 per incident from Associated Electric & Gas Insurance Services, Ltd. (AEGIS) plus \$25,000,000 from Energy Insurance Mutual, Ltd. (EIM). The policies are renewable in January 2009. Public Officials' Liability Insurance in excess of \$500,000 is insured by AEGIS Insurance Company for \$10,000,000 per incident and an aggregate of \$35,000,000 renewable in July 2008.

PURMS Property Pool is comprised of seventeen (17) members. The Fund self insures each incident for the first \$500,000 and has purchased a Pool excess limit of \$100,000,000. The District and other members of the Pool have also purchased an additional property and vehicle policy with coverage to \$25,000,000.

The District participates in the PURMS Health and Welfare pool for medical and dental coverage. This Pool is comprised of twelve (12) members. The Pool purchases excess insurance with an individual limit of \$150,000.

The District is self insured for unemployment insurance and reimburses the State of Washington for any claims paid. There were no unemployment claims paid in 2007 and 2006.

**NOTE 7 CONSERVATION PROGRAMS**

The Conservation and Renewables Discount (C&RD) is a credit that was available to Bonneville Power Administration's (BPA) regional wholesale power customers that takes action to further conservation and renewable resource development. The rate period is four years long and runs from October 1 through September 30.

The C&RD credit is a \$0.05 per kWh discount off the BPA Firm Power rate and amounted \$302,568 and \$307,140 for 2006 and 2007, respectively.

A credit is earned from the installation of conservation measures or by making other qualifying expenditures for renewable energy, qualified research projects, or through donations to qualifying organizations. At the end of the rate period, customers pay BPA for any C&RD credits not accounted for. The District claimed its total 2002 – 2006 C&RD by the end of 2004.

The credit continues to be available to the District for 2007 – 2011. The District anticipates that conservation expenditures will exceed the amount of the credit by the end of the rate period.

## NOTE 8 PURCHASED POWER AND WATER CONTRACTS

### **Bonneville Power Administration (Bonneville)**

The District obtains power from the Bonneville Power Administration under a long-term power purchase agreement. The District's Bonneville power is supplied under a 10-year agreement for the Full Service Product, which extends from October 1, 2001 through September 30, 2011. The Full Service product provides all firm power necessary to meet a customer's actual loads in excess of the customer's small non-dispatchable generating resources. This service includes Heavy Load Hour (HLH) energy, Light Load Hour (LLH) energy, demand (peaking and capacity), and any shaping necessary to cover load variations in Total Retail Load due to temperature changes and load loss/growth except when due to voluntary retail access.

Bonneville is required by federal law to recover all of its costs through the rates it charges its customers. Bonneville makes various filings with FERC to confirm that rates are sufficient to cover costs. Under Bonneville's adopted power and transmission rate provisions, its rates are subject to revision in order to enable Bonneville to recover its actual costs of service. The rate provisions for the Full Service Product include a cost recovery adjustment clause (CRAC) and a dividend distribution clause (DDC).

Either may be triggered if certain thresholds are met. The CRAC, including a special fish related adjustment and emergency fish related surcharge, allows Bonneville to raise rates to collect sufficient funds to pay costs. The DDC results in dollars being returned to customers, in the form of future power rate decreases, if excess dollars are collected.

Pursuant to the Full Service product rate provisions, the District is subject to additional charges or credits from Bonneville if Bonneville's actual costs deviate from budgeted amounts. Bonneville Power Administration's wholesale power rates for the FY 2007-2009 rate period were established during the Wholesale Power WP-07 Rate Case through a formal process described in Section 7(i) of the Northwest Power Act. The current rate case concluded when the Administrator signed the Final Record of Decision on July 17, 2006. The complete rate case record was then sent to the Federal Energy Regulatory Commission (FERC) for their review. FERC granted interim approval to the 2007 Wholesale Power Rates Schedules and General Rate Schedule Provisions (GRSPs) on September 21, 2006. The District also entered into a contract with Bonneville for network transmission service effective May 31, 1997, which provides adequate transmission capacity to meet the District's annual system peak load. The transmission contract extends through September 30, 2031.

### **Klickitat Landfill Natural Gas**

The District has a contract for the purchase of 1 MW of landfill natural gas from Klickitat County Public Utility District. The District has a one year contract that expires on September 30, 2008. For the years ended 2007 and 2006 the amount paid to Klickitat PUD for power was \$354,728 and \$340,203, respectively.

