



Report of Independent Auditors  
and Financial Statements with  
Supplementary Information for  
  
Public Utility District No. 1 of  
Okanogan County, Washington  
  
December 31, 2013 and 2012

**MOSS ADAMS** LLP

Certified Public Accountants | Business Consultants

*Acumen. Agility. Answers.*

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## REPORT OF INDEPENDENT AUDITORS

To the Commissioners  
Public Utility District No. 1  
of Okanogan County, Washington

### **Report on Financial Statements**

We have audited the accompanying financial statements of Public Utility District No. 1 of Okanogan County, Washington (the District), which comprise the statements of net position as of December 31, 2013 and 2012, and the related statements of revenues, expenses, and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of December 31, 2013 and 2012, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Other Matters***

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the accompanying management's discussion and analysis on pages 4 through 8 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.

#### *Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements. The schedule of expenditures of federal awards as required by Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and the unaudited supplementary information are presented for purposes of additional analysis and are not a required part of the financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the financial statements as a whole.

The unaudited supplementary information presented on pages 37 through 39 has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

***Other Reporting Matters Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated May 12, 2014, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

A handwritten signature in blue ink that reads "Mess Adams HP". The signature is written in a cursive, somewhat stylized font.

Everett, Washington

May 12, 2014

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

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

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The following discussion and analysis is designed to assist the reader in focusing on the significant financial issues, provide an overview of Public Utility District No. 1 of Okanogan County (the District) financial activity, and identify changes in the District's financial position during 2013 and 2012. Please consider the information presented here in conjunction with the financial statements as a whole, including the footnotes and other supplementary information that is provided.

The District, a municipal corporation of the state of Washington, was established in 1936 and began operations in 1945. The District is governed by a three-member board of commissioners locally elected to six-year terms. The District operates both electric and telecommunications systems that are accounted for in a single proprietary fund.

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

The financial statements include the management's discussion and analysis and financial statements with accompanying notes. In accordance with standards issued by the Governmental Accounting Standards Board (GASB), the District's financial statements are presented on an accrual basis of accounting, which recognizes revenues when earned and expenses when incurred, regardless of when cash is received or paid.

The financial statements are presented as of and for the years ended December 31, 2013 and 2012, and consist of:

**Statements of net position** - The statements of net position present information on the District's assets, deferred outflows of resources, liabilities, and net position at year-end. These statements also provide information about the nature and amounts of investments in resources (assets) and the District's obligations to its creditors (liabilities).

**Statements of revenues, expenses, and changes in net position** - The statements of revenues, expenses, and changes in net position account for the year's revenue and expense transactions. These statements measure the District's operations over the past year and may be used to determine whether the District has been successful in recovering its costs through rates and other charges.

**Statements of cash flows** - The statements of cash flows provide information on the District's cash receipts and disbursements during the year. The statements report changes in cash resulting from operations, investing, and capital and related financing activities.

The notes to the financial statements provide additional information that is an integral part of the financial statements. This information includes the disclosure of significant accounting policies, financial activities, risks, commitments, and obligations.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON  
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

**Selected Financial Information**

	December 31,		
	2013	2012	2011
<b>ASSETS</b>			
Current and other assets	\$ 32,492,823	\$ 31,602,964	\$ 35,993,121
Net utility plant	106,028,834	97,967,535	92,263,566
<b>Total assets</b>	<b>138,521,657</b>	<b>129,570,499</b>	<b>128,256,687</b>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>			
	620,315	695,260	770,206
<b>Total assets and deferred outflows of resources</b>	<b>\$ 139,141,972</b>	<b>\$ 130,265,759</b>	<b>\$ 129,026,893</b>
<b>LIABILITIES</b>			
Current liabilities	\$ 9,416,638	\$ 8,175,967	\$ 8,088,669
Long-term debt	38,176,983	38,180,543	38,726,154
<b>Total liabilities</b>	<b>47,593,621</b>	<b>46,356,510</b>	<b>46,814,823</b>
<b>NET POSITION</b>			
Net investment in capital assets	66,827,166	66,518,757	60,460,089
Restricted	8,141,401	8,327,470	8,450,023
Unrestricted	16,579,784	9,063,022	13,301,958
<b>Total net position</b>	<b>91,548,351</b>	<b>83,909,249</b>	<b>82,212,070</b>
<b>Total liabilities and net position</b>	<b>\$ 139,141,972</b>	<b>\$ 130,265,759</b>	<b>\$ 129,026,893</b>
<b>Years Ended December 31,</b>			
	2013	2012	2011
<b>REVENUE</b>			
<b>Operating</b>			
Electric - retail	\$ 39,861,279	\$ 35,588,404	\$ 33,355,835
Electric - wholesale	5,132,270	3,531,677	6,741,527
Telecommunications	2,217,116	2,096,256	1,955,276
Other operating revenue	1,286,159	1,412,834	1,041,958
<b>Total operating income</b>	<b>48,496,824</b>	<b>42,629,171</b>	<b>43,094,596</b>
<b>Nonoperating</b>			
Interest income, net	58,695	74,313	113,944
Other nonoperating income	3,065,848	2,065,233	1,019,149
Contributed capital	990,165	991,816	974,691
<b>Total nonoperating income</b>	<b>4,114,708</b>	<b>3,131,362</b>	<b>2,107,784</b>
<b>Total revenue</b>	<b>52,611,532</b>	<b>45,760,533</b>	<b>45,202,380</b>

