



Report of Independent Auditors and  
Combined Financial Statements for

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

December 31, 2011 and 2010

**MOSS-ADAMS<sub>LLP</sub>**

Certified Public Accountants | Business Consultants

*Acumen. Agility. Answers.*

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## REPORT OF INDEPENDENT AUDITORS

Board of Commissioners  
Public Utility District No. 1 of Klickitat County  
Goldendale, Washington

We have audited the accompanying combined balance sheets of Public Utility District No. 1 of Klickitat County (the District) as of December 31, 2011 and 2010 and the related combined statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These combined financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these combined 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 combined financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Public Utility District No. 1 of Klickitat County as of December 31, 2011 and 2010 and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Government Accounting Standards Board (GASB) 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 with sufficient evidence to express an opinion or provide any assurance.

*Moss Adams LLP*

Portland, Oregon  
July 5, 2012

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY -  
MCAG No. 1785  
DIRECTORY OF OFFICIALS**

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<u>Office</u>	<u>Official</u>	<u>Term</u>	<u>Term Expiration</u>
Board of Commissioners			
President	Randy L. Knowles	6 years	December 2012
Vice President	Dan G. Gunkel	6 years	December 2014
Secretary	Ray A. Mosbrucker	6 years	December 2016
Appointed Officials			
General Manager	James R. Smith	1313 S. Columbus	
Chief Financial Officer/Auditor	Shannon N. Crocker	Goldendale, WA 98620	
Public Utility District No. 1 of Klickitat County – Attorney	Ronald J. English	15624 111th Avenue N.E. Bothell, WA 98011	

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
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MANAGEMENT’S DISCUSSION AND ANALYSIS**

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This section provides an overview and analysis of key data presented in the basic financial statements for the years ended December 31, 2011 and 2010. Information within this section should be read in conjunction with the basic financial statements and accompanying notes.

**Overview of the Combined Financial Statements**

Public Utility District No. 1 of Klickitat County (the District) consists of the electric system, eight water systems and five wastewater systems. The District’s service area covers approximately 1,680 square miles in Klickitat County. The District also serves small areas in the surrounding counties of Yakima, Skamania and Benton. As of December 31, 2011 the District had 12,232 electric, 1,145 water, and 1,171 wastewater customers. The District’s wholesale activity is a significant part of the electric system business lines. Wholesale revenues are generated from the sale of the output from the Landfill Gas Project, a 36.5 MW facility, and from the White Creek Wind I power purchase contract, which the District owns 13% of the generated output from the 205 MW project.

The financial statements of the District report the self-supporting, proprietary activities of the District funded primarily by the sale of power, water and wastewater services. The District reports these business-type activities in a manner similar to private sector business enterprises, using the accrual basis of accounting, in accordance with accounting principles generally accepted in the United States of America.

The Balance Sheet presents information on the District’s assets and liabilities, with the difference between the two reported as net assets, and provides information regarding the nature and amount of resource investment (assets) and obligations incurred in the pursuit of such resources. This statement also provides a vehicle for evaluating the capital structure of the District and assessing liquidity and financial flexibility of the District.

The Statement of Revenues, Expenses and Changes in Net Assets reports revenues and expenses as well as change in net assets (net income) for this period. This statement provides a measurement of the District’s operations, helps to evaluate the level of cost recovery from charges for products and services, and can be used as a partial determinant of creditworthiness.

The Statement of Cash Flows provides information concerning cash receipts and disbursements during the reporting period resulting from operating, financing and investing activities. This information provides insight into the District’s ability to generate net cash flows to meet obligations, as they become due, and is an important indicator of the District’s liquidity and financial strength.

The Notes to Financial Statements provide additional information that is essential to a full understanding of the financial statements, as described above, including significant accounting policies, commitments, obligations, risks, contingencies and other financial matters of the District.

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
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MANAGEMENT’S DISCUSSION AND ANALYSIS**

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**Financial Highlights – 2011 to 2010**

- The year ended December 31, 2011 financial results recorded a \$570,704 change in net assets. The District was in compliance with its debt service coverage covenant at year-end.
- In 2011, the District completed a \$13.61 million bond sale to fund Electric Distribution capital construction and redeem a bond anticipation note.
- On 10/01/2011, the District imposed a 9.8% Electric Rate Increase.
- In 2011 the District capitalized 71.8% of the Land Fill Gas II (LFG II) project equating to \$51.2 million. LFG II is a 26.0 MW gas-fired combustion turbine and steam recovery generating facility located at the Roosevelt landfill.
- The District receives transmission revenues for providing transmission services for the White Creek Wind I project, Harvest Wind, Tuolumne, Windy Flats, Linden Farms, Windy Point, and from the Goldendale Energy Center, a 248 MW natural gas-fired combined cycle combustion turbine electric generating facility owned and operated by Puget Sound Energy. The revenue received from this business-line was approximately \$5,238,469.
- Customer growth was near 0.6% in 2011, which is slightly below the past 5 years.
- In 2011 the District took its second draw of \$401,589 on the Drinking Water State Revolving Fund Loan of \$1,175,566 for Glenwood’s Water System. The project will replace distribution lines and develop an additional water source for the Glenwood Water System, lifting moratoriums on new connections due to undersized distribution lines.
- Staff worked with each local community in which we serve either water or wastewater or both to review operations, rates and projected future projects. Rate increases were adopted for those systems where revenues did not cover estimated expenses and debt service.

**Financial Highlights – 2010 to 2009**

- The year ended December 31, 2010 financial results showed the continued financial strength of the District. The District was in compliance with its debt service coverage covenant at year-end with a change in net assets of \$22,267,750. A large portion of this change is from contributions of Transmission Plant for three different Wind projects, while \$3,850,574 is from Operations.
- In 2010 the District expended \$36.8 million on construction of the Land Fill Gas II (LFG II) project and \$7.5 million on Electric Distribution capital construction. LFG II is a 26.5 MW gas-fired combustion turbine and steam recovery generating facility located at the Roosevelt landfill expected to be online in 2011.

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
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MANAGEMENT’S DISCUSSION AND ANALYSIS**

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- In October 2010 the District took a first draw of \$232,248 on the Drinking Water State Revolving Fund Loan of \$1,175,566 for Glenwood’s Water System. The project will replace distribution lines and develop an additional water source for the Glenwood Water System, lifting moratoriums on new connections due to undersized distribution lines.
- The District receives transmission revenues for providing transmission services for the White Creek Wind I project, Harvest Wind, Tuolumne, Windy Flats, Linden Farms, Windy Point, and from the Goldendale Energy Center, a 248 MW natural gas-fired combined cycle combustion turbine electric generating facility owned and operated by Puget Sound Energy. The revenue received from this business-line was approximately \$5,145,000.
- Customer growth was near 1% in 2010, which is consistent over the last 4 years. Energy consumption was 1% lower than in 2009.
- Staff worked with each local community in which we serve either water or wastewater or both to review operations, rates and projected future projects. Rate increases were adopted for those systems where revenues did not cover estimated expenses and debt service.

