WELLS HYDROELECTRIC PROJECT

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

FINANCIAL STATEMENTS

Including Independent Auditors' Report

As of and for the Years Ended August 31, 2016 and 2015

WELLS HYDROELECTRIC PROJECT
East Wenatchee, Washington

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As of and for the Years Ended August 31, 2016 and 2015

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INDEPENDENT AUDITORS' REPORT

To the Board of Commissioners
Public Utility District No.1 of Douglas County, Washington
East Wenatchee, WA

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), as of and for the year ended August 31, 2016, and the related notes to the financial statements which collectively comprise the Project's financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 Projects 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 Projects internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Wells Hydroelectric Project as of August 31, 2016, and the respective changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Prior Period Financial Statements

The financial statements of the Wells Hydroelectric Project, as of and for the year ended August 31, 2015, were audited by other auditors whose report dated January 20, 2016, expressed an unmodified opinion on those statements.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the financial position of Wells Hydroelectric Project and do not purport to, and do not, present fairly the financial position of the Public Utility District No. 1 of Douglas County, Washington, as of August 31, 2016 and the respective changes in financial position, or cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the required supplementary information as listed in the table of contents be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Baker Tilly Virchow Krause, LLP

Madison, Wisconsin
December 8, 2016

MANAGEMENT DISCUSSION AND ANALYSIS

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

Management's Discussion and Analysis (Unaudited)

August 31, 2016 and 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, 2016 and 2015. 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, deferred outflows and deferred inflows 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, 2016 and 2015.

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, 2016 and 2015, 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.

Condensed Comparative Financial Information (Amounts in Thousands)

Statements of Net Position

	August 31		
	2016	**2015**	**2014**
Assets:			
Current	$ 44,130	$ 40,812	$ 131,546
Net electric plant	281,367	242,084	230,236
Noncurrent assets and deferred outflows	48,349	89,491	17,435
Total assets and deferred outflows	$ 373,846	$ 372,387	$ 379,217
Liabilities:			
Current	$ 42,079	$ 34,534	$ 37,234
Noncurrent	189,843	205,546	217,402
Deferred inflows	647	1,636	—
Total liabilities	232,569	241,716	254,636
Net position:			
Net investment in capital assets	169,615	116,173	104,119
Restricted for debt service	30,394	13,400	15,980
Unrestricted	(58,732)	1,098	4,482
Total net position	141,277	130,671	124,581
Total liabilities, deferred inflows and net position	$ 373,846	$ 372,387	$ 379,217

Statements of Revenues, Expenses, and Changes in Net Position

	August 31		
	2016	**2015**	**2014**
Operating revenues	$ 52,007	$ 53,383	$ 49,353
Operating expenses	32,075	31,463	29,093
Operating income	19,932	21,920	20,260
Nonoperating expenses	(9,326)	(7,311)	(11,810)
Change in net position	10,606	14,609	8,450
Net position, beginning of year	130,671	124,581	116,131
Effect of accounting change in pensions, as previously reported	—	(8,519)	—
Net position, beginning of year, as restated	130,671	116,062	116,131
Net position, end of year	$ 141,277	$ 130,671	$ 124,581

Financial Analysis

Assets

Current assets decreased 8% from 2015 to 2016 and decreased 12% from 2014 to 2015. The decrease in current assets is primarily from reductions in accounts receivable. Net utility plant increased by $39 million from 2015 to 2016 and increased by $11.8 million from 2014 to 2015 primarily from construction projects reclassified from construction work in progress to depreciable assets. Noncurrent assets, regulatory assets and deferred outflows decreased 234% from 2015 to 2016 and 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. Noncurrent assets decreased primarily from the spending of bond funds on construction projects.

Liabilities

Current liabilities increased 22% from 2015 to 2016 and decreased by 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 8% from 2015 to 2016 and 5% from 2014 to 2015 was due to normal maturities of long-term debt.

Net Position

The Project's net position increased 8% from 2015 to 2016 and 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, the increase is due to new reporting standards relating to pensions.