### **Water**

The District is a party to a "Wholesale Water Contract" with the City of Port Angeles through August 16, 2036. The rates are tied to the City's Residential Rate Structure. Gales Addition Reservoir is 89% of the cost per 100 cubic feet under the City's residential rate and the Baker Street Intertie is 85% of the

cost per 100 cubic feet under the City's residential rate. Water rates from January 2006 to December 2008 are as follows:

Gales Addition Reservoir (High Zone)

Jan 2006 – Dec 2006 billing cycle	\$1.25/100 cubic feet/month
Jan 2007 – Dec 2007 billing cycle	\$1.51/100 cubic feet/month
Jan 2008 – Dec 2008 billing cycle	\$1.62/100 cubic feet/month

Baker Street Intertie (Low Zone)

Jan 2006 – Dec 2006 billing cycle	\$1.19/100 cubic feet/month
Jan 2007 – Dec 2007 billing cycle	\$1.45/100 cubic feet/month
Jan 2008 – Dec 2008 billing cycle	\$1.55/100 cubic feet/month

The District's purchased water expense under this contract for 2007 and 2006 was \$254,723 and \$240,662, respectively.

NOTE 9 ASSOCIATION WITH ENERGY NORTHWEST

Energy Northwest (formerly Washington Public Power Supply System [WPPSS]) is a Washington municipal corporation which has acted as a joint operating agency for various power supply initiatives in the Northwest. The District was a member until August 1984 when it withdrew as a member. Subsequent to year end the District rejoined Energy Northwest and became a member in May 2008.

The District has remained contractually interested in the following projects:

Energy Northwest Nuclear Projects Nos. 1, 2, and 3

The District has entered into "net billing agreements" with Energy Northwest and BPA. Under terms of these agreements, the District has purchased a maximum of 1.157%, 1.769%, and 1.001% of the capability of Energy Northwest's Nuclear Projects Nos. 1 and 2 and Energy Northwest's 70% ownership share of its Nuclear Project No. 3, respectively, and has sold this capability to BPA. BPA is unconditionally obligated to pay the District and the District is unconditionally obligated to pay Energy Northwest, the pro rata share of the total annual costs of each project, including the debt service on revenue bonds issued to finance the project whether the projects are completed, operable or operating and notwithstanding the suspension, reduction, or curtailment of the projects' output. The District's respective shares may be increased by not more than 25% upon default of other public agency participants.

Packwood Lake Hydroelectric Project

The Packwood Lake Hydroelectric Project is an Energy Northwest hydroelectric generating project in western Washington with a nameplate rating of 27.5 MW. In 1961 the District executed a contract with Energy Northwest which expires upon payment or the making of provision for payment of Energy Northwest's revenue bonds issued in conjunction with the Packwood Project (scheduled for final payment on March 1, 2012) or when Energy Northwest discontinues operation of the Packwood Project, or, upon the election of the District, 24 months prior to any scheduled termination date. Under the terms of this contract, the District, as a member-purchaser is obligated to purchase **7%** of the capability of the Packwood Project, and is unconditionally obligated to pay 7% of the annual costs of the Project including outstanding bond debt. At the end of 2007, Energy Northwest had approximately \$1.9 million in bond debt outstanding for the Packwood Project. In 2007 Energy Northwest borrowed \$600,000 on a line of credit to pay for repairs caused by flooding in November 2006. Some of the costs of the emergency repairs to stabilize a pipeline where a slide occurred may be reimbursed by the Federal Emergency Management Agency.

Since November 1, 2002, the firm output of 7 aMW, as well as any secondary, or nonfirm, energy, has been sold by Energy Northwest to the Franklin PUD and Benton PUD ("Purchasers") under a separate Power Sales Agreement. The latest amendment to this agreement extended the contract term through September 2008. The Franklin PUD receives 43% of the output and Benton PUD receives the remainder. For the firm energy, the two PUDs currently pay Energy Northwest Bonneville's monthly Priority Firm rate minus \$2 per MWh. The Purchasers pay Energy Northwest the Dow Jones Mid-Columbia Daily Index price, minus \$1 per MWh, for any nonfirm energy. Revenues from power sales are credited to each of the member-purchasers in proportion to their ownership shares. If the amount so credited is less than the member-purchasers' share of the annual costs, they must pay the balance due. If the amount credited exceeds the annual costs, the excess will be paid to the member-purchasers. The District's records show that the Packwood Project credits have exceeded costs since 1981. The Purchasers and Energy Northwest are not obligated to continue the current arrangement beyond September 2008 and neither have declared their intent either to extend or end the arrangement.

#### NOTE 10 FIBER OPTIC SYSTEM

##### NoaNet

The District, along with 13 other Washington State Public Utility Districts and Energy Northwest, is a member of Northwest Open Access Network, Inc. (DBA NoaNet), a Washington nonprofit mutual corporation. NoaNet was incorporated in February 2000 to provide a broadband communications backbone, over Public Benefit Fibers leased from BPA, throughout the Pacific Northwest for assisting its members in the efficient management of load conservation and acquisition of electric energy as well as other purposes. The network began commercial operation in January 2001.