**Condensed Comparative Financial Information**

**Combined balance sheet**

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Capital assets	\$ 227,511,508	\$ 222,592,618	\$ 167,546,723
Current, restricted and other assets	<u>65,301,286</u>	<u>65,613,629</u>	<u>103,677,107</u>
Total assets	<u>\$ 292,812,794</u>	<u>\$ 288,206,247</u>	<u>\$ 271,223,830</u>
Long-term liabilities	\$ 140,591,635	\$ 130,292,057	\$ 133,779,264
Current liabilities	<u>12,390,980</u>	<u>18,654,715</u>	<u>20,452,841</u>
Total liabilities	<u>152,982,615</u>	<u>148,946,772</u>	<u>154,232,105</u>
Invested in capital assets, net of related debt	94,217,644	91,370,913	72,287,796
Restricted	14,890,710	13,728,023	13,403,331
Unrestricted	<u>30,721,825</u>	<u>34,160,539</u>	<u>31,300,598</u>
Total net assets	<u>139,830,179</u>	<u>139,259,475</u>	<u>116,991,725</u>
Total liabilities and net assets	<u>\$ 292,812,794</u>	<u>\$ 288,206,247</u>	<u>\$ 271,223,830</u>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
MANAGEMENT’S DISCUSSION AND ANALYSIS**

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**Capital activity**

*2011 to 2010*

Net utility plant for the District increased \$5.0 million during 2011. Some of the large projects completed to plant in 2011 were White Creek to Roosevelt Transmission, Roosevelt Substation Upgrade, John Day Substation Upgrade, and Glenwood Substation Upgrade. The District is in the process of finalizing the construction of our LFG II facility and capitalized 71.8% of the project in 2011 equating to \$51.2 million.

*2010 to 2009*

Net utility plant for the District increased \$55 million during 2010. Some of the large projects completed to plant in 2010 were Linden Farm Wind, Biogas II Substation, Windy Flats, Harvest Wind, and Spearfish Substation Addition. These five projects contributed \$26 million to plant assets. Currently the District is in the process of constructing our LFG II facility expending \$36.8 million on this project in 2010.

**Debt activity**

*2011 to 2010*

The District issued \$13,610,000 in electric system revenue bonds in December 2011. The proceeds are being used to fund Electric Distribution capital construction and redeem a bond anticipation note.

*2010 to 2009*

The District took a first draw of \$232,248 on the Drinking Water State Revolving Fund Loan of \$1,175,566 for Glenwood’s Water System. The project will replace distribution lines and develop an additional water source for the Glenwood Water System with expected completion in 2011.

**Current, restricted, and other activity**

*2011 to 2010*

Current, restricted and other assets recognized \$7.1 million in construction funds due to capital construction bond proceeds. This was partially offset by the exhaustion of the 2009 capital construction bond proceeds being fully exhausted in 2011 along with the continued amortization of White Creek Wind I purchase power agreement.

*2010 to 2009*

Current, restricted and other assets decrease by \$38 million, primarily due to the expenditure of \$36.8 million in funds for construction of Landfill Gas II project.

**Overall results of operations**

*2011 to 2010*

The District’s 2011 results are slightly better than 2010 and continued their trend of positive operating income recording Net operating income of \$1,208,286.



**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
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MANAGEMENT’S DISCUSSION AND ANALYSIS**

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*2010 to 2009*

The District’s 2010 results are 25% better than expectations set during the planning and budget process. Net operating income of \$5,198,591 puts the District in a position of continued financial strength.

**Electric system operating results**

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Operating revenues	\$ 32,239,253	\$ 33,631,876	\$ 35,259,915
Operating expenses	<u>30,967,006</u>	<u>28,467,883</u>	<u>27,794,077</u>
Operating income	1,272,247	5,163,993	7,465,838
Net non-operating revenue (expense)	(1,633,256)	(3,513,666)	(2,679,412)
Capital contributions	<u>947,114</u>	<u>20,504,483</u>	<u>12,726,042</u>
Change in net assets (net income)	<u>\$ 586,105</u>	<u>\$ 22,154,810</u>	<u>\$ 17,512,468</u>

**Operating revenues**

*2011 to 2010*

The District recorded a 4.1% decrease in Operating revenues in 2011 vs. 2010 mainly attributed the end of a 3 year contract for White Creek Wind Generation and the continued decline in wholesale market prices for Landfill Gas and White Creek Wind Generation projects that are located within Klickitat County. These were partially offset by a 9.8% electric rate increase that went into effect on 10/01/2011.

*2010 to 2009*

The District had decreased retail sales of 3,493,486 KWH during 2010 leading to decreased electric revenues of \$1,955,982 over 2009 as follows: Residential sales down \$330,642, general service sales up \$115,961, industrial sales down \$133,660, irrigation sales down \$30,033 and street lighting up \$1,031. Other wholesale and transmission electric revenues decreased \$1,578,639 mainly due to decreased prices in wholesale markets for our Landfill Gas and wind generation projects that are located within Klickitat County. Overall revenues decreased by 5% during 2010.

**Operating expenses**

*2011 to 2010*

Operating expense increased by 8.8% in 2011. Mainly attributed to a 47.4% increase in depreciation expense from the 71.8% capitalization of the Landfill Gas Phase II Project. Power Generation costs were up 2.9% vs. 2010 due to the continued increase in generation from the LFG II project. SG&A expenses were down in 2011 by 3.7% vs. 2010 mainly attributed to the continued focus the district has placed on controlled spending and re-evaluating of expenses as it continues to work on focusing its efforts on finalizing the HW Hill Landfill Gas Project.

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*2010 to 2009*

Operating expense increased in 2010 by \$673,806. Power, Operations and Maintenance costs are down \$121,204 because of decreased power generation and purchases during 2010. Admin and General expense increased by \$659,340 mainly due to expensing consulting fees to The Energy Authority in preparation for upcoming Slice Contract with BPA during 2010. Taxes accrued for state and municipal governments decreased \$763,538 due a change in estimate in accrued taxes and a credit received on privilege tax during 2010. Finally depreciation expense increased on Distribution and Transmission Plant by \$522,669 due to the large amount of work orders closed in 2010 for these asset classes.

**Non-operating revenue/(expense)**

*2011 to 2010*

Non-operating expense decreased by \$1,880,410 which equates to 53.5% over 2010. This change is mainly attributed to additional capitalization of interest expense primarily due to the LFG II project.

*2010 to 2009*

Non-operating income overall decreased in 2010 by \$834,254 due to several factors. New interest expense incurred for the 2009 Bond Issue raised interest expense by \$385,521 after the refund of interest for Build America Bonds. Investment income decreased \$317,926 due to lower cash availability throughout the year because of funding of construction projects and continued lower interest rates in the state investment pool during 2010. Rent revenues decreased by \$108,640 during 2010.

**Capital contributions**

*2011 to 2010*

Capital contributions for the district in 2011 were \$947,114, a significant decreased compared to 2010. The capital contributions in 2010 were above normal contributions for a given year due to an \$18.4 million contribution of plant assets from the District’s agreements with Harvest Wind, Windy Flats and Linden Farms to maintain and operate transmission and substation equipment.

*2010 to 2009*

Capital contributions increased \$7,778,441 in 2010 over 2009. The capital contributions in 2010 were above normal contributions for a given year due to an \$18.4 million contribution of plant assets from the District’s agreements with Harvest Wind, Windy Flats and Linden Farms to maintain and operate transmission and substation equipment.

**Legal settlement**

There were no legal issues during 2011 or 2010 where the District received or disbursed a settlement.

