



WELLS HYDROELECTRIC PROJECT
(A Department of Public Utility District No. 1
of Douglas County, Washington)

Financial Statements

August 31, 2015

(With Independent Auditors' Report Thereon)

WELLS HYDROELECTRIC PROJECT
(A Department of Public Utility District No. 1
of Douglas County, Washington)

August 31, 2015

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KPMG LLP
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

Independent Auditors' Report

The Board of Commissioners
Public Utility District No. 1 of Douglas County, Washington:

Report on the Financial Statements

We have audited the accompanying financial statements of Wells Hydroelectric Project (Wells Project or the Project), a department of Public Utility District No. 1 of Douglas County, Washington (the District), which comprise the statement of net position as of August 31, 2015, and the related statements of revenues, expenses, and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these 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 the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity'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 entity'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.

As discussed in Note 1, the financial statements of the Wells Project, a department of the District, are intended to present the net position, the changes in net position, and cash flows of only that portion of the business-type activities of the District that are attributable to the transactions of the Wells Project. They do not purport to, and do not, present fairly the net position of the District as of August 31, 2015, or the changes in its net position, or its cash flows for the year then ended in accordance with U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Wells Hydroelectric Project as of August 31, 2015, and the results of its operations and its cash flows for the year then ended, in accordance with U.S. generally accepted accounting principles.

Emphasis of Matter

As discussed in note 1 to the financial statements, on August 31, 2014, the Wells Project adopted new accounting guidance requiring governments providing defined benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, as well as recognizing most changes in the net pension liability within pension expense. Our opinion is not modified in respect to this matter.

Other Matter

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 6, and the schedules of required supplementary information on page 32, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us sufficient evidence to express an opinion or provide any assurance.

KPMG LLP

Seattle, Washington
January 20, 2016

WELLS HYDROELECTRIC PROJECT

(A Department of Public Utility District No. 1
of Douglas County, Washington)

Management's Discussion and Analysis (Unaudited)

August 31, 2015

The Management's Discussion and Analysis (MD&A) presents an overview and analysis of the financial activities of the Wells Hydroelectric Project (Wells Project or Project), a department of Public Utility District No. 1 of Douglas County, Washington (District) during the fiscal years ended August 31, 2015 and 2014. Please read it in conjunction with the accompanying audited financial statements and related notes thereto.

Overview of the Wells Hydroelectric Project and the Financial Statements

The Project is a hydroelectric generating facility located on the Columbia River in the State of Washington, owned and operated by the District. The Project is 516 river miles from the mouth of the Columbia River. It was placed in commercial operation in September 1967. The Project has earth embankments and a central integrated concrete structure that incorporates generating units, spillways, a switchyard, and fish passage facilities. It has 10 generating units with an installed nameplate rating of 815,000 kilovolt-amperes (KVA) and peaking capability of 840,000 kilowatts. The Project includes a 29.5-mile reservoir, land surrounding the reservoir, fish hatcheries, transformers, and transmission lines. Generation from the Project is sold at cost to four Pacific Northwest investor-owned utilities and the Colville Confederated Tribes pursuant to long-term power sales contracts, and to the District's Electric Distribution System. In November 2012, the Federal Energy Regulatory Commission issued the Project a new 40-year license to operate the Project.

The financial statements of the Project report information about the Project using accounting methods similar to those used by private utility companies. These statements offer financial information about the Project's activities. The Project's financial statements presented in this report consist of 1) the statements of net position, 2) statement of revenues, expenses, and changes in net position, 3) statements of cash flows, and 4) the notes to the financial statements.

The statements of net position include the assets, liabilities, and deferred outflows of the Project. They provide information about the nature and amounts of the Project's investments in resources (assets) and the obligations to the Project's creditors (liabilities) at August 31, 2015 and 2014.

The statements of revenues, expenses, and changes in net position report each fiscal year's revenues and expenses of the Project and reflect the increase or decrease in net position for each of the years presented.

The statements of cash flows report information about the Project's cash receipts and cash disbursements during each of the years ended August 31, 2015 and 2014, including changes in cash flows from operating, investing, and capital and related financing activities.

The notes to the financial statements provide additional information that is essential for a full understanding of the information provided in the financial statements described above.

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Management's Discussion and Analysis (Unaudited)

August 31, 2015

Condensed Comparative Financial Information (Amounts in Thousands)

Statements of Net Position

	August 31	
	2015	2014
Assets:		
Current	\$ 115,820	131,546
Net electric plant	242,084	230,236
Regulatory assets and deferred outflows	14,483	17,435
Total assets and deferred outflows	\$ 372,387	379,217
Liabilities:		
Current	\$ 34,534	37,234
Noncurrent	205,546	217,402
Deferred inflows	1,636	—
Total liabilities	241,716	254,636
Net position:		
Net investment in capital assets	116,173	104,119
Restricted for debt service	13,400	15,980
Unrestricted	1,098	4,482
Total net position	130,671	124,581
Total liabilities and net position	\$ 372,387	379,217

Statements of Revenues, Expenses, and Changes in Net Position

	August 31	
	2015	2014
Operating revenues	\$ 53,383	49,353
Operating expenses	31,463	29,093
Operating income	21,920	20,260
Nonoperating expenses	(7,311)	(11,810)
Change in net position	14,609	8,450
Net position, beginning of year, as previously reported	124,581	116,131
Effect of accounting change in pensions	(8,519)	—
Net position, beginning of year, as restated	116,062	116,131
Net position, end of year	\$ 130,671	124,581

WELLS HYDROELECTRIC PROJECT
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Management's Discussion and Analysis (Unaudited)

August 31, 2015

Financial Analysis

Assets

Current assets decreased 12% from 2014 to 2015. The decrease in current assets is primarily from the spending of bond funds on construction projects. Net utility plant increased by \$11.8 million from 2014 to 2015 primarily from construction projects and depreciation taken on plant in service. Regulatory assets and deferred outflows decreased 17% from 2014 to 2015. The Project's regulatory asset balance decreased due to amortization. Regulatory assets include: certain repairs made to turbines and the earthen embankment at the Project, costs related to legal settlements, and recreational property improvements.

Liabilities

Current liabilities decreased 7% from 2014 to 2015 because of normal fluctuation in accounts payable and excess cash that is annually refunded to the Project's power purchasers. The decrease in noncurrent liabilities of 5% from 2014 to 2015 was due to normal maturities of long-term debt and a bond refunding transaction, which retired a portion of the Hydro's September 2015 maturities in June.