Statement of Revenues, Expenses, and Changes in Net Position

Project revenue decreased 3% from 2015 to 2016 and 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 2% from 2015 to 2016 and increased 8% from 2014 to 2015, primarily due to an increase in depreciation expense. Maintenance also increased due to seismic monitoring costs and equipment upgrades and replacements in the Project’s infrastructure.

Investment income increased 194% from 2015 to 2016 and 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 9% from 2015 to 2016 and 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.

Capital Asset and Long-Term Debt Activity

As of August 31, 2016, and 2015 the Project had $148 and $116 million invested in capital assets, net of accumulated depreciation. The Project's capital assets consist of a hydroelectric generation plant, transmission facilities, fish 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 has been returned to service and is showing improved efficiencies. Work on the second unit is now underway. 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 may be required.

The Wells Project is in the process of a modernizing their on-site fish hatchery. The 2.5 year, $41 million dollar project is approximately 70% complete as of August 31, 2016 and is on schedule to be completed next summer.

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, 2016 and 2015, the total amount outstanding was $9.5 and $9.4 million, respectively.

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.

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

Statements of Net Position

August 31, 2016 and 2015

Assets and Deferred Outflows	**2016**	**2015**
Current assets:		
Restricted:		
Debt repayment funds – cash	$ 23,491,005	$ 19,867,300
Debt repayment funds – investments	6,903,113	4,308,496
Reserve and contingency fund – cash	2,303,287	3,736,611
Reserve and contingency fund – investments	4,516,441	—
Total restricted	37,213,846	27,912,407
Unrestricted:		
Cash	201	868,632
Investments	3,883,816	4,842,078
Accounts receivable	2,556,318	6,705,556
Other assets	476,159	483,197
Total unrestricted	6,916,494	12,899,463
Total current assets	44,130,340	40,811,870
Noncurrent assets:		
Restricted:		
Construction funds – cash	12,871,581	66,520,528
Construction funds – investments	23,706,524	8,487,991
Total restricted	36,578,105	75,008,519
Electric plant:		
Electric plant in service	314,642,016	309,355,136
Construction work in progress	80,757,206	41,135,257
Gross electric plant	395,399,222	350,490,393
Less accumulated depreciation and amortization	114,032,083	108,406,104
Net electric plant	281,367,139	242,084,289
Regulatory assets	9,842,834	12,874,611
Total noncurrent assets	291,209,973	254,958,900
Deferred outflows:		
Loss on reacquired debt	749,556	1,040,623
Pension related outflows	1,178,084	567,612
Total assets and deferred outflows	$ 373,846,058	$ 372,387,524

See accompanying notes to financial statements.

(Continued)

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

Statements of Net Position

August 31, 2016 and 2015

Liabilities, Deferred Inflows and Net Position	**2016**	**2015**
Current liabilities:		
Accounts payable	$ 17,394,222	$ 14,756,754
Other accrued liabilities	1,432,144	1,484,949
Excess revenue fund	2,397,732	1,402,610
Payable from restricted assets:		
Accrued interest payable	4,172,008	3,490,073
Current portion long-term debt	16,682,988	13,400,000
Total current liabilities	42,079,094	34,534,386
Noncurrent Liabilities:		
Bonds payable, excluding current portion	167,311,593	183,874,581
Unamortized bond premiums and discounts	4,292,495	4,554,487
Bonds payable, net	171,604,088	188,429,068
Intradistrict note payable	9,355,000	9,475,000
Compensated absences	734,406	710,012
Net pension liability	8,149,782	6,931,602
Total noncurrent liabilities	189,843,276	205,545,682
Total liabilities	231,922,370	240,080,068
Deferred inflows:		
Gain on required debt	417,468	443,470
Pension related inflows	229,645	1,192,790
Net position:		
Net investment in capital assets	169,614,916	116,172,812
Restricted for debt service	30,394,118	13,400,000
Unrestricted	(58,732,459)	1,098,384
Total net position	141,276,575	130,671,196
Total liabilities and net position	$ 373,846,058	$ 372,387,524

See accompanying notes to financial statements.