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
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MANAGEMENT’S DISCUSSION AND ANALYSIS**

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**Water and wastewater systems operating results**

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Operating revenues	\$ 1,396,608	\$ 1,351,946	\$ 1,414,787
Operating expenses	<u>1,460,569</u>	<u>1,317,348</u>	<u>1,540,216</u>
Operating income	(63,961)	34,598	(125,429)
Net non-operating revenue/(expense)	18,574	15,515	(14,226)
Capital contributions and grants	<u>29,986</u>	<u>62,827</u>	<u>871,905</u>
Change in net assets (net income)	<u>\$ (15,401)</u>	<u>\$ 112,940</u>	<u>\$ 732,250</u>

**Operating revenues**

*2011 to 2010*

The District Water/Waste Water revenues recorded an increase of 3.3% in 2011.

*2010 to 2009*

The District Water/Waste Water revenues were down in 4% in 2010 mainly due to large sewer connection fees being recorded in 2009 for one customer in the amount of \$62,183. All other revenues were essentially unchanged from 2009.

**Operating expenses**

*2011 to 2010*

The expenses to operate the Water/Waste Water systems were up 10.9% or \$143,221 in 2011 compared to a 2010. This increase in operating expenses can be attributed to increased preventative maintenance schedules for all water/waste water facilities to avoid failures.

*2010 to 2009*

The expenses to operate the Water/Waste Water systems were down 14% or \$222,868 compared to a year ago. This decrease in operating expenses can be attributed to a change in the methodology of allocating Administrative Costs to Water/Waste Water systems during 2009. Also, initial cost of taking over operations for the Dallesport Wastewater and Industrial Park Water Systems only appears in 2009 not 2010.

**Non-operating revenue/(expense)**

*2011 to 2010*

Non-operating revenue increased by 19.7% primarily due to new service connection charges for the Dallesport Sewer system during 2011.

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
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MANAGEMENT’S DISCUSSION AND ANALYSIS**

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*2010 to 2009*

Non-operating revenue increased primarily due to service connection charges in the amount of \$15,497 for Dallesport Sewer system during 2010.

**Capital contributions and grants**

*2011 to 2010*

Capital contributions were in line with expectations during 2011 as no significant LUD’s were established.

*2010 to 2009*

The significant decrease was primarily due to the establishment of Ponderosa Park LOUD, contributing \$828,200 during 2009.

**The District looking forward 2012**

The District issued bonds in 2011 to finance capital improvements to the electric system and redeem a \$5.0 million bond anticipation note.

During 2012, the District will be in its first full year of their new BPA Slice rate structure. The District is continuing work on further improving and integrating their processes and data systems with TEA, who manages their day to day marketing and purchasing functions. In addition, BPA will be releasing the Slice Optimization computer application in September and the District and TEA are preparing to take advantage of the ability to control its share of the BPA system output.

The District will also be completing improvements on the HW Hill Landfill Gas generation facility. The District is working with a contractor who has yet to meet all the requirements of their contract, which will take focus from the District. The plant has been operating since October, 2011. 2012 also marks the first full year of a new Gas Supply Optimization agreement with Rabanco, the owner of the landfill where the HW Hill facility is located. While Rabanco owns the landfill, the District owns the gas rights for all methane produced in the landfill. As a result, the District has developed contracts and a close partnership in ensuring that the gas delivery is optimized.

The District does not anticipate further 230 kV transmission business line construction in 2012 due to the current electric and Renewable Energy Credit marketplace. The District does however; anticipate interconnection work in the coming years as those conditions change.

The District will also be continuing work on its transmission & distribution electric and water / waste water system customer interconnection and long range plan capital work, as well as operations and maintenance programs.



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**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY -  
MCAG No. 1785  
COMBINED BALANCE SHEETS**

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**ASSETS**

	December 31,	
	2011	2010
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 9,952,816	\$ 12,639,161
Notes receivable	164,495	162,938
Accounts receivable, net	1,295,620	1,128,610
Unbilled revenue	1,640,269	1,462,226
Other receivables	2,872,923	4,063,916
Materials and supplies	1,621,313	1,529,715
Prepayments	308,701	244,560
Current portion of prepaid power contract	1,180,359	1,180,359
	<u>19,036,496</u>	<u>22,411,485</u>
<b>RESTRICTED ASSETS</b>		
Special deposits	400	400
Construction funds	7,147,975	3,846,789
Special funds	15,454,649	14,307,309
	<u>22,603,024</u>	<u>18,154,498</u>
<b>CAPITAL ASSETS</b>		
Total plant in service	262,543,537	206,110,631
Construction work in progress	25,246,775	70,647,675
	<u>287,790,312</u>	<u>276,758,306</u>
Total utility plant	287,790,312	276,758,306
Accumulated provision for depreciation	(60,278,804)	(54,165,688)
	<u>227,511,508</u>	<u>222,592,618</u>
<b>OTHER ASSETS</b>		
Other investments and transmission deposits	2,195,740	2,451,853
Deferred debits and prepaid power contract	21,466,026	22,595,793
	<u>23,661,766</u>	<u>25,047,646</u>
<b>Total other assets</b>	<u>23,661,766</u>	<u>25,047,646</u>
<b>Total assets</b>	<u>\$ 292,812,794</u>	<u>\$ 288,206,247</u>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY -  
MCAG No. 1785  
COMBINED BALANCE SHEETS**

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**LIABILITIES AND NET ASSETS**

	December 31,	
	2011	2010
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 5,232,347	\$ 6,791,209
Current portion of long-term debt	3,432,579	3,391,010
Bond anticipation note	-	5,000,000
Consumers deposits	277,032	281,594
Other current and accrued liabilities	3,449,022	3,190,902
Total current liabilities	12,390,980	18,654,715
<b>NONCURRENT LIABILITIES</b>		
Compensated absences	190,434	267,443
Long-term debt	140,401,201	130,021,403
Deferred credits	-	3,211
Total noncurrent liabilities	140,591,635	130,292,057
Total liabilities	152,982,615	148,946,772
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	94,217,644	91,370,913
Restricted	14,890,710	13,728,023
Unrestricted	30,721,825	34,160,539
Total net assets	139,830,179	139,259,475
Total liabilities and net assets	\$ 292,812,794	\$ 288,206,247



**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY -  
MCAG No. 1785  
COMBINED STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS**