Net Position

The Project's net position increased 5% from 2014 to 2015. The increases are from continued investment in Project capital assets and normal fluctuations to debt service funds that are restricted for debt repayment. In addition, due to new reporting standards relating to pensions, beginning net position was adjusted. See note 1 (a) and (i).

Statement of Revenues, Expenses, and Changes in Net Position

Project revenue increased 8% from 2014 to 2015. Electricity generated by the Project is sold at cost under power sales contracts. The cost of power includes debt service, but excludes depreciation. Operating revenues fluctuate based on operating expenses (exclusive of depreciation) and debt service requirements.

Operating expenses increased 8% from 2014 to 2015 primarily due to pension expense recorded in accordance with new reporting standards relating to pensions. Maintenance also increased due to seismic monitoring costs and equipment upgrades and replacements in the Project's infrastructure.

Investment income increased 17% from 2014 to 2015. This increase is mainly due to shifting of the Project's investment portfolio to include more municipal bonds and other instruments, which have a better rate of return.

Interest expense decreased 4% from 2014 to 2015. The Project's debt is structured to provide level debt service, so this is an expected outcome. The Project realized lower interest expense due to the call and refunding of our 2005 bonds at current lower rates.

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Management's Discussion and Analysis (Unaudited)

August 31, 2015

Capital Asset and Long-Term Debt Activity

As of August 31, 2015, the Project had \$242 million invested in capital assets, net of accumulated depreciation. The Project's capital assets consist of a hydroelectric generation plant, transmission facilities, fish rearing facilities, land, office buildings, and equipment. Major additions or replacements are funded from bond proceeds. The District is currently refurbishing generators and turbines at the Project.

All ten of the generators and turbines at the Project are in the process of being refurbished. The refurbishment will continue for the next several years and is expected to cost over \$200 million. Progress of the project is behind schedule. However, the first unit is nearing completion and the District is in the process of placing it into service (see note 5(e) for more information). Cost of the refurbishment is being financed through the issuance of revenue bonds. In 2010, bonds were issued for this project in the par amount of \$112.9 million, of which \$12.9 million was used to refinance outstanding bonds for debt service savings. It is anticipated that the remaining 2010 bond proceeds will not be sufficient to complete the generator and turbine refurbishment and that future borrowings will be required.

The District is in process of modernizing the fish hatchery at the Project. The hatchery modernization will cost the Project about \$30 million over the next two years.

In December 2004, the District Commission authorized a revolving note (Note), from the District's Electric Distribution System to the Project. The purpose of the Note was to finance the cost of relicensing the Project. Amounts borrowed by the Project under the Note were to be due upon the expiration of the current Federal Energy Regulatory Commission (FERC) license and any subsequent annual FERC licenses issued to the District. Accordingly, amounts borrowed under the Note were included in short-term liabilities. When the new 40-year license was approved in November 2012, the District exercised an option to extend the terms of the Note, which will be repaid over the licensing term and is now classified as a long-term liability (excluding current portion). As of August 31, 2015, the total amount outstanding was \$9.5 million.

In 2015, Moody's affirmed its "Aa3" rating of the Project, and changed its outlook to stable from negative due to the expectation the Project will maintain at least 250 days cash on hand, achieve consolidated debt service coverage of 1.15x through 2017, and improve financial performance starting in 2018 under new long-term contracts. During 2015, Standard & Poor's also affirmed its "AA" rating of the Project together with a stable outlook.

Contact Information

This financial report is designed to provide a general overview of the finances of the Project. If you have questions about this report or need additional financial information, please contact the Treasurer of Public Utility District No. 1 of Douglas County, 1151 Valley Mall Parkway, East Wenatchee, Washington 98802.

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Statement of Net Position

August 31, 2015

Assets

Current assets:

Restricted:

Construction funds – cash	\$ 66,520,528
Construction funds – investments	8,487,991
Debt repayment funds – cash	19,867,300
Debt repayment funds – investments	4,308,496
Reserve and contingency fund – cash	<u>3,736,611</u>
Total restricted	<u>102,920,926</u>

Unrestricted:

Cash	868,632
Investments	4,842,078
Accounts receivable	6,705,556
Other assets	<u>483,197</u>
Total unrestricted	<u>12,899,463</u>

Total current assets	<u>115,820,389</u>
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Noncurrent assets:

Electric plant:

Electric plant in service	309,355,136
Construction work in progress	<u>41,135,257</u>
Gross electric plant	350,490,393
Less accumulated depreciation and amortization	<u>108,406,104</u>
Net electric plant	242,084,289

Regulatory assets	<u>12,874,611</u>
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Total noncurrent assets	254,958,900
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Deferred outflows:

Loss on reacquired debt	1,040,623
Pension related outflows	<u>567,612</u>

Total assets and deferred outflows	<u>\$ 372,387,524</u>
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Statement of Net Position

August 31, 2015

Liabilities and Net Position

Current liabilities:	
Accounts payable	\$ 14,756,754
Other accrued liabilities	1,484,949
Excess revenue fund	1,402,610
Payable from restricted assets:	
Accrued interest payable	3,490,073
Current portion long-term debt	<u>13,400,000</u>
Total current liabilities	<u>34,534,386</u>
Noncurrent liabilities:	
Bonds payable, excluding current portion	183,874,581
Unamortized bond premiums and discounts	<u>4,554,487</u>
Bonds payable, net	188,429,068
Intradistrict note payable	9,475,000
Compensated absences	710,012
Net Pension Liability	<u>6,931,602</u>
Total noncurrent liabilities	<u>205,545,682</u>
Total liabilities	<u>240,080,068</u>
Deferred inflows:	
Gain on required debt	443,470
Pension related inflows	1,192,790
Net position:	
Net investment in capital assets	116,172,812
Restricted for debt service	13,400,000
Unrestricted	<u>1,098,384</u>
Total net position	<u>130,671,196</u>
Total liabilities and net position	<u>\$ 372,387,524</u>

See accompanying notes to financial statements.

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Statement of Revenues, Expenses, and Changes in Net Position
Year ended August 31, 2015

Operating revenues	\$	53,382,862
Operating expenses:		
Operations		18,908,912
Maintenance		5,891,809
Depreciation		5,251,200
Taxes		1,410,720
Total operating expenses		31,462,641
Operating income		21,920,221
Nonoperating revenues (expenses):		
Interest income		177,376
Interest expense		(9,177,669)
Amortization of other charges, debt discounts, premiums, and costs		(3,125,651)
Other		4,815,316
Total nonoperating expenses		(7,310,628)
Change in net position		14,609,593
Net position, beginning of year, as restated		116,061,603
Net position, end of year	\$	130,671,196

See accompanying notes to financial statements.