WELLS HYDROELECTRIC PROJECT

Statements of Revenues, Expenses, and Changes in Net Position

Year ended August 31, 2016 and 2015

	2016	2015
Operating revenues	$ 52,007,064	$ 53,382,862
Operating expenses:		
Operations	18,813,196	18,908,912
Maintenance	6,257,888	5,891,809
Depreciation	5,617,644	5,251,200
Taxes	1,386,816	1,410,720
Total operating expenses	32,075,544	31,462,641
Net operating revenue	19,931,520	21,920,221
Nonoperating revenues (expenses):		
Interest income	521,096	177,376
Interest expense	(8,344,018)	(9,177,669)
Amortization: other charges, debt discounts and premiums	(3,034,523)	(3,125,651)
Other	1,531,305	4,815,316
Total nonoperating expenses	(9,326,140)	(7,310,628)
Change in net position	10,605,379	14,609,593
Net position, beginning of year	130,671,196	116,061,603
Net position, end of year	$ 141,276,575	$ 130,671,196

See accompanying notes to financial statements.

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

Statements of Cash Flows

Years ended August 31, 2016 and 2015

	2016	2015
Cash flow from operating activities:		
Receipts from customers	$ 53,002,186	$ 50,553,603
Payments to Employees & Payroll Related	(12,441,523)	(12,622,467)
Payments to Suppliers & Other Agencies	(13,554,500)	(16,526,486)
Net cash provided by operating activities	27,006,163	21,404,650
Cash flows from investing activities:		
Purchase of investments	(35,412,833)	(21,142,916)
Proceeds from sales and maturities of investments	14,737,124	14,649,014
Interest on investments	767,139	301,208
Net cash (used in) provided by investing activities	(19,908,570)	(6,192,694)
Cash flows from capital and related financing activities:		
Additions to electric plant in service	(39,357,638)	(15,856,008)
Proceeds from capital contributions	—	4,100,000
Proceeds from issuance of long-term debt, net of debt discount and premium	—	64,535,277
Cost of issuance, underwriter's discount	—	(431,919)
Principal payments on long-term debt-defeased 2005 bonds	—	(67,075,000)
Principal payments on long-term debt-scheduled maturities	(13,285,000)	(16,095,000)
Interest payments on long-term debt	(7,472,377)	(10,689,874)
Build America bonds interest rebates	690,425	696,651
Net cash used in capital and related financing activities	(59,424,590)	(40,815,873)
Net decrease in cash and cash equivalents	(52,326,997)	(25,603,917)
Cash and cash equivalents, beginning of year	90,993,071	116,596,988
Cash and cash equivalents, end of year	$ 38,666,074	$ 90,993,071
Reconciliation of net operating income to net cash provided by operating activities:		
Operating income	$ 19,931,520	$ 21,920,221
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	5,617,644	5,251,200
Cash provided by changes in operating assets and liabilities:		
Receivables	983,379	(2,369,809)
Other assets	12,557	(83,880)
Excess revenue fund	995,125	(2,829,259)
Accounts payable – excluding construction payables	(519,541)	(347,583)
Other current liabilities	—	(118,915)
Compensated absences	(14,521)	(17,325)
Net cash provided by operating activities	$ 27,006,163	$ 21,404,650
Reconciliation of Cash and Cash Equivalents to Statements of Net Position accounts:		
Cash and Investments	$ 200	$ 868,632
Restricted Cash and Investments	38,665,874	90,124,439
Cash and cash equivalents, end of year	$ 38,666,074	$ 90,993,071

See accompanying notes to financial statements.

(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 non-employer contributing entity, to a defined benefit pension plan after the measurement date of the government's beginning net pension liability. Currently, the Project participates in a multiple-employer plan (Washington State Public Employees Retirement System). The Project has evaluated this statement and determined that its contributions after the measurement date need to be reported for pension related purposes.