	Years Ended December 31,	
	2011	2010
<b>OPERATING REVENUES</b>		
Electric system		
Sales to retail customers	\$ 21,513,337	\$ 20,987,714
Sales to wholesale and transmission customers	10,725,916	12,644,162
Water/wastewater systems	<u>1,396,608</u>	<u>1,351,946</u>
Total operating revenues	<u>33,635,861</u>	<u>34,983,822</u>
<b>OPERATING EXPENSES</b>		
Power expense	8,571,212	9,910,919
Operations expense	8,193,639	7,230,448
Maintenance expense	3,313,267	2,781,833
Administrative and general expense	4,362,118	4,573,880
Depreciation expense	6,642,815	4,456,412
Tax expense	<u>1,344,524</u>	<u>831,739</u>
Total operating expenses	<u>32,427,575</u>	<u>29,785,231</u>
<b>OPERATING INCOME</b>	<u>1,208,286</u>	<u>5,198,591</u>
<b>NON-OPERATING REVENUES/(EXPENSES)</b>		
Interest income	183,497	170,437
Other non-operating revenues	1,290,175	1,418,709
Interest expense	(2,928,854)	(4,928,234)
Amortization expense	<u>(159,500)</u>	<u>(159,063)</u>
Total non-operating revenues/(expenses)	<u>(1,614,682)</u>	<u>(3,498,151)</u>
<b>INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS AND GRANTS</b>	(406,396)	1,700,440
<b>CAPITAL CONTRIBUTIONS AND GRANTS</b>	<u>977,100</u>	<u>20,567,310</u>
<b>CHANGE IN NET ASSETS</b>	<u>570,704</u>	<u>22,267,750</u>
<b>NET ASSETS, beginning of year</b>	<u>139,259,475</u>	<u>116,991,725</u>
<b>NET ASSETS, end of year</b>	<u>\$ 139,830,179</u>	<u>\$ 139,259,475</u>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY -  
MCAG No. 1785  
COMBINED STATEMENTS OF CASH FLOWS**

	Years Ended December 31,	
	2011	2010
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts from customers	\$ 34,472,566	\$ 40,804,708
Payments to suppliers for goods and services	(18,101,535)	(24,196,798)
Payments to employees for services	(6,660,894)	(6,391,239)
Taxes paid	(1,363,726)	(1,473,717)
Net change in cash flows from operating activities	<u>8,346,411</u>	<u>8,742,954</u>
<b>CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES</b>		
Proceeds from BPA transmission deposits	256,113	242,988
Other non-operating income	1,290,175	1,418,709
Net change in cash flows from non-capital financing activities	<u>1,546,288</u>	<u>1,661,697</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED</b>		
Principal payments on long-term debt	(8,392,009)	(2,557,263)
Issuance of long-term debt	14,011,589	-
Bond issuance costs	(207,520)	-
Interest payments	(3,142,014)	(4,935,937)
Capital contributions, DOE funds and grants	977,100	2,150,120
Deferred debits/credits - preliminary engineering	(2,567)	74,466
Capital expenditures	(11,561,710)	(41,085,119)
Net change in cash flows from capital and related financing activities	<u>(8,317,131)</u>	<u>(46,353,733)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Interest received	186,613	173,916
Net change in LGIP	(4,448,526)	33,055,628
Net change in cash flows from investing activities	<u>(4,261,913)</u>	<u>33,229,544</u>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>(2,686,345)</b>	<b>(2,719,538)</b>
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<b>12,639,161</b>	<b>15,358,699</b>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<b>\$ 9,952,816</b>	<b>\$ 12,639,161</b>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY -  
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COMBINED STATEMENTS OF CASH FLOWS**

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	Years Ended December 31,	
	<u>2011</u>	<u>2010</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES		
OPERATING INCOME	<u>\$ 1,208,286</u>	<u>\$ 5,198,591</u>
ADJUSTMENTS TO RECONCILE OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES		
Depreciation expense	6,642,815	4,456,412
Amortization of prepaid power contract	1,180,359	1,180,359
CHANGES IN OPERATING ASSETS AND LIABILITIES		
Receivables and unbilled revenue	841,267	320,370
Materials and supplies	(91,598)	305,576
Prepayments	(64,141)	2,013
Accounts payable	(1,558,862)	(1,934,126)
Customer deposits	(4,562)	(15,780)
Other current and accrued liabilities	273,067	(652,453)
Compensated absences	(77,009)	(96,038)
Deferred credits	<u>(3,211)</u>	<u>(21,970)</u>
Total adjustments	<u>7,138,125</u>	<u>3,544,363</u>
Net cash from operating activities	<u>\$ 8,346,411</u>	<u>\$ 8,742,954</u>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 1 – Organization and Significant Accounting Policies**

**Organization and combined financial statements** – Public Utility District No. 1 of Klickitat County, Washington (the District) is a municipal corporation governed by an elected three-person Board of Commissioners. The District’s reporting entity is comprised of the combined electric system, eight water systems and five wastewater systems. All significant intercompany balances and transactions have been eliminated from the combined amounts reported. The District has no component units. The District’s service area covers approximately 1,680 square miles in Klickitat County. The District also serves small areas in the surrounding counties of Yakima, Skamania and Benton. As of December 31, 2011 the District had 12,232 electric, 1,145 water, and 1,171 wastewater customers. The District’s wholesale activity is a significant part of the electric system business lines. Wholesale revenues are generated from the sale of the output from the Landfill Gas project, 10.5 MW, and from the White Creek Wind I power purchase contract. The District owns 13% of the generated output from the White Creek Wind I 205 MW project.

**Basis of accounting and presentation** – The accounting policies of the District conform to generally accepted accounting principles (GAAP) as applicable to proprietary funds of governments using the full accrual basis of accounting. 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 methods prescribed by the State Auditor under the authority of Chapter 43.09 RCW, the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission (FERC) for the Electric System and the Uniform System of Accounts for Class A & B Water Utilities prescribed by the National Association of Regulatory Utility Commissioners for the Water System.

GASB Statement No. 20 requires that the District apply all GASB pronouncements as well as the pronouncements issued on or before November 30, 1989 by the Financial Accounting Standard Board (FASB) and its predecessor organizations, unless those pronouncements conflict with or contradict GASB pronouncements. As provided for in GASB Statement No. 20, the District has elected not to implement FASB Statements and Interpretations issued after November 30, 1989.

**Cash equivalents** – The District considers all highly liquid investments (including restricted assets) with a maturity of three months or less to be cash equivalents. Assets in the Local Government Investment Pool (LGIP) that are for operating purposes are considered cash equivalents as they can be converted to cash within one day.

**Investments** – The District records investments at fair value based on quoted market rates, with changes in unrealized gains and losses reported as investment income (see Note 2). Restricted funds in the LGIP are considered investments.

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 1 – Organization and Significant Accounting Policies (continued)**

**Accounts receivable and allowance for uncollectible accounts** – Accounts receivable are recorded when invoices are issued and are written off when they are determined to be uncollectible. The allowance for uncollectible accounts includes amounts estimated through an evaluation of specific accounts, based on the best available facts and circumstances, of customers that may be unable to meet their financial obligations, and a reserve is recorded based on historical experience. The allowance for uncollectible accounts at December 31, 2011 and 2010 was \$33,538 and \$68,287, respectively.

**Other receivables** – Other receivables consists of amounts due from customers for small material purchases, certain aid in construction billings, repairs to damaged plant and equipment from accidents caused by others, funding requests to granting or loaning agencies, customers who take primary electric service from the District or have a power sales contract, and other miscellaneous items that may require invoicing that would not normally be entered into the customer service billing system.

**Materials and supplies** – Materials and supplies provide for additions, maintenance and repairs to utility plant and are stated at average cost.

**Restricted assets** – In accordance with bond resolutions and certain related agreements, separate restricted funds are required to be established. Cash and investments held in these funds are restricted for specific uses, including construction, debt service and other special reserve requirements.