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Statement of Cash Flows

Year ended August 31, 2015

Cash flow from operating activities:	
Receipts from customers	\$ 50,553,603
Payments to suppliers and employees	<u>(29,148,953)</u>
Net cash provided by operating activities	<u>21,404,650</u>
Cash flows from investing activities:	
Purchase of investments	(21,142,916)
Proceeds from sales and maturities of investments	14,649,014
Interest on investments	<u>301,208</u>
Net cash used in investing activities	<u>(6,192,694)</u>
Cash flows from capital and related financing activities:	
Additions to electric plant in service	(15,856,008)
Proceeds from capital contributions	4,100,000
Net proceeds from issuance of long-term debt	64,103,358
Principal payments on long-term debt-defeasance 2005 bonds	(67,075,000)
Principal payments on long-term debt-scheduled maturities	(16,095,000)
Interest payments on long-term debt	(10,689,874)
Build America bonds interest rebates	<u>696,651</u>
Net cash used in capital and related financing activities	<u>(40,815,873)</u>
Net decrease in cash and cash equivalents	(25,603,917)
Cash and cash equivalents, beginning of year	<u>116,596,988</u>
Cash and cash equivalents, end of year	<u><u>\$ 90,993,071</u></u>
Reconciliation of net operating income to net cash provided by operating activities:	
Operating income	\$ 21,920,221
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	5,251,200
Cash provided by changes in operating assets and liabilities:	
Receivables	(2,369,809)
Other assets	(83,880)
Excess revenue fund	(2,829,259)
Accounts payable – excluding construction payables	(347,583)
Other current liabilities	(118,915)
Compensated absences	<u>(17,325)</u>
Net cash provided by operating activities	<u><u>\$ 21,404,650</u></u>

See accompanying notes to financial statements.

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Notes to Financial Statements

August 31, 2015

(1) Organization and Summary of Significant Accounting Policies

Public Utility District No. 1 of Douglas County, Washington (District) is a municipal corporation of the State of Washington established in 1936. The District is administered by a three person Board of Commissioners, elected by the voters of Douglas County. The District is organized in two primary operating systems: the Electric Distribution System and the Wells Hydroelectric Project (Wells Project or Project). The Wells Hydroelectric Project generates electricity from a hydroelectric dam located on the Columbia River. The Wells Project represents only one department of the District and the Project's financial statements do not purport to, and do not, present fairly the financial position, the changes in financial position or the cash flows of the District for any period presented.

(a) Accounting Policies

The accounting policies of the Project are prepared using the economic resources measurement focus and conform to accounting principles generally accepted in the United States of America (GAAP) applicable to municipal utilities. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. Accounting records are maintained in accordance with the Uniform System of Accounts of the Federal Power Act, prescribed by the Federal Energy Regulatory Commission (FERC).

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions*. On September 1, 2014, the Project adopted GASB 68. This statement requires governments providing defined benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, which is measured as the total pension liability less the amount of the pension plan's fiduciary net position. The total pension liability is determined by discounting projected benefit payments based on the benefit terms and legal agreements existing at the pension plan's fiscal year end. Projected benefit payments are required to be discounted using a single rate that reflects the expected rate of return on investments, to the extent that plan assets are available to pay benefits. When plan assets are insufficient to pay benefits, the discount rate used is a blended rate comprised of the expected rate of return over the period when projected plan assets are not available. This statement requires that most changes in the net pension liability be included based on cash contributions paid to the pension plan administrator. In addition to the reporting changes described above, implementation of this statement resulted in a restatement of fiscal year 2015 beginning unrestricted net position, reducing it by \$8,519,275.

In November 2014, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, an amendment of GASB Statement No. 68. The purpose of this statement is to address an issue regarding application of the transition provisions of GASB Statement No. 68. The statement relates to amounts associated with contributions, if any, made by a state or local government employer, or nonemployer contributing entity, to a defined benefit pension plan after the measurement date of the government's beginning net pension liability. Currently, the District participates in a multiple-employer plan (Washington State Public Employees Retirement System).

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(b) Revenue Recognition

Wells Project revenues are derived through the sale of power to four major Pacific Northwest electric utilities and the Colville Confederated Tribes, under the terms of long-term power sales contracts, and to the District's Electric Distribution System. The contracts stipulate that the power purchasers will pay annual power costs, which are defined as "all costs and expenses in connection with the Wells Project (excluding depreciation and items properly chargeable to cost of acquisition and construction), whether or not the Wells Project is operable or the operation thereof is interrupted, suspended, or interfered with, in whole or in part, during the term of this contract or any portion of said term." Revenues related to the Project's principal operations are considered to be operating revenues. Revenues related to financing and investing activities, and any other revenues not related to the Project's principal operations, are considered to be nonoperating revenues.

(c) Utility Plant and Depreciation

Wells Project plant, including land and all related facilities, is recorded at cost. Cost comprises the following: (a) all direct construction and acquisition costs; (b) all indirect costs up to the commencement of initial power generated on September 7, 1967, and only those indirect costs related to the construction and acquisition since that date; and (c) interest costs capitalized up to certain dates, which were subsequent to the date generating units were placed in service. Under FERC accounting, interest costs would cease to be capitalized after units are placed in service. Management of the District elected to capitalize interest costs through January 1, 1969, as to the 1963 series bonds, and to September 1, 1972, as to the 1965 series bonds, because this was the accounting treatment specifically prescribed in the bond resolutions and power sales contracts. Depreciation of substantially all depreciable assets are provided over estimated useful lives ranging from 15 to 95 years, using the sinking fund method (6% rate). The sinking fund method was selected at the inception of the Wells Project and continues to be applied because its use corresponds more closely to revenue determined from debt service than would an alternative cost allocation method.

(d) Cash and Cash Equivalents

For purposes of the statements of cash flows, the Project considers all short-term investments with a remaining maturity of three months or less when purchased to be cash equivalents.

(e) Cash and Investment Funds

The Wells Project Revenue Fund represents working capital in the Project. The amount of working capital maintained is determined by the power sales contracts. Excess Revenue Funds are returned to Project participants. Shortfalls in working capital are recovered from Project participants. Reserve & Contingency Funds are used for contingencies, renewals, and replacements of Project assets. The account is funded by transfers from the Revenue Fund. Reserve & Contingency Funds in excess of \$5 million dollars are returned to project participants. Construction Funds are bond proceeds that are being used for capital improvement projects.

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(f) *Compensated Absences*

Employees accrue personal leave to be used for vacation, sick, and family leave purposes. Personal leave granted each employee varies in accordance with years of service and may be carried forward from year-to-year, capped at a maximum bank of 1,200 hours for employees hired before April 1, 2011 and 700 hours for employees hired on or after April 1, 2011. The Project records personal leave as an expense and liability when earned.