In February 2015 GASB issued Statement No. 72, *Fair Value Measurement and Application*. This statement provides guidance for applying fair value to investments. Wells Project evaluated this statement and determined the Project's investments are required to be measured and reported at fair value. See note 2 for implementation details.

In June 2015 GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This statement provides guidance on identifying the context of the current governmental financial reporting environment – the hierarchy of generally accepted accounting principles (GAAP). Wells Project evaluated this statement and implemented its objective for fiscal year 2016.

In December 2015 GASB issued Statement No. 79, *Certain External Investment Pools and Pool Participants*. This statement provides guidance for addressing accounting and financial reporting for certain external investment pools and pool participants. Wells Project evaluated this statement and determined the Project is a pool participant and has implemented this objective to make appropriate note disclosures.

(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 certain 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 non-operating 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 generation and transmission plant is 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. Depreciation of general plant assets are recorded using the straight-line method.

(d) Cash and Cash Equivalents

For purposes of the statements of cash flows, the Project considers all short-term investments with an initial 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.

(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 non-ownership 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.

(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 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. As a pool participant, the Project does not have limitations or restrictions on withdrawals.

The Project's investments consist of direct obligations of the U.S. Government, government sponsored enterprises (agencies), and municipal bonds of U.S., states and local governments, 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.

Fair Value - The Project categorizes its fair value measurement within the hierarchy established by GAAP. The hierarchy is based on the valuation inputs to measure the fair value of the asset. Level 1inputs are quoted prices in the active markets for identical assets; Level 2 inputs are significant other observable inputs; level 3 inputs are significant unobservable inputs. The valuation method for fair value measurements as of August 31, 2016 and 2015 are as follows:

Investment Type	Balance as of August 31, 2016			2016	2015
	Level 1	**Level 2**	**Level 3**	**Total**	**Level 2**
Federal Agency Securities	$ —	$ 27,207,906	$ —	$ 27,207,906	$ 6,243,750
Municipal Bond Securities	—	14,589,484	—	14,589,484	7,207,246
Total	$ —	$ 41,797,390	$ —	$ 41,797,390	$ 13,450,996

Interest Rate Risk – The risk the value of investments will decrease as a result of a rise in interest rates.

As of August 31, 2016 the average maturities of investments are as follows:

Investment	**Fair Value**	**Less than 1 year**	**1-5 years**
Federal Agency Securities	$ 27,207,906	$ 11,231,853	$ 15,976,053
Municipal Bond Securities	14,589,484	1,126,192	13,463,292
Total	$ 41,797,390	$ 12,358,045	$ 29,439,345

As of August 31, 2015 the average maturities of investments are as follows:

Investment	**Fair Value**	**Less than 1 year**	**1-5 years**
Federal Agency Securities	$ 10,552,246	$ 4,308,496	$ 6,243,750
Municipal Bond Securities	7,207,246	1,108,754	6,098,492
Total	$ 17,759,492	$ 5,417,250	$ 12,342,242

Credit Risk – State law limits investment authority to local governments. The projects investments are made in investment types authorized by state law.

As of August 31, 2016 the credit quality ratings of debt securities are as follows:

Investment	**Fair Value**	**Rating**	**Rating Organization**
Federal Agency Securities	$ 27,207,906	AAA	S&P
Municipal Bond Securities	14,589,484	A1/Aa/AAA	S&P

As of August 31, 2015 the credit quality ratings of debt securities are as follows:

Investment	**Fair Value**	**Rating**	**Rating Organization**
Federal Agency Securities	$ 6,243,750	AAA	S&P
Municipal Bond Securities	7,207,246	A1/Aa/AAA	S&P

Concentration of Credit Risk – As of August 31, 2016 the Project had municipal bond investments in the amount of $14,589,484 (approximately 35%) of the investment portfolio. As of August 31, 2015 the Project had municipal bond investments in the amount of $7,207,246 (approximately 40%) of the investment portfolio. These municipal bonds are not guaranteed by the U.S. Government.