**Capital assets (utility plant)** – Utility plant is stated at original cost, contract price or fair value if donated (see Note 3). Costs include labor, materials and related indirect costs, such as engineering, transportation and allowance for funds (i.e. interest) used during construction. Additions, renewals and betterments with a minimum cost of \$500 per item are capitalized. Repairs and minor replacements are charged to operating expenses. In the case of disposals, unless there is a major retirement or a general plant asset is retired, the cost of property and any removal cost less salvage are charged to accumulated depreciation when property is retired. Depreciation is computed using straight-line group rates; 3% for distribution plant, 2.75% for transmission plant, and 1.67% to 2.5% for generating plant. Depreciation of water and wastewater plant has been computed over useful lives of 25 to 40 years. General plant composite rates range from 2.2% to 14.4%.

**Unamortized debt expense and premium** – Bond issue costs are amortized to expense using the straight-line method over the term of the bonds. Bond premiums are amortized to interest expense, using the weighted average method over the term of the bonds.

**Other investments** – Consists of investment in White Creek Public LLC, carried on the equity basis of accounting.

**Transmission deposits** – Consists of deposits for certain transmission services paid to Bonneville Power Administration (BPA).

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 1 – Organization and Significant Accounting Policies (continued)**

**Unamortized prepaid power contract** – Consists of prepaid power amortized using the straight-line method over the term of the contract (see Note 4).

**Compensated absences** – Compensated absences are absences for which employees will be paid, such as vacation and sick leave. The District records compensated absences as an expense and liability when earned. Vacation pay and sick leave pay policies were superseded by a Personal Time Off (PTO) Policy in 2008. District employees are entitled to time off based upon length of continuous service which is payable upon resignation, retirement or death. There is a 700-hour cap on PTO accrual, determined according to the employees’ anniversary dates. After the annual transfer of PTO hours into Volunteer Employee Beneficiary Association (VEBA) or deferred comp, any hours over the 700-hour cap will be forfeited. At separation, if an employee is not eligible to retire, they may cash out their PTO bank at a schedule governed by years of service.

**Fair value of financial instruments** – The carrying amounts of current assets, including restricted cash and investments, and current liabilities approximate fair value due to the short-term maturity of those instruments. The fair value of the District’s investments and debt are estimated based on the quoted market prices for the same or similar issues.

**Net assets** – Net assets consist of:

- **Invested in capital assets, net of related debt** – This component of net assets consists of capital assets, net of accumulated depreciation, and unspent bond proceeds less outstanding balances of any bonds and other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- **Restricted** – This component consists of net assets on which constraints are placed as to their use. Constraints include those imposed by creditors (such as through debt covenants), contributors, or laws or regulation of other governments or constraints imposed by law through constitutional provisions or through enabling legislation.
- **Unrestricted** – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

**Revenues and expenses** – Operating revenues and expenses result from providing services and producing and delivering goods in connection with the District’s principal ongoing operations. Operating revenues are recognized when billed and expenses are recognized when incurred. In addition, the District recognizes unbilled revenue, revenues from services provided, but not yet billed. The principal operating revenues of the District are charges to customers for electric, water and wastewater service. Operating expenses for the District include the cost of sales and services, maintenance, administrative expenses, depreciation on capital assets and taxes. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 1 – Organization and Significant Accounting Policies (continued)**

The credit practices of the District require an evaluation of each new customer’s credit worthiness on a case-by-case basis. Based on policy, a deposit may be obtained from the customer. Concentrations of credit risk with respect to receivables for residential customers are limited due to the number of customers comprising the District’s customer base. Credit losses have been within management’s expectations. Similar to its evaluation of residential, commercial and industrial customers’ credit reviews, the District continually evaluates its wholesale power customers by reviewing credit ratings and financial credit worthiness of existing and new customers.

**Capital contributions** – Capital contributions are District-mandated customer connection charges used to fund construction of system properties necessary to extend service to a new customer.

**Use of estimates** – The preparation of combined financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the combined financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Significant risks and uncertainties** – The District is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include, but are not limited to, weather and natural disaster related disruptions; collective bargaining labor disputes; fish and other Endangered Species Act issues; Environmental Protection Agency regulations; federal government regulations or orders; deregulation of the electric industry; and market risks inherent in the buying and selling of power, a commodity with inelastic demand characteristics and minimal storage capability.

**Reclassifications** – Changes have been made to prior year account classifications as needed to conform to the current year presentation format. The primary change is in the classification of capital assets.

**Note 2 – Deposits and Investments**

Cash and investments consist of the following at December 31:

	Restricted Cash Equivalents	Unrestricted Cash and Cash Equivalents	Total 2011	Total 2010
Construction funds	\$ 7,147,975	\$ -	\$ 7,147,975	\$ 3,846,789
Special funds	15,454,649	-	15,454,649	14,307,309
Cash – general funds	-	9,952,816	9,952,816	12,639,161
Special deposits	400	-	400	400
Totals	<u>\$ 22,603,024</u>	<u>\$ 9,952,816</u>	<u>\$ 32,555,840</u>	<u>\$ 30,793,659</u>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 2 – Deposits and Investments (continued)**

**Interest rate risk** – The District’s investment policy limits investment maturities to less than five years from the date of purchase unless authorized by the General Manager and Finance Manager for a specific purpose. During 2011 and 2010 all investments were in the State Treasurer’s LGIP, which has a weighted average portfolio maturity of less than 90 days.

**Credit risk** – In accordance with the Revised Code of Washington, District bond resolutions and District internal investment policies, all investments are direct obligations of the U.S. Government, deposits in the LGIP, or deposits with financial institutions recognized as qualified public depositories of the State of Washington. The District’s cash deposits are covered by federal depository insurance or protected against loss by deposit with financial institutions recognized as qualified public depositories of the State of Washington. The District intends to hold deposits and securities until maturity.

**Concentration of credit risk** – District policies allow the entire portfolio to be invested in direct United States Government guaranteed obligations or in the LGIP. No other investment may exceed half of portfolio market value. The LGIP, a 2a7-like pool as defined by GASB Statement No. 31 and the Securities and Exchange Commission, invests in high quality, short term investments; all LGIP money market securities must be rated A-1 by Standard & Poor’s Corporation or P1 by Moody’s Investor Services, Inc. The LGIP weighted average maturity must not exceed 90 days and no single investment may exceed 762 days in maturity. Withdrawals in excess of \$10 million are available on a one day notice. The LGIP Annual Report is available on the Washington State Treasurer’s website.