(g) *Accounting Estimates*

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount 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 those estimates.

(h) *Insurance*

The Project holds insurance policies for general liability, employee benefits liability, directors' and officers' liability, excess liability, and property insurance. Among other things, the property insurance policies cover flood, earth movement, terrorism, and mobile equipment. Other types of insurance carried by the Project include business automobile liability and physical damage, aircraft nonownership liability, comprehensive crime coverage, and information security and privacy liability coverage.

For purposes of certain employee benefits insurance the Project is a member of the Central Washington Public Utilities Unified Insurance Program Trust (Trust). The Trust was organized pursuant to the provisions of RCW Title 54 and inter-local governmental agreements. Its general objectives include provision for the central collection and disbursement of employee benefit premiums and claims involving medical, dental, life, and long-term disability coverage. The Trust is administered by a Board of Trustees comprised of an appointed Trustee from each of the seven member public utility districts. The Trustees are authorized to negotiate, obtain, and maintain insurance policies, and authorize disbursements made from the Trust to third-party administrators or other entities. Effective August 1, 2002 and January 1, 2009, the Trust established a self-insured medical plan and self-insured dental plan, respectively, approved by the Washington State Office of Risk Management. The audit report for the Trust is available from the Washington State Auditor's Office. Claims settlements have not exceeded insurance coverage during any of the past three years. The Trust utilizes stop loss coverage that protects the plan from high exposure. The thresholds for this coverage are \$250,000/individual in excess of deductible and \$1,000,000 after exceeding the aggregate to the entire Trust.

(i) *Pensions*

For purposes of measuring the net pension liability, deferred outflows of resources, and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the PERS pension plans, and additions to/deductions from those plans' fiduciary net position have been determined on the same basis as they are reported by the Washington State Department of Retirement Systems. For this purpose, benefit payments (including refunds of employee

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contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

(2) Deposits and Investments

The Project's deposits are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington State Public Deposit Protection Commission. Cash held in the Local Government Investment Pool (LGIP) is managed by the Washington State Treasurer's Office. The LGIP is a 2a7-like pool and represents an interest in a group of securities with no specific securities subject to custodial risk.

The Project's investments consist of direct obligations of the U.S. Government, government sponsored enterprises (agencies), and bonds with the state of Washington or local governments in the state of Washington, which are all eligible investments for public funds in the state of Washington (RCW 43.84.080). To minimize custodial risk, the District's investments are held in a third-party safekeeping account which uses delivery vs. payment protocol. The Project's practice is to, generally, hold investments to maturity. The Project's investments are recorded at cost, including premiums and discounts and carrying values are adjusted (amortized) each period and approximate market value. The Project had the following investments as of August 31, 2015:

Agencies	\$	10,558,496
Municipal bonds		7,080,069
		17,638,565
Total	\$	17,638,565

(3) Utility Plant

As stated in note 1, utility plant is recorded at cost. Cost includes both direct costs of construction or acquisition and indirect costs. The Project's capitalization threshold is \$5,000 and an expected useful life of three years or more. The cost of maintenance and repairs is charged to expense as incurred, while the cost of additions, replacements, and improvements is capitalized. Major assets are held in the construction work in progress account until the asset is ready for service. When the asset is ready for service, costs are transferred out of construction work in progress to the appropriate plant account. Increases in plant balances are from placing assets in service. Construction work in progress may contain amounts that will be transferred to a deferred charge account. The book cost of operating property retired or otherwise disposed of, less salvage,

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is charged to accumulated depreciation. Decreases in plant balances are the result of normal retirement, sale and salvage of obsolete plant. The following changes occurred in the Project's utility plant:

Electric Plant Assets Wells Hydroelectric Project	Balance August 31, 2014	Increase	Decrease	Balance August 31, 2015
Utility plant not being depreciated:				
Land and land rights	\$ 51,391,133	786,769	—	52,177,902
Construction work in progress	65,145,434	17,332,514	(41,342,691)	41,135,257
Subtotal	<u>116,536,567</u>	<u>18,119,283</u>	<u>(41,342,691)</u>	<u>93,313,159</u>
Utility plant being depreciated:				
Hydraulic generation	178,569,535	38,033,828	—	216,603,363
Transmission	16,883,081	2,069,921	—	18,953,002
General	21,433,683	327,528	(140,342)	21,620,869
Subtotal	216,886,299	40,431,277	(140,342)	257,177,234
Accumulated depreciation	<u>(103,187,107)</u>	<u>(5,359,339)</u>	<u>140,342</u>	<u>(108,406,104)</u>
Net plant being depreciated	<u>113,699,192</u>	<u>35,071,938</u>	<u>—</u>	<u>148,771,130</u>
Net utility plant – Wells Project	<u>\$ 230,235,759</u>	<u>53,191,221</u>	<u>(41,342,691)</u>	<u>242,084,289</u>

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(4) Long-Term Debt

Wells Hydroelectric Project

	Hydroelectric Project				Balance August 31, 2015	Due within one year
	Purpose	Balance August 31, 2014	Additions	Reductions		
Revenue Bonds:						
Series of 2005A, serial bonds maturing annually to September 1, 2025 and term bonds maturing September 1, 2030 and 2035, interest at 3.70%–5.00%	Capital improvements	\$ 36,635,000	—	36,635,000	—	—
Series of 2005B, serial bonds maturing annually to September 1, 2026 and term bonds maturing September 1, 2022, 2030 and 2035, interest at 3.60%–5.25%	Refunding, capital improvements, and Colville settlement	29,090,000	—	29,090,000	—	—
Series of 2005C, serial bonds maturing annually to September 1, 2014 and term bonds maturing September 1, 2018, interest at 4.654%–5.112%	Colville settlement	4,125,000	—	4,125,000	—	—
Series of 2006A, serial bonds maturing annually to September 1, 2016 and term bonds maturing September 1, 2018, interest at 4.50%–5.00%	Refunding	5,395,000	—	975,000	4,420,000	1,025,000
Series of 2010A, serial bonds maturing annually to September 1, 2022 and term bonds maturing September 1, 2030 and 2040, interest at 1.484%–5.450%	Capital improvements	50,940,000	—	1,005,000	49,935,000	1,030,000
Series of 2010B, serial bonds maturing annually to September 1, 2020 and term bonds maturing September 1, 2030 and 2040, interest at 1.484%–5.495%	Capital improvements	43,030,000	—	1,065,000	41,965,000	1,080,000
Series of 2010C, serial bonds maturing annually to September 1, 2029, interest at 3.00%–5.00%	Refunding	10,360,000	—	905,000	9,455,000	955,000
Series of 2012, serial bonds maturing annually to September 1, 2018, interest at 0.40%–1.75%	Refunding	42,280,000	—	9,145,000	33,135,000	9,195,000