In July 2001, NoaNet issued \$27 million in Telecommunications Network Revenue bonds (taxable) to finance the repayment of the founding members and the costs of initial construction, operations, and maintenance. The Bonds become due beginning in December 2003 through December 2016 with interest due semi-annually at rates ranging from 5.05% to 7.09%. Each member of NoaNet has entered into a Repayment Agreement to guarantee the debt of NoaNet. The District's guarantee is limited to its 7.23% interest or \$1,935,900. A 25% step-up provision in the agreement allows for a maximum exposure of \$2,419,900. The District's recorded as expense member assessments of \$220,301 in 2006 and \$220,357 in 2007.

NoaNet recorded net operating losses of \$1,767,002, and \$2,046,529 for 2007 and 2006, respectively. In accordance with Accounting Principles Board Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*, as well as a position statement issued by the Washington State Auditor concerning the appropriate accounting treatment for NoaNet, a proportionate share of these losses has not been recorded by the District since NoaNet had a negative net equity position of \$12,483,384 as of December 31, 2007, and \$13,789,700 as of December 31, 2006.

Financial statements for NoaNet may be obtained by writing to: Northwest Open Access Network, 21507 42<sup>nd</sup> Avenue, SeaTac, WA 98198.

##### District Fiber Network

The District has installed a fiber optic system in its service area for use by the electric utility. The District has connected its fiber optic system with NoaNet's fiber optic communications network and intends to make excess capacity available to retail service providers.

In 2003 the District implemented a pilot project to test service provider and customer interest in utilizing excess capacity in the District's telecommunications network. A fiber distribution network was constructed connecting approximately 400 District electric customers to the network via direct fiber or wireless connections. A customer acceptance/cost-benefit study was conducted in 2004.

Broadband excess capacity revenues were \$326,994 in 2007 and \$237,738 in 2006. Operations and maintenance expenses were \$425,430 and \$320,696, respectively.

**NOTE 11 COMMITMENTS AND CONTINGENCIES**

In September 2006, the District entered into a contract with Port Townsend Paper and a separate contract with BPA for the purchase and sale of surplus firm power of approximately 17 megawatt hours per month. Under the terms of the purchase agreement with BPA, the District is able to sell up to 17 megawatt surplus power to Port Townsend Paper. The terms of the sales agreement with Port Townsend Paper require the District to sell power it purchases under the terms of the agreement with BPA. The District sells the power to Port Townsend Paper for cost plus an administration fee. As part of the contract, Port Townsend Paper agreed to place cash on deposit equal to the highest estimated monthly bill in addition to prepaying the power bills each month. In January 2007, Port Townsend Paper filed Chapter 11 Bankruptcy. The District believes it is reasonably protected from loss under the terms of the agreement. Total sales under this contract for 2007 and 2006 were \$4,608,271 and \$1,224,513, respectively.

On February 17, 2004, the District entered into a contract with Hawkeye Construction, Inc., to provide certain facilities for the District located near and under the Quillayute River in western Clallam County. The contract is incomplete and certain issues have arisen concerning the contract. The parties are in negotiation on those issues and how to best complete the purpose of the contract.

**NOTE 12 SUBSEQUENT EVENTS**

The District issued \$8,570,000 of Electric System Revenues Bonds dated April 24, 2008, with interest rates ranging from 3.9% to 5% over 20 years. The money was borrowed to fund future capital expenditures.

In lieu of maintaining a Bond Reserve Fund, it was decided to purchase a Surety Bond Insurance Policy through Assured Guaranty. The Surety Policy guarantees the scheduled payment of principal and interest on the bonds

The required debt service payments under the 2008 Revenue Bonds are as follows:

	Principal	Interest	Total
2008	\$ 0	\$ 64803	\$ 64803
2009	0	348195	348195
2010	0	348195	348195
2011	0	348195	348195
2012	0	348195	348195
2013-2017	0	1740975	1740975
2018-2022	3435000	1380525	4815525
2023-2027	4190000	616928	4806928
2028-	945000	18900	963900



## **ABOUT THE STATE AUDITOR'S OFFICE**

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

Our mission is to work in cooperation with our audit clients and citizens as an advocate for government accountability. As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

The State Auditor's Office has 300 employees who are located around the state to deliver our services effectively and efficiently. Approximately 65 percent of our staff are certified public accountants or hold other certifications and advanced degrees.

Our regular audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. We also perform fraud and whistleblower investigations. In addition, we have the authority to conduct performance audits of state agencies and local governments.

The results of our audits are widely distributed through a variety of reports, which are available on our Web site. We continue to refine our reporting efforts to ensure the results of our audits are useful and understandable.

We take our role as partners in accountability seriously. We provide training and technical assistance to governments and have an extensive program to coordinate audit efficiency and to ensure high-quality audits.

**State Auditor**  
**Chief of Staff**  
**Chief Policy Advisor**  
**Director of Administration**  
**Director of State and Local Audits**  
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**Director of Special Investigations**  
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**Web Site**

**[www.sao.wa.gov](http://www.sao.wa.gov)**