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

**Selected Financial Information (continued)**

	Years Ended December 31,		
	2013	2012	2011
EXPENSES			
Operating			
Cost of power	23,534,220	23,198,810	24,860,599
Taxes	2,413,881	2,220,161	2,138,550
Depreciation	4,584,884	4,601,137	4,258,323
Other operating expenses	12,736,964	12,656,728	11,172,318
Total operating expenses	<u>43,269,949</u>	<u>42,676,836</u>	<u>42,429,790</u>
Nonoperating			
Interest expense	1,555,826	1,386,518	1,407,221
Other expense	146,655	-	726,596
Total nonoperating	<u>1,702,481</u>	<u>1,386,518</u>	<u>2,133,817</u>
Total expenses	<u>44,972,430</u>	<u>44,063,354</u>	<u>44,563,607</u>
CHANGE IN NET POSITION	7,639,102	1,697,179	638,773
NET POSITION, beginning of period	<u>83,909,249</u>	<u>82,212,070</u>	<u>81,573,297</u>
NET POSITION, end of period	<u>\$ 91,548,351</u>	<u>\$ 83,909,249</u>	<u>\$ 82,212,070</u>

**Financial Highlights**

During 2013, the District's overall financial position remained strong due in part to a 1.9% increase in retail load. Part of the increase in retail sales was due to one of the District's largest customers coming back on line October 1, 2013. In addition, the District increased retail rates an average of 9.5% on September 1, 2013. The rate adjustment came at the conclusion of the District preparing an updated equity management plan and conducting a cost of service study. Market prices for wholesale energy sales increased by 101%, which also improved the District's financial position. The District's net position increased \$7,639,102 compared with an increase in net position in 2012 of \$1,697,179.

The following is an analysis of key financial factors with an emphasis on changes between 2013 and 2012:

**Cash and investments** - The District had cash and investments totaling \$22,943,554, \$22,051,035, and \$27,469,235 as of December 31, 2013, 2012, and 2011, respectively. The increase of \$892,519 in 2013 is less than expected given the significant change in net position due to continued financial demands of the District's capital outlays. As noted in Note 1 to the financial statements, investments in the amount of \$10,368,838 are considered restricted as of December 31, 2013. The funds are restricted as follows: \$289,338 for debt service payments, \$1,944,500 for bond reserve requirements, \$2,000,000 for customer deposits and compensated absences, and the remaining \$6,135,000 is restricted in a rate stabilization fund.

# **PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

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## **Financial Highlights (continued)**

**Utility plant** - Net utility plant increased by \$8,061,299, or 8.2%, during 2013, compared with an increase of \$5,703,969, or 6.2%, during 2012. A summary of utility plant in service is included in Note 3 to the financial statements.

**Long-term debt** - As of December 31, 2013, the District had \$36,440,000 in revenue bonds outstanding, compared with \$38,040,000 as of December 31, 2012. During 2013, the District did not issue additional revenue bonds. The decrease in revenue bonds outstanding was a result of scheduled debt payments made during 2013.

In addition, in 2010, the District authorized a not-to-exceed \$3,667,855 loan with the United States Department of Agriculture (USDA) for broadband improvements (the RUS Note) related to the American Recovery and Reinvestment Act (ARRA) award. As of December 31, 2013, the RUS Note had a balance outstanding in the amount of \$3,043,705.

**Net operating revenues (expenses)** - The District recorded revenues from operations of \$48,496,824, which were \$5,226,875 more than operating expenses of \$43,269,949 in 2013, in comparison with 2012, when operating expenses exceeded operating revenues by \$47,665.

**Operating revenue** - Revenues from the retail sale of electricity increased by 12.0%, from \$35,588,404 in 2012 to \$39,861,279 in 2013, compared with an increase in retail sales in 2012 of 6.7%. This increase was anticipated during 2013 due to a retail rate increase of 9.5% on September 1, 2013. In addition, retail revenue also increased due to a 1.9% increase in load. During 2013, revenue from wholesale sales of electricity increased 45.3%, to \$5,132,270 from \$3,531,677, as reported in 2012. The increase in wholesale sales of electricity was the result of an over 100% increase in the average market price offset in part by 27.8% less electricity to sell in the wholesale market than 2012. Wholesale telecommunications revenue growth of 5.8% pushed revenue to \$2,217,116 in 2013, compared with \$2,096,256 in 2012.

**Operating expenses** - Operating expenses increased by \$593,113, or 1.4%, from \$42,676,836 in 2012 to \$43,269,949 in 2013. The moderate increase of operating expenses is comparable to a slightly lower increase in 2012 of 0.6% over 2011's expenses. The low annual increase in operating costs reflects the District's ongoing efforts to maintain minimal increases in costs over the previous year.

**Rates** - During 2013, the District implemented a rate increase effective September 1. The increase, in the amount of 9.5%, is expected to bring in an additional \$3,500,000 annually. The 2013 increase came at the completion of an updated equity management plan and cost of service study. The study included working with a group of rate payers from communities throughout the District. During 2012, the District also had a rate increase that