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		Hydroelectric Project				
Purpose	Balance August 31, 2014	Additions	Reductions	Balance August 31, 2015	Due within one year	
Series of 2015A, serial bonds maturing annually to September 1, 2025 and term bonds maturing September 1, 2030 and 2035, interest at 3.70%–5.00%	\$ —	31,675,000	—	31,675,000	—	
Series of 2015B, serial bonds maturing annually to September 1, 2026 and term bonds maturing September 1, 2022, 2030 and 2035, interest at 3.60%–5.25%	—	24,155,000	—	24,155,000	—	
Series of 2015C, serial bonds maturing annually to September 1, 2016 and term bonds maturing September 1, 2018, interest at 4.654%–5.112%	—	2,419,581	—	2,419,581	—	
Revenue bonds payable	<u>\$ 221,855,000</u>	<u>58,249,581</u>	<u>82,945,000</u>	<u>197,159,581</u>	<u>13,285,000</u>	

The changes in long-term debt, including the portion maturing currently, for the year ended August 31, 2015 are as follows:

Long-term debt as of August 31, 2014	\$ 221,855,000
Principal payments	(15,870,000)
Issuance of bonds	58,249,581
Defeasance of debt	<u>(67,075,000)</u>
Long-term debt as of August 31, 2015	<u>\$ 197,159,581</u>

In 2004, the board authorized an intersystem loan, in the form of a revolving note (Note) for the purpose of funding the cost of relicensing the Wells Project. Under the terms of the Note, the Project was allowed to take semiannual draws from the Electric Distribution System's Wells Relicensing Fund. The interest rate for each draw was established at the time of the draw and was equal to the yield on U.S. Treasury bonds maturing in May 2018, plus 100 basis points. Amounts borrowed under the Note were to be due upon the expiration of the current Wells Project license and any subsequent annual FERC licenses issued to the District. On May 31, 2012, the original Wells Project license expired and FERC issued an annual license that allowed the District to continue operating the Wells Project until a new long-term license could be issued. Under the terms of the Note the District had the option, by election prior to maturity, to extend the maturity date such that principal would be amortized over the life of the new FERC license, with interest payable semiannually. In May 2012, the District Commission, in anticipation of receiving a new long-term license, chose to utilize

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this option. On November 9, 2012, FERC issued to the District a new 40-year license to operate and maintain the Wells Project. Repayment of the Note was amortized over the new license period at an interest rate equal to the 30-year US Treasury bond yield at November 1, 2012, the effective date of the new license, plus 100 basis points. The note was reclassified to a long-term liability in 2014.

Following is a summary of future debt service requirements for Wells Project revenue bonds outstanding at August 31, 2015:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2016	\$ 13,285,000	7,295,082	20,580,082
2017	16,562,988	7,825,074	24,388,062
2018	16,875,857	7,458,298	24,334,155
2019	13,080,736	7,051,629	20,132,365
2020	4,970,000	6,754,833	11,724,833
2021–25	27,415,000	30,288,797	57,703,797
2026–30	33,700,000	23,149,078	56,849,078
2031–35	36,405,000	14,398,928	50,803,928
2036–40	29,070,000	5,268,432	34,338,432
2041–45	5,795,000	158,452	5,953,452
	<u>\$ 197,159,581</u>	<u>109,648,603</u>	<u>306,808,184</u>

Interest on all bonds for the Wells Hydroelectric Project is payable on March 1 and September 1. All bond covenants were complied with for fiscal year 2015.

Following is a summary of the debt service requirements for the intra-district note payable at August 31, 2015.

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2016	\$ 115,000	367,001	482,001
2017	120,000	362,478	482,478
2018	125,000	357,761	482,761
2019	130,000	352,853	482,853
2020	135,000	347,751	482,751
2021–25	750,000	1,655,500	2,405,500
2026–30	910,000	1,496,303	2,406,303
2031–35	1,100,000	1,303,418	2,403,418
2036–40	1,325,000	1,070,781	2,395,781
2041–45	1,600,000	790,020	2,390,020
2046–50	1,930,000	451,028	2,381,028
2051–54	1,350,000	79,503	1,429,503
	<u>\$ 9,590,000</u>	<u>8,634,397</u>	<u>18,224,397</u>

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Advance Debt Refunding

In July 2005, the Wells Project issued its Wells Hydroelectric Revenue and Refunding Bonds, Series 2005A, 2005B, and 2005C (the 2005 Bonds), in the total par amount of \$87,585,000. The issuance of the 2005 Bonds resulted in a premium of \$2,027,482. A portion of the 2005 Bonds refinanced and legally defeased \$5,160,000 of the outstanding 1999B Bonds. This refinancing resulted in a reduction of \$1,058,000 in total Wells Project debt service over the succeeding 24 years and an economic gain (difference between the present values of the old and new debt service requirements) of \$358,000.

In August 2006, the Wells Project issued its Wells Hydroelectric Revenue Refunding Bonds, Series 2006A and 2006B (the 2006 Bonds), in the total par amount of \$13,280,000. The issuance of the 2006 Bonds resulted in a premium of \$251,744. The 2006 Bonds refinanced and legally defeased \$14,080,000 of the 1986A Bonds, which was the remaining outstanding balance of 1986A Bonds. This refinancing resulted in a reduction of \$4,774,000 in total Wells Project debt service over the succeeding 12 years and an economic gain (difference between the present values of the old and new debt service requirements) of \$2,214,000.

In August 2010, the Wells Project issued its Wells Hydroelectric Bonds, Revenue Series 2010A, Revenue Series 2010B, and Revenue Refunding Series 2010C (the 2010 Bonds), in the total par amount of \$112,900,000. The issuance of the 2010 Bonds resulted in a net discount of \$410,845. A portion of the 2010 Bonds refinanced and/or legally defeased \$8,520,000 of the outstanding 1999A Bonds and \$5,740,000 of the outstanding 2000A Bonds. This refinancing resulted in a reduction of \$3,400,000 in total Wells Project debt service over the succeeding 19 years and an economic gain (difference between the present values of the old and new debt service requirements) of \$2,259,000.