**PUBLIC UTILITY DISTRICT NO. 1 OF KCLICKITAT COUNTY –  
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NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 3 – Capital Assets (Utility Plant)**

The following are changes in capital assets for the year ended December 31, 2011:

Description	Balance 01/01/2011	Additions	Retirements and Transfers	Balance 12/31/2011
Capital assets not being depreciated				
Organization	\$ 14,767	\$ -	\$ -	\$ 14,767
Franchises and consents	211,427	-	-	211,427
Land and land rights	1,409,916	46,437	-	1,456,353
Construction work in progress	<u>70,647,675</u>	<u>11,502,289</u>	<u>56,903,189</u>	<u>25,246,775</u>
	<u>72,283,785</u>	<u>11,548,726</u>	<u>56,903,189</u>	<u>26,929,322</u>
Capital assets being depreciated				
Electric plant				
Distribution plant	99,874,817	3,701,053	452,358	103,123,512
Transmission plant	52,180,211	818,836	145,547	52,853,500
Generating plant	24,311,271	51,912,396	-	76,223,667
Water and wastewater plant	18,544,008	219,708	3,395	18,760,321
General plant	<u>9,564,214</u>	<u>337,629</u>	<u>1,853</u>	<u>9,899,990</u>
	<u>204,474,521</u>	<u>56,989,622</u>	<u>603,153</u>	<u>260,860,990</u>
Total capital assets	276,758,306	68,538,348	57,506,342	287,790,312
Accumulated depreciation	<u>(54,165,688)</u>	<u>(6,716,914)</u>	<u>603,798</u>	<u>(60,278,804)</u>
Net capital assets	<u>\$ 222,592,618</u>	<u>\$ 61,821,434</u>	<u>\$ 56,902,544</u>	<u>\$ 227,511,508</u>

**Note 4 – Deferred Debits**

Deferred debits consist of the following:

	2011	2010
Prepaid power contract, net of current portion	\$ 17,705,400	\$ 18,885,756
Unamortized debt issuance expense	3,184,421	3,343,919
Preliminary investigation charges	<u>576,205</u>	<u>366,118</u>
	<u>\$ 21,466,026</u>	<u>\$ 22,595,793</u>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 4 – Deferred Debits (continued)**

**Prepaid power contract** – The District entered into a 20-year Energy Purchase Agreement for the White Creek Wind I Facility, which became effective January 1, 2008. Under this Agreement, the District had rights to 26% of the output from the 205 MW facility and was obligated to pay the same percentage of the reimbursable operating expenses. In June 2008, the District completed a transaction with Lewis PUD to sell 10% of the 26% share of the White Creek Wind I project power output. In December 2008, the District also sold 3% of the remaining 16% share of the White Creek Wind I project power output to Benton PUD. The gain on the sale of White Creek power rights was \$23,678,404. The remaining portion of the project is amortized on a straight-line basis over the remaining term of the contract.

**Note 5 – Long-Term Debt**

The following are changes in long-term debt for the year ended December 31, 2011:

	Balance 01/01/2011	Additions	Payments/ Amortization	Balance 12/31/2011	Due Within One Year
Electric revenue bonds	\$ 128,805,000	\$ 13,610,000	\$ 3,180,000	\$ 139,235,000	\$ 3,240,000
Unamortized bond premium	2,601,994	-	198,212	2,403,782	
W/WW revenue bonds	257,500	-	30,000	227,500	32,000
W/WW loans	1,747,919	401,589	182,010	1,967,498	160,579
Total long-term debt	<u>\$ 133,412,413</u>	<u>\$ 14,011,589</u>	<u>\$ 3,590,222</u>	<u>\$ 143,833,780</u>	<u>\$ 3,432,579</u>

Substantially all electric revenues are pledged as security for the electric revenue bonds and substantially all water/wastewater revenues are pledged as security for the water/wastewater revenue bonds. Water/wastewater loans are secured by water/wastewater assets. Electric revenue bonds carry fixed and variable interest rates ranging from 2.030% to 6.680% and 1.470% to 7.038%, respectively, for the years ended December 31, 2011 and 2010. The water/wastewater revenue bonds have a 5.0% fixed rate. The loans from the Public Work Trust Fund (PWTF) carry fixed rates from 0.0% to 3.0% and the State Revolving Fund (SRF) loans have fixed rates of 0.0% to 1.0%. Electric revenue bonds mature through December 1, 2031, water/wastewater bonds mature through September 1, 2021 and the PWTF and SRF loans mature through October 1, 2028. There is \$19,915,000 in restricted assets of the District representing revenue bond reserve requirements, construction funds and debt service accounts for the various indentures. There are a number of other limitations and restrictions contained in the various bond indentures.

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
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NOTES TO COMBINED FINANCIAL STATEMENTS**

**Note 5 – Long-Term Debt (continued)**

Future maturities are as follows:

Electric Revenue Bonds			
Year(s)	Principal	Interest	Totals
2012	\$ 3,240,000	\$ 7,328,196	\$ 10,568,196
2013	3,325,000	7,254,090	10,579,090
2014	3,430,000	7,148,389	10,578,389
2015	3,565,000	7,017,534	10,582,534
2016	3,710,000	6,869,052	10,579,052
2017-21	32,380,000	30,393,703	62,773,703
2022-26	45,925,000	20,266,912	66,191,912
2027-31	43,660,000	7,977,468	51,637,468
	<u>\$ 139,235,000</u>	<u>\$ 94,255,344</u>	<u>\$ 233,490,344</u>

Water/Wastewater Revenue Bonds			
Year(s)	Principal	Interest	Totals
2012	\$ 32,000	\$ 11,325	\$ 43,325
2013	23,000	9,775	32,775
2014	23,000	8,625	31,625
2015	26,000	7,475	33,475
2016	121,500	16,375	137,875
2021	2,000	100	2,100
	<u>\$ 227,500</u>	<u>\$ 53,675</u>	<u>\$ 281,175</u>

Water/Wastewater PWTf & SRF Loans			
Year(s)	Principal	Interest	Totals
2012	\$ 160,579	\$ 6,561	\$ 167,140
2013	160,579	6,200	166,779
2014	160,579	5,795	166,374
2015	160,579	5,390	165,969
2016	160,579	4,985	165,564
2017-21	578,330	18,853	597,183
2022-26	500,228	9,008	509,236
2027-28	86,045	1,075	87,120
	<u>\$ 1,967,498</u>	<u>\$ 57,867</u>	<u>\$ 2,025,365</u>
Total	<u>\$ 141,429,998</u>	<u>\$ 94,366,886</u>	<u>\$ 235,796,884</u>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 5 – Long-Term Debt (continued)**

The carrying amounts of the Bonds and P WTF and SRF loans approximate the fair value since such loans are exclusive and have no market.

At December 31, 2011, the District’s 2001 Electric Revenue Bonds in the amount of \$24,955,000 were considered defeased. This refunded bond constitutes a contingent liability of the District only to the extent that cash and investments presently in the control of the refunding trustees are not sufficient to meet debt service requirements, and are therefore excluded from the combined financial statements because the likelihood of additional funding requirements is considered remote.

**Note 6 – Short-Term Debt**

The District issued a bond anticipation note on November 5, 2007 in the amount of \$47,000,000 to finance the District’s 26% of the power output from the White Creek Wind I project for the term of 20 years per the agreement. This note was in two sections, a \$42,000,000 and a \$5,000,000 section. Proceeds from the sale of 13% of the District’s 26% share of power output from White Creek Wind project was used to pay off the first \$42,000,000 section of the bond anticipation note. The remaining balance of \$5,000,000 was paid off during the year ended December 31, 2011.

**Note 7 – Retirement Benefits**

**1. Pension plan**

Substantially all of the District’s full-time and qualifying part-time employees participate in one of the statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer public employee defined benefit and defined contribution retirement plans. The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan.

The DRS CAFR may be obtained by writing to: Department of Retirement Systems, Communications Unit – PO Box 48380 – Olympia WA 98504-8380. The following disclosures are made pursuant to GASB Statement 27, Accounting for Pensions by State and Local Government Employers.

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

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

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
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NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 7 – Retirement Benefits (continued)**

Membership in the system includes elected officials; state employees; employees of the Supreme, Appeals and Superior courts (other than judges 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 government.