(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, 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, 2015	Increase	Decrease	Balance August 31, 2016
Utility plant not being depreciated:				
Land and land rights	$ 52,177,902	$ —	$ —	$ 52,177,902
Construction work in progress	41,135,257	44,127,026	(4,505,077)	80,757,206
Subtotal	93,313,159	44,127,026	(4,505,077)	132,935,108
Utility plant being depreciated:				
Hydraulic generation	216,603,363	5,254,630	(282,809)	221,575,184
Transmission	18,953,002	—	—	18,953,002
General	21,620,868	478,918	(163,858)	21,935,928
Subtotal	257,177,233	5,733,548	(446,667)	262,464,114
Accumulated depreciation	(108,406,104)	(5,789,417)	163,438	(114,032,083)
Net plant being depreciated	148,771,129	(55,869)	(283,229)	148,432,031
Net utility plant – Wells Project	$ 242,084,288	$ 44,071,157	$ (4,788,306)	$ 281,367,139

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	17,656,518	(41,666,695)	41,135,257
Subtotal	116,536,567	18,443,287	(41,666,695)	93,313,159
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	327,527	(140,342)	21,620,868
Subtotal	216,886,299	40,431,276	(140,342)	257,177,233
Accumulated depreciation	(103,187,107)	(5,359,339)	140,342	(108,406,104)
Net plant being depreciated	113,699,192	35,071,937	—	148,771,129
Net utility plant – Wells Project	$ 230,235,759	$ 53,515,224	$ (41,666,695)	$ 242,084,288

(4) Long-Term Debt

Wells Hydroelectric Project

	Hydroelectric Project					
	Purpose	**Balance August 31, 2015**	**Additions**	**Reductions**	**Balance August 31, 2016**	**Due within one year**
Revenue Bonds:						
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	4,420,000	—	1,025,000	3,395,000	1,075,000
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	49,935,000	—	1,030,000	48,905,000	1,060,000
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	41,965,000	—	1,080,000	40,885,000	1,100,000
Series of 2010C, serial bonds maturing annually to September 1, 2029, interest at 3.00%–5.00%	Refunding	9,455,000	—	955,000	8,500,000	995,000
Series of 2012, serial bonds maturing annually to September 1, 2018, interest at 0.40%–1.75%	Refunding	33,135,000	—	9,195,000	23,940,000	9,270,000
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%	Refunding	31,675,000	—	—	31,675,000	1,105,000
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%	Refunding	24,155,000	—	—	24,155,000	1,160,000
Series of 2015C, serial bonds maturing annually to September 1, 2016 and term bonds maturing September 1, 2018, interest at 4.654%–5.112%	Refunding	2,419,581	—	—	2,419,581	797,988
Revenue bonds payable		$ 197,159,581	—	13,285,000	183,874,581	16,562,988

The changes in long-term debt, including the portion maturing currently, for the year ended August 31, 2016 and 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		(67,075,000)
Long-term debt as of August 31, 2015		197,159,581
Principal payments		(13,285,000)
Long-term debt as of August 31, 2016	$	183,874,581

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 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, 2016:

		Principal		**Interest**		**Total**
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		5,060,000		6,538,894		11,598,894
2022–26		28,530,000		29,015,211		57,545,211
2027–31		34,160,000		21,501,402		55,661,402
2032–36		38,115,000		12,451,118		50,566,118
2037–41		26,520,000		3,757,059		30,277,059
	$	183,874,581	$	102,353,518	$	286,228,099

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 2016 and 2015.

Following is a summary of the debt service requirements for the intra-district note payable at August 31, 2016.

	Principal	Interest	Total
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	140,000	342,458	482,458
2022–26	780,000	1,626,048	2,406,048
2027–31	945,000	1,460,594	2,405,594
2032–36	1,140,000	1,260,297	2,400,297
2037–41	1,375,000	1,018,806	2,393,806
2042–46	1,665,000	727,169	2,392,169
2047–51	2,000,000	375,375	2,375,375
2052–55	920,000	35,805	955,805
	$ 9,475,000	$ 8,267,395	$ 17,742,395

Advance Debt Refunding

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 $2,735,664.