In August 2012, the Wells Project issued its Wells Hydroelectric Revenue and Refunding Bonds, Series 2012 (Taxable) (the 2012 Bonds), in the total par amount of \$43,360,000. The 2012 Bonds were issued at par. A portion of the 2012 Bonds refinanced and legally defeased \$6,560,000 of the outstanding 2003A Bonds, \$1,790,000 of the outstanding 2003B Bonds, and \$31,905,000 of the outstanding 2003C Bonds. This refinancing resulted in a reduction of \$2,998,000 in total Wells Project debt service over the succeeding seven years and an economic gain (difference between the present values of the old and new debt service requirements) of \$3,176,000.

In June 2015, the Wells Project issued its Wells Hydroelectric Revenue and Refunding Bonds, Series 2015A, 2015B, and 2015C (the 2015 Bonds), in the total combined par amount of \$58,249,581. The 2015 Bonds were issued at par. A portion of the 2015 Bonds refinanced and legally defeased \$67,075,000 of the outstanding 2005 Series Bonds. This refinancing resulted in a reduction of \$1,058,000 in total Wells Project debt service over the succeeding 24 years and an economic gain (difference between the present values of the old and new debt service requirements) of \$358,000.

Debt service on all outstanding Wells Project bonds, which have been refinanced and legally defeased is met by cash and investments held in irrevocable trust with escrow agents. As of August 31, 2015, the escrow agent was holding cash and investments of \$27,842,163, which are expected to fully fund debt service on all outstanding Wells Project legally defeased bonds. The trust account assets and the liability for the corresponding refunded bonds are not included in the Project's financial statements.

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(5) Other Commitments and Contingencies

(a) *Colville Confederated Tribes Settlement*

In January 2003, the Colville Confederated Tribes (Tribes) presented an economic consultant's study indicating the District owed the Tribes approximately \$950,000,000 for past annual charges and approximately \$18,000,000 annually for use of freeboard lands previously considered tribal lands and one-half of the bed of the Okanogan and Columbia Rivers bordering the Colville Reservation. The District had been aware of a claim made by the Tribes for the use of the bed of the river for years, but there had never been a claim to shore land that the District owns. The bed of the river claim had surfaced on several occasions during the previous 25 years, but the Tribes chose not to pursue it seriously until January 2003. The Tribes' claim in 2003 included annual charges, past and future, for all of the lands that the District previously acquired in fee title from allottees, individuals of the Tribes, and the Bureau of Indian Affairs, as well as for one-half of the bed of the Okanogan and Columbia Rivers abutting the Colville Reservation. The District has recorded fee title deeds to all of the shore land below Project Boundary abutting the Colville Reservation.

In 2004, the District and the Tribes entered into a settlement of this claim which provided for a \$13,500,000 cash payment and the transfer of land with a book value of \$958,140 to the Tribes. Additionally the District agreed to sell to the Tribes 4.5% of the output of the Wells Project through August 31, 2018, and 5.5% thereafter, at Wells Project cost, for so long as the District holds a license for the Wells Project. In return, the Tribes granted and affirmed all land rights previously conveyed by the Tribes to the District; granted to the District overflow rights to the bed of the Okanogan and Columbia Rivers; covenanted not to compete for a license for the Wells Project and to support the District's relicensing application; and granted the District certain water rights in connection with the Wells Project.

The cash portion of the settlement was paid in July 2005, financed with Wells Project Revenue Bonds, and is reported as a deferred charge on the balance sheet, to be amortized over the corresponding revenue bond debt service period. The amortized balance of the settlement charges as of August 31, 2015 was \$2,892,854. The land portion of the settlement was transferred in March 2005.

The Wells Project's four investor-owned Power Purchasers approved the settlement, as evidenced by an Endorsement Agreement between the Power Purchasers and the District dated November 1, 2004. The District, the Tribes, and the Power Purchasers filed a joint application with the Federal Energy Regulatory Commission (FERC) seeking approval of the Colville Settlement Agreement and the Colville Power Sales Contract. FERC formally approved the contracts on February 11, 2005.

(b) *Endangered Species*

Several species of fish in the vicinity of the Wells Project are listed as threatened or endangered under the Endangered Species Act (ESA). Upper Columbia River (UCR) Steelhead and UCR spring Chinook were listed as endangered species on August 18, 1997 and March 24, 1999, respectively. Subsequently, the endangered status of UCR spring Chinook was reaffirmed and the status of UCR steelhead was upgraded to threatened.

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The District has negotiated with state and federal fisheries resource agencies and Indian tribes, a multispecies Anadromous Fish Agreement and Habitat Conservation Plan (HCP). The plan species are spring Chinook, summer/fall Chinook, steelhead, sockeye, and coho salmon. The purpose of the HCP is to have legally enforceable measures in place to either avoid a listing under the ESA or, in the event of a listing, allow continued operation of the Wells Project under an incidental take permit. The HCP satisfies all FERC relicensing and ESA requirements for the plan species. FERC approved the HCP in June of 2004 and amended the Wells Project license accordingly. At the District's request, FERC also issued an Order on Rehearing in November 2004, clarifying several technical items.

Bull trout were listed as a threatened species on June 10, 1998. On September 30, 2010, the United States Fish and Wildlife Service (FWS) designated critical habitat for ESA listed Columbia River bull trout. This designation included most of the waters found within the Wells Project. ESA listed bull trout have been observed at the Wells Project but are not covered in the HCP. In May 2004, FWS issued a biological opinion and incidental take permit that covered the operations of the Wells Project and the implementation of the HCP.

There is extensive litigation in the federal court system under the ESA, challenging actions taken by the responsible federal agencies in regard to anadromous fish. Future legal actions to protect fish may have a significant impact on the amount and/or cost of power generated at the Wells Project. As the ultimate outcome of this matter is not determinable, no accruals have been made to the financial statements.

(c) *Plan Species Account*

In accordance with the Tributary Conservation Plan, formed under the HCP, a plan species account was established to fund projects for the protection and restoration of plan species habitat. The HCP requires a Tributary Committee, composed of one representative of each party to the HCP, to select the projects and approve the project budgets from the plan species account for purposes of implementing the Tributary Conservation Plan. All budget and spending decisions must be made by unanimous vote of the Tributary Committee members. The HCP requires the District to make monetary contributions to the plan species account. In 2015, the Project made payments of \$258,476 to the plan species account. Funds paid into the plan species account are no longer under the substantive control of the District; therefore, those funds are not included in the Project's statement of net position.

(d) *Relicensing*

On November 9, 2012, FERC issued to the District a new long-term license for the Wells Project. The new license was issued for a period of 40 years, effective November 1, 2012.