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

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

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

Plan 2 members are vested after the completion of five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of two percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60 month period. Plan 2 retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a three percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit; and a cost of living allowance is granted (indexed to the Seattle Consumer Price Index), capped at three percent annually.

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 7 – Retirement Benefits (continued)**

Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit portion provides a benefit calculated at one percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60 month period. Effective June 7, 2007, Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service, if twelve months of that service are earned after age 44; or after five service credit years earned in PERS Plan 2 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 to retire with full benefits at age 65, or at age 55 with 10 years of service. Retirements prior to age 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a three percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit and Plan 3 provides the same cost of living allowance as Plan 2.

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

There are 1,197 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of June 30, 2010:

Retirees and beneficiaries receiving benefits	76,899
Terminated plan members entitled to but not yet receiving benefits	28,860
Active plan members vested	105,521
Active plan members non-vested	<u>51,005</u>
Total	<u><u>262,285</u></u>

**PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY –  
MCAG No. 1785  
NOTES TO COMBINED FINANCIAL STATEMENTS**

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**Note 7 – Retirement Benefits (continued)**

**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 PERS Plan 1 are established by statute at 6 percent for state agencies and local government unit employees, and at 7.5 percent for state government elected officials. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefits portion for 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 Employee Retirement Benefits Board sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee’s age. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of current year covered payroll, as of December 31, 2011, were as follows:

	<u>PERS Plan 1</u>	<u>PERS Plan 2</u>	<u>PERS Plan 3</u>
Employer*	7.25%**	7.25%**	7.25%***
Employee	6.00%****	4.64%****	****

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

\*\* The employer rate for state elected officials is 10.80% for Plan 1, 7.25% for Plan 2 and Plan 3.

\*\*\* Plan 3 defined benefit portion only.

\*\*\*\* The employee rate for state elected officials is 7.50% for Plan 1, and 4.64% for Plan 2.

\*\*\*\*\* Variable from 5% to 15% maximum based on rate selected by the PERS3 member.

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

	<u>PERS Plan 1</u>	<u>PERS Plan 2</u>	<u>PERS Plan 3</u>
2011	\$ 9,522	\$ 655,744	\$ 35,680
2010	8,678	537,268	34,399
2009	20,312	589,365	33,197

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**Note 7 – Retirement Benefits (continued)**

**2. Post employment benefits plan other than pensions**

**Plan description** – In addition to pension benefits, the District provides post employment health care benefits. District members are eligible for retiree medical benefits after becoming eligible for service retirement pension benefits under Plan 2 of the PERS (age 65 with 5 years of service; age 55 with 20 years of service). Currently former members who are entitled to a deferred vested pension benefit are not eligible to receive medical benefits after pension benefit commencement. Survivors of members who die are not eligible for medical benefits.

**Funding policy** – The funding policy is based upon the pay-as-you-go financing requirements.

**Annual OPEB cost and net OPEB obligation** – The District’s annual other postemployment benefit (OPEB) cost is based upon the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities over a period of thirty years as of January 1, 2008.

The District’s annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for years ended December 31 were as follows:

<u>Fiscal Year Ended</u>	<u>Annual OPEB Cost</u>	<u>Percentage of OPEB Cost Contributed</u>	<u>Net OPEB Obligation</u>
12/31/2011	\$ 413,320	43.30%	\$ 958,177
12/31/2010	413,230	43.30%	723,886
12/31/2009	410,566	39.58%	489,595

**Funding status and funding progress** – As of January 1, 2008, the most recent valuation date, the plan was 0% funded. The accrued liability for benefits was \$4.8 million, and the actuarial value of assets was \$0, resulting in a UAAL of \$4.8 million.

The following table presents a schedule of funding progress for the District’s OPEB Plan:

<u>Valuation Date</u>	<u>Actuarial Value of Assets</u>	<u>Accrual Accrued Liability</u>	<u>Unfunded Actuarial Accrued Liabilities (UAAL)</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>UAAL as a Percentage of Covered Payroll</u>
1/1/2008	\$ -	\$ 4,784,699	\$ 4,784,699	0%	N/A	N/A



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**Note 7 – Retirement Benefits (continued)**

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

**Note 8 – Segment Information – Enterprise Funds**

The District operates an electric, eight water, and five wastewater utilities which are primarily financed by user charges. The key financial data for the years ended December 31, 2011 and 2010 is as follows:

Condensed balance sheets:

	Electric System	Water- Wastewater Systems	Total 2011	Total 2010
<b>Assets</b>				
Current, restricted and other assets	\$ 61,723,160	\$ 3,578,126	\$ 65,301,286	\$ 65,613,629
Capital assets	211,132,026	16,379,482	227,511,508	222,592,618
<b>Total assets</b>	<b>\$ 272,855,186</b>	<b>\$ 19,957,608</b>	<b>\$ 292,812,794</b>	<b>\$ 288,206,247</b>
<b>Liabilities</b>				
Current liabilities	\$ 11,295,978	\$ 1,095,002	\$ 12,390,980	\$ 18,654,715
Noncurrent liabilities	137,759,699	2,831,936	140,591,635	130,292,057
<b>Total liabilities</b>	<b>149,055,677</b>	<b>3,926,938</b>	<b>152,982,615</b>	<b>148,946,772</b>
<b>Net assets</b>				
Invested in capital assets, net of related debt	80,849,871	13,367,773	94,217,644	91,370,913
Restricted	14,895,689	(4,979)	14,890,710	13,728,023
Unrestricted	28,053,951	2,667,874	30,721,825	34,160,539
<b>Total net assets</b>	<b>123,799,511</b>	<b>16,030,668</b>	<b>139,830,179</b>	<b>139,259,475</b>
<b>Total liabilities and net assets</b>	<b>\$ 272,855,188</b>	<b>\$ 19,957,606</b>	<b>\$ 292,812,794</b>	<b>\$ 288,206,247</b>

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**Note 8 – Segment Information – Enterprise Funds (continued)**

Condensed statements of revenues, expenses and changes in net assets:

	Electric System	Water- Wastewater Systems	Total 2011	Total 2010
Operating revenues	\$ 32,239,253	\$ 1,396,608	\$ 33,635,861	\$ 34,983,822
Operating expenses	24,858,347	926,413	25,784,760	25,328,819
Depreciation	6,108,659	534,156	6,642,815	4,456,412
Operating income	1,272,247	(63,961)	1,208,286	5,198,591
Non-operating revenues (expenses)				
Interest income	149,760	33,737	183,497	170,437
Interest expense	(2,887,079)	(41,775)	(2,928,854)	(4,928,234)
Other non-operating revenue (expense), net	1,104,063	26,612	1,130,675	1,259,646
Capital contributions and grants	947,114	29,986	977,100	20,567,310
Change in net assets	586,105	(15,401)	570,704	22,267,750
Net assets, beginning of year	123,331,176	15,928,299	139,259,475	116,991,725
Net assets, end of year	\$ 123,917,281	\$ 15,912,898	\$ 139,830,179	\$ 139,259,475

**Note 9 – Risk Management and Self Insurance**

**Unemployment insurance** – The District maintains insurance against most normal hazards, except for unemployment insurance, where the District has elected to become self-insured for all losses. The District reimburses the State Employment Security Department for actual costs upon receipt of any claim. The District does not estimate any future liability as the amount is not significant.