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 $443,469.

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, and 2016 the escrow agent was holding cash and investments of $27,842,163 and $20,328,154, 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.

(5) Other Commitments and Contingencies

(a) 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 and 2016, the Project made payments of $258,476 and $261,970 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.

(b) 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.

(c) 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. Toshiba America Energy Systems has completed the first unit and the second unit is now underway. The first unit was completed behind schedule and the contract provides liquidated damages, of which $3.5 million has been withheld from payments.

(d) 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 2016 and 2015:

Aggregate Pension Amounts – PERS Plans 1/2/3

	2016	2015
Net pension liabilities*	$ 8,149,782	$ 7,963,312
Pension assets	—	—
Deferred outflows of resources	1,178,084	567,612
Deferred inflows of resources	229,645	1,192,790
Pension expense	(372,617)	69,213

* For 2016, current portion of net pension liability of $1,014,530 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.

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 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.

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.

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, 2016 and 2015, are as follows:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
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.

The Project and the employees made the required contributions. The Project's required contribution for the year ended August 31, 2016 and 2015 was $1,028,178 and $869,158, respectively.

Actuarial Assumptions

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2016 with a valuation date of June 30, 2016. 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 2016 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2016. Plan liabilities were rolled forward from June 30, 2015 to June 30, 2016, 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 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, 2016 and 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.

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

Sensitivity of NPL

The table below presents the Project's proportionate share of the net pension liability as of June 30, 2016 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.

	1% Decrease (6.5%)	Current discount rate (7.5%)	1% Increase (8.5%)
PERS 1	$ 5,188,032	$ 4,302,209	$ 3,539,905
PERS 2/3	8,952,009	4,862,104	(2,531)

The table below presents the Project's proportionate share of the net pension liability as of June 30, 2015 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.

	1% Decrease (6.5%)	Current discount rate (7.5%)	1% Increase (8.5%)
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.

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

At August 31, 2016 and 2015, the Project reported a liability of $9,164,313 and 7,963,312 for its proportionate share of the net pension liabilities as follows:

	Net pension liability	
	2016	2015
PERS 1	$ 4,302,209	$ 4,411,541
PERS 2/3	4,862,104	3,551,771

The net pension liability was measured as of June 30, 2016 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, 2015	Proportionate share June 30, 2016	Change in proportion
PERS 1	0.162184%	0.154055%	0.008129%
PERS 2/3	0.191162	0.185707	0.005455

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

Pension Expense, Deferred Outflows and Deferred Inflows

For the year ended August 31, 2016, the Project recognized pension expense of $(372,617). At August 31, 2016, 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	108,323	—
Changes of assumptions	—	—
Changes in proportion and differences between contributions and proportionate share of contributions	—	—
Contributions subsequent to the measurement date	71,819	—
Total	$ 180,142	$ —

PERS Plan 2/3	Deferred outflows of resources	Deferred inflows of resources
Differences between expected and actual experience	$ 258,904	$ (160,506)
Net difference between projected and actual investment earnings on pension plan investments	594,981	—
Changes of assumptions	50,254	—
Changes in proportion and differences between contributions and proportionate share of contributions	—	(69,139)
Contributions subsequent to the measurement date	93,802	—
Total	$ 997,941	$ (229,645)

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)

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:		
2017	$	(26,671)
2018		(26,671)
2019		99,483
2020		62,182
2021		—
Thereafter		—
Total	$	108,323

		PERS Plan 2/3
Year ended August 31:		
2017	$	(18,175)
2018		(18,175)
2019		432,917
2020		277,927
2021		—
Thereafter		—
Total	$	674,494

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 Outflows, Inflows of Resources and Regulatory Assets

The Wells Hydroelectric Project had deferred outflows of $1,608,235 and $1,927,640 at August 31, 2015 and 2016. Deferred outflows consist of unamortized losses on reacquired debt related to the sale of bonds and pension related estimated costs. The Project had deferred inflows of $1,636,260 and $647,113 at August 31, 2015 and 2016. Deferred inflows consist of unamortized gains on reacquired debt related to the sale of bonds and pension related gains.