(e) *Generator and Turbine Refurbishment*

A generator and turbine refurbishment is in progress at the Project and will continue for several years until all 10 units are refurbished. Cost of the refurbishment is being financed through the issuance of revenue bonds. Completion of the first unit refurbishment (Unit 7) is complete and the refurbishing

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for the second unit is underway. As of August 31, 2015, liquidated damages for the first unit amount to \$3.5 million, which have been withheld from payments to the contractor.

(f) Chief Joseph Dam Encroachment

The Project’s pool encroaches on the Chief Joseph Dam tailrace. Chief Joseph Dam is a federal hydroelectric project operated by the United States Army Corps of Engineers (COE). In conjunction with the Project’s relicensing process, encroachment compensation for the new FERC license period must be resolved. Currently a 1968 settlement agreement resolves the issue of tailwater encroachment on Chief Joseph Dam. Under the 1968 agreement, the Project delivers replacement power to the Federal Transmission System at no cost to the United States as compensation for power loss due to the Project’s encroachment. The District, COE, and the Bonneville Power Administration are discussing a settlement as to future compensation to be paid by the Project. FERC has a long-standing policy of directing the parties to attempt to negotiate an agreement within a specific time, but reserving authority to determine compensation in the event the parties are unable to reach an agreement. The ultimate outcome of this matter is not determinable. No accruals have been made to the financial statements.

(6) Pension Plans, Deferred Compensation Plans

The following table represents the aggregate pension amounts for all plans subject to the requirements of GASB 68 for the year 2015:

<u>Aggregate Pension Amounts – PERS Plans 1/2/3</u>	
Net pension liabilities*	\$ 7,963,312
Pension assets	—
Deferred outflows of resources	567,612
Deferred inflows of resources	1,192,790
Pension expense	938,372

* Current portion of net pension liability of \$1,031,710 included in accounts payable in the accompanying statement of net position

Substantially, all Project full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer public employee defined benefit and defined contribution retirement plans. The 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 Web site at www.drs.wa.gov. The following disclosures are made pursuant to GASB Statement No. 68.

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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 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 exercise 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 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. Notwithstanding, PERS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill, with less than five years to live.

PERS comprises 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 defined-benefit Plan 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 defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PERS retirement benefit provisions are established in Chapters 41.34 and 41.40 RCW and may be amended only by the State Legislature.

PERS Plan 1 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement 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 monthly benefit is 2% of the average final compensation (AFC) per year of service. (AFC is the monthly average of the 24 consecutive highest-paid service credit months.) The retirement benefit may not exceed 60% of AFC. The monthly benefit is subject to a minimum for PERS Plan 1 retirees who have 25 years of service and have been retired 20 years, or who have 20 years of service and have been retired 25 years. Plan 1 members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. If a survivor option is chosen, the benefit is further reduced. Plan 1

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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% annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 1 provides duty and nonduty disability benefits. Duty disability retirement benefits for disablement prior to the age of 60 consist of a temporary life annuity payable to the age of 60. The allowance 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. A member with five years of covered employment is eligible for nonduty disability retirement. Prior to the age of 55, the allowance amount is 2% of the AFC for each year of service reduced by 2% for each year that the member's age is less than 55. The total benefit is limited to 60% of the AFC and is actuarially reduced to reflect the choice of a survivor option. A cost-of-living allowance is granted at age 66 based upon years of service times the COLA amount. This benefit was eliminated by the Legislature, effective July 1, 2011. 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% annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 1 members can receive credit for military service. Members can also purchase up to 24 months of service credit lost because of an on-the-job injury.

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% of the AFC per year of service. (AFC is the monthly average of the 60 consecutive highest-paid service months.)

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:

- With a benefit that is reduced by 3% for each year before age 65
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules

PERS Plan 2 retirement benefits are also actuarially reduced to reflect the choice, if made, 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% annually.

The surviving spouse or eligible child or children of a PERS Plan 2 member who dies after leaving eligible employment having earned 10 years of service credit may request a refund of the member's accumulated contributions.

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PERS 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 monthly benefit that is 1% of the AFC per year of service. (AFC is the monthly average of the 60 consecutive highest-paid service months.)

Effective June 7, 2006, PERS Plan 3 members are vested in the defined benefit portion of their Plan after 10 years of service; or after five years of service, if 12 months of that service are earned after age 44; or after five service credit years earned in PERS Plan 2 prior to 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 10 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, they have the choice of a benefit that is reduced by 3% 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.

PERS Plan 3 defined benefit retirement benefits are also actuarially reduced to reflect the choice, if made, 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.

PERS Plan 3 defined contribution retirement benefits are solely dependent upon contributions and the results of investment activities.

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 Director of the Department of Retirement Systems.

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% of the AFC per year of service. For Plan 3, the monthly benefit amount is 1% 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% annually.

PERS Plan 2 and Plan 3 members may have up to 10 years of interruptive military service credit; five years at no cost and five years that may be purchased by paying the required contributions. Effective July 24, 2005, a member who becomes totally incapacitated for continued employment while serving the uniformed services, or a surviving spouse or eligible children, may apply for interruptive military service credit. Additionally, PERS Plan 2 and Plan 3 members can also purchase up to 24 months of service credit lost because of an on-the-job injury.

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PERS members may also purchase up to five years of additional service credit once eligible for retirement. This credit can only be purchased at the time of retirement and can be used only to provide the member with a monthly annuity that is paid in addition to the member's retirement benefit.

Beneficiaries of a PERS Plan 2 or Plan 3 member with 10 years of service who is killed in the course of employment receive retirement benefits without actuarial reduction, if the member was not at normal retirement age at death. This provision applies to any member killed in the course of employment, on or after June 10, 2004, if found eligible by the Department of Labor and Industries.

A one-time duty-related death benefit is provided to the estate (or duly designated nominee) of a PERS member who dies in the line of service 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 said member's covered employment, if found eligible by the Department of Labor and Industries.

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% for state agencies and local government unit employees, and at 7.5% for state government elected officials. The Plan 2/3 employer rates include a component to address the PERS Plan 1 UAAL and an administrative expense that is currently set at 0.18%. 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. The Director of the Department of Retirement Systems sets Plan 3 employee contribution rates. Six rate options are available ranging from 5% to 15%; two of the options are graduated rates dependent on the employee's age. 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 August 31, 2015, are as follows:

	<u>PERS Plan 1</u>	<u>PERS Plan 2</u>	<u>PERS Plan 3</u>
Employer	11.18%	11.18%	11.18%
Employee	6.00	6.12	*

* Variable from 5% minimum to 15% maximum based on rate selected by the PERS 3 member.