**Public utility risk management services** – The District, along with seventeen other public utility districts and one joint operating agency, is a member of the Public Utility Risk Management Services self-insurance fund. The program provides members with various liability, property and health insurance coverage in three separate pools.

The District has not accrued a liability for any outstanding claims of the self-insured pools, including incurred-but-not-reported health and welfare claims, as the amount cannot be reasonably estimated. Management believes the claims, for those that are successful, will not have a significant impact on the financial position of the District.

The District is a participant in the liability pool, which maintains a base self-insured retention level of \$1,000,000, funded reserves ranging from \$1,500,000 to \$2,000,000, and individual member deductibles of \$250. The liability pool provides the District with shared excess coverage of \$60,000,000 general liability, \$10,000,000 professional liability, and \$10,000,000 per occurrence Directors and Officers liability.

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**Note 9 – Risk Management and Self Insurance (continued)**

The District is also a participant in the property pool, which maintains a self-insured retention level of \$250,000, funded reserves ranging from \$500,000 to \$750,000, and varying deductibles of \$250 on most property and \$75,000 on the H. W. Hill Landfill Gas project. The property pool provides the District with \$175,000,000 shared excess coverage, attaching at the self-insured retention level for all property risks excepting flood and earthquake, which attach at 2% of total insured value. Any gap between the self-insured level and excess insurance is funded half by the property pool and half by the affected member.

The District also participates in the health and welfare pool. Participating members are billed each month for shared costs (administration costs to operate the pool, mail order prescription plan costs, and stop loss carrier costs), claims by the members covered employees and dependents, and any shared claims for members who exceeded stop loss limits.

**Note 10 – Joint Ventures**

**Conservation and Renewable Energy System (CARES)** – The District, along with seven other public utility districts, is a member of CARES, a municipal corporation and joint operating agency of the State of Washington. CARES was formed pursuant to RCW Chapter 43.52. The purpose of CARES is to develop and acquire conservation, renewable and high efficiency resources consistent with the Northwest Conservation and Electric Power Plan. CARES issued Conservation Project Revenue Bonds which are tax-exempt and unconditionally guaranteed by the BPA. The District has not contributed any money to CARES for several years. The District has no equity interest or liability for CARES operations.

**McNary North Fishway Hydroelectric Project** – On August 14, 1995, the District and Northern Wasco County PUD entered into an Ownership Agreement to jointly construct and operate the McNary North Fishway Hydroelectric Project. The project was completed in September 1997 and is generating approximately ten megawatts (10 MW) of electricity. Both the District and Northern Wasco County PUD share equally in the output, as well as the construction and operation costs of the Project. In 2011 and 2010 the District contributed \$450,000.

**Last Mile Electrical Cooperative (LMEC)** – The District, along with seven other public utility districts and two other organizations, is a member of LMEC, a non-profit cooperative. LMEC was formed pursuant to RCW Chapter 24.06. The purpose of LMEC is to develop wind and other renewable energy projects. At this time, LMEC has not issued any debt and is solely funded by its members. The District has no equity interest or liability for the LMEC operations at this time.

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**Note 10 – Joint Ventures (continued)**

**White Creek Public, LLC & White Creek Project, LLC** – The District, along with Cowlitz PUD, formed White Creek Public, LLC to participate in White Creek Project, LLC which also includes as members Tanner Electric Co-op and Lakeview Light & Power. Early development of the project was done by the utilities involved, but prior to the end of 2007 the project was sold to Prudential and Lehman Brothers. Energy purchase agreements were signed by the utilities for 20 years of power that began commercial operation on November 21, 2007 (see Note 4). The percentage owned by each utility was determined based upon their contribution made during the original development stage. Phases 1 and 2 of White Creek Wind I have a total of 89 2.3 MW wind turbines for an anticipated output of 205 MW. Both phases were in production as of November 21, 2007. In 2011 and 2010, the District's investment in the project of \$(14,988) consisted of a share of the remaining assets. These amounts have been shown on the balance sheet as other investments and transmission deposits.

**Note 11 – Contingencies**

**Lawsuits** – The District is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, it is the opinion of District management that resolution of these matters will not have a material adverse effect on the financial condition of the District.

**Construction financing** – On April 17, 2001 the District entered into a thirty (30) year agreement with the Goldendale Energy, Inc. in order to provide for the transmission of the electric energy to be produced at Goldendale Energy Inc. generating facility from the E.E. Clouse Substation to Bonneville's Harvalum Substation. The generating facility was sold through bankruptcy auction in February 2007 to Puget Sound Energy. The District established a new letter of credit for the transmission line service, which the District built and operates for the generation facility. The letter of credit covers the net present value of the remaining contract amount including the debt outstanding.

The District established a new letter of credit on August 16, 2006 for the White Creek transmission line service, which the District built and operates at a cost of \$17.7 million, for the generation facility. The letter of credit covers the net present value of the remaining 20 year contract amount including the debt outstanding.

**Grants** – Grants received by the District are subject to audit by the granting agency and may result in certain costs being disallowed and required to be returned. Management believes it has complied with grant guidelines and the likelihood of disallowed costs is remote.

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**Note 12 – Power Contracts**

The District purchased power from BPA under a partial requirement contract which expired on September 30, 2011. Under this contract the District served a portion of customer load with existing generation from the McNary Fishway Project, approximately 5 MW. The balance of the District's load requirement is supplied by BPA at the public preference customer rate.

Effective October 1, 2011, the District entered into a Slice/Block Agreement with the BPA. The provisions of this agreement establishes the terms under which the District is committed to purchase its power for a period of seventeen years. The Slice/Block Agreement specifies that BPA rates are variable and includes provisions for various adjustments depending on actual load and BPA costs. In addition, the Slice portion of the agreement includes a true-up provision that allows BPA to recover Slice costs not previously recovered during the fiscal year. BPA assesses this true up on an annual basis. The true up is paid, or refunded if a credit, during the next fiscal year.

The Slice portion of the agreement commits the District to purchase a certain fixed percentage of BPA generation which varies depending on the available water and may result in power that is surplus to the District's needs and which the District intends to sell on the open market. The Block portion of the agreement specifies a specific amount of MWs BPA will supply to the district. This amount is adjusted per the contract on a yearly basis.

The White Creek Wind I facility energy purchase agreement for 13% of the 205 MW project was sold under contract to other utilities through March 2011. The output for the remainder of the year went to market. (see Note 4).

**Note 13 – Generation Assets**

H. W. Hill Landfill Gas project is rated a 10.5 MW plant that takes methane gas from the regional landfill and produces electricity from five 2.1 MW reciprocating combustion engines. 2.0 MW's of the output from this project is sold to a public utility and the balance sold on the spot market.

McNary Dam Hydroelectric project is a 10 MW plant that the District shares joint ownership with Northern Wasco Peoples Utility District in The Dalles, Oregon. The facility is located on the north shore fish bypass area of McNary Dam and received a 50-year license on September 30, 1991. Of the 5 MW's the District receives, 4.5 MW's are declared to load.

**Note 14 – Union Contracts**

The District has a contract with the International Brotherhood of Electrical Workers which covers the electrical line workers employed by the District. The District signed a new contract with the union which was executed beginning June 1, 2011 for a three year period.