The Wells Hydroelectric Project had regulatory assets of $12,874,611 and $9,842,834 as of August 31, 2015 and 2016. Those balances are net of accumulated amortization of $45,382,509 in 2015 and $48,939,448 in 2016. 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 years ended August 31, 2016 and 2015 include building expenses, salary costs, network costs, travel costs, and other miscellaneous items and are as follows:

	2016	2015
Received from the distribution system	$ 13,989,981	$ 13,201,018
Paid to the distribution system	17,129,150	17,235,790

(9) Subsequent Events

The Project's series 2006A bonds were called effective September 1, 2016 in the amount of $2,320,000 through proceeds received from an intersystem loan from the Electric Distribution System. The loan was authorized by the board on August 22, 2016 will be repaid over a two-year period.

REQUIRED SUPPLEMENTARY INFORMATION

REQUIRED SUPPLEMENTARY INFORMATION

Public Utility District No. 1 of Douglas County
Schedule of Proportionate Share of the Net Pension Liability
PERS Plan 1
As of June 30, 2016
Last 10 Fiscal Years

		2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Employer's proportion of the net pension liability (asset)	%	0.162184%	0.154055%								
Employer's proportionate share of the net pension liability	$	8,483,732	8,058,509								
TOTAL	$	8,483,732	8,058,509								
Employer's covered employee payroll	$	17,173,115	17,359,459								
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	%	49.40%	46.42%								
Plan fiduciary net position as a percentage of the total pension liability	%	59.10%	57.03%								

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

Notes to Schedule:
There are no factors that significantly affect trends in the amounts reported above. Second year reporting.

REQUIRED SUPPLEMENTARY INFORMATION

Public Utility District No. 1 of Douglas County
Schedule of Employer Contributions
PERS Plan 1
As of June 30, 2016
Last 10 Fiscal Years

		2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Contractually required contributions	$	745,396	856,049								
Contributions in relation to the contractually required contributions	$	(745,396)	(856,049)								
Contribution deficiency (excess)	$	0	0								
Covered Employer Payroll	$	17,173,115	17,359,459								
Contributions as a percentage of covered employee payroll	%	4.34%	4.93%								

Notes to Schedule:
There are no factors that significantly affect trends in the amounts reported above. Second year reporting.

REQUIRED SUPPLEMENTARY INFORMATION

Public Utility District No. 1 of Douglas County
Schedule of Proportionate Share of the Net Pension Liability
PERS Plan 2 & 3
As of June 30, 2016
Last 10 Fiscal Years

		2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Employer's proportion of the net pension liability (asset)	%	0.191162%	0.185707%								
Employer's proportionate share of the net pension liability	$	6,830,329	6,635,419								
TOTAL	$	6,830,329	6,635,419								
Employer's covered employee payroll	$	17,173,115	17,359,459								
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	%	39.77%	38.22%								
Plan fiduciary net position as a percentage of the total pension liability	%	89.20%	85.82%								

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

Notes to Schedule:
There are no factors that significantly affect trends in the amounts reported above. Second year reporting.

REQUIRED SUPPLEMENTARY INFORMATION

Public Utility District No. 1 of Douglas County
Schedule of Employer Contributions
PERS Plan 2 & 3
As of June 30, 2016
Last 10 Fiscal Years

		2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Contractually required contributions	$	851,534	1,072,067								
Contributions in relation to the contractually required contributions	$	(851,534)	(1,072,067)								
Contribution deficiency (excess)	$	0	0								
Covered Employer Payroll	$	17,173,115	17,359,459								
Contributions as a percentage of covered employee payroll	%	4.96%	6.18%								

Notes to Schedule:
There are no factors that significantly affect trends in the amounts reported above. Second year reporting.