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The Project and the employees made the required contributions. The Project's required contribution for the year ended August 31, 2015 was \$869,158.

Actuarial Assumptions

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

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

- **Inflation:** 3% total economic inflation; 3.75% salary inflation
- **Salary increases:** In addition to the base 3.75% salary inflation assumption, salaries are also expected to grow by promotions and longevity.
- **Investment rate of return:** 7.5%

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

Discount Rate

The discount rate used to measure the total pension liability for all DRS plans was 7.5%.

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

Long-Term Expected Rate of Return

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

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investment returns at various future times. The long-term expected rate of return of 7.5% approximately equals the median of the simulated investment returns over a 50-year time horizon.

Estimated Rates of Return by Asset Class

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

<u>Asset class</u>	<u>Target allocation</u>	<u>Percentage long-term expected real rate of return arithmetic</u>
Fixed income	20%	1.70%
Tangible assets	5	4.40
Real estate	15	5.80
Global equity	37	6.60
Private equity	23	9.60
	<u>100%</u>	

Sensitivity of NPL

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

	<u>1% Decrease (6.5%)</u>	<u>Current discount rate (7.5%)</u>	<u>1% Increase (8.5%)</u>
PERS 1	\$ 5,371,062	4,411,541	3,586,440
PERS 2/3	10,385,560	3,551,771	(1,680,606)

Pension Plan Fiduciary Net Position

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

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

At August 31, 2015, the Project reported a liability of \$7,963,312 for its proportionate share of the net pension liabilities as follows:

	Net pension liability
PERS 1	\$ 4,411,541
PERS 2/3	3,551,771

The net pension liability was measured as of June 30, 2015 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. At June 30, the Project's proportionate share of the collective net pension liabilities was as follows:

	Proportionate share June 30, 2014	Proportionate share June 30, 2015	Change in proportion
PERS 1	0.158832%	0.162184%	0.003352%
PERS 2/3	0.184485	0.191162	0.006677

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

Pension Expense, Deferred Outflows and Deferred Inflows

For the year ended August 31, 2015, the Project recognized pension expense of \$938,372. At August 31, 2015, the Project reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

PERS Plan 1	Deferred outflows of resources	Deferred inflows of resources
Differences between expected and actual experience	\$ —	—
Net difference between projected and actual investment earnings on pension plan investments	—	(241,360)
Changes of assumptions	—	—
Changes in proportion and differences between contributions and proportionate share of contributions	—	—
Contributions subsequent to the measurement date	82,304	—
Total	\$ 82,304	(241,360)

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PERS Plan 2/3	Deferred outflows of resources	Deferred inflows of resources
Differences between expected and actual experience	\$ 377,554	—
Net difference between projected and actual investment earnings on pension plan investments	—	(948,154)
Changes of assumptions	5,723	—
Changes in proportion and differences between contributions and proportionate share of contributions	—	(3,276)
Contributions subsequent to the measurement date	102,031	—
Total	\$ 485,308	(951,430)

Deferred outflows of resources related to pensions resulting from the Project's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended August 31, 2016. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

		PERS Plan 1
Year ended August 31:		
2016	\$	(48,272)
2017		(48,272)
2018		(48,272)
2019		(48,272)
2020		(48,272)
Thereafter		—
Total	\$	(241,360)

		PERS Plan 2
Year ended August 31:		
2016	\$	(113,630)
2017		(113,630)
2018		(113,630)
2019		(113,630)
2020		(113,630)
Thereafter		—
Total	\$	(568,150)

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Deferred Compensation Plans

The Project also offers its employees deferred compensation plans created in accordance with Internal Revenue Code Sections 457 and 401(a) permitting employees to defer a portion of their salary until future years. The Project provides a 50% match of employee contributions capped at 2% of regular straight-time wages. The deferred compensation is not available to employees until separation from service through termination, retirement, death, or unforeseeable emergency. The plan assets are held in trust for the exclusive benefit of Plan participants and beneficiaries.

(7) Deferred Outflow of Resources and Regulatory Assets

The Wells Hydroelectric Project had deferred outflows of \$1,608,235 at August 31, 2015. Deferred outflows consist of unamortized losses on reacquired debt related to the sale of bonds and pension related costs.

The Wells Hydroelectric Project had regulatory assets of \$12,874,611 at August 31, 2015. Those balances are net of accumulated amortization of \$36,510,177 in 2015. Regulatory assets amortized by the Project consist of the following: improvements to recreational facilities, repair and maintenance costs, miscellaneous fish improvements, preliminary survey and investigation, legal settlement charges, and miscellaneous clearing accounts. Regulatory assets are amortized using the sinking fund method (6% rate).

(8) Related-Party Transactions

As discussed in note (1), the Project represents only one department of the District. Related-party transactions occur when the Project and the District's electric distribution system share facilities, employees, equipment or other resources, often making it necessary for one department to reimburse the other for use of the shared resource. Related-party transactions for the year ended August 31, 2015 include building expenses, salary costs, network costs, travel costs, and other miscellaneous items and are as follows:

Received from the distribution system	\$ 13,201,018
Paid to the distribution system	17,235,790

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Schedules of Required Supplementary Information (Unaudited)

August 31, 2015

Last 10 Fiscal Years*

Schedule of the Project's Proportionate Share of the Net Pension Liability

PERS Plan 1

Employer's proportion of the net pension liability (asset)		0.162184%
Employer's proportionate share of the net pension liability	\$	4,411,541
Employer's covered employee payroll		8,930,000
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll		49.40%
Plan fiduciary net position as a percentage of the total pension liability		59.10%

PERS Plan 2/3

Employer's proportion of the net pension liability (asset)		0.001912%
Employer's proportionate share of the net pension liability	\$	3,551,771
Employer's covered employee payroll		8,930,000
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll		39.77%
Plan fiduciary net position as a percentage of the total pension liability		89.20%

Schedule of Project Contributions

PERS Plan 1

Contractually required contributions	\$	745,396
Contributions in relation to the contractually required contribution		(745,396)
Contribution deficiency (excess)		—
Covered employer payroll		8,930,000
Contributions as a percentage of covered employee payroll		8.35%

PERS Plan 2/3

Contractually required contributions	\$	851,534
Contributions in relation to the contractually required contribution		(851,534)
Contribution deficiency (excess)		—
Covered employer payroll		8,930,000
Contributions as a percentage of covered employee payroll		9.54%

Notes to Schedules:

See note 2 of DRS Participating Employer Financial Information report for these percentages for each plan.

There are no factors that significantly affect trends in the amounts reported above. First year reporting.

*Until a full 10-year trend is compiled, governments should present information only for those years for which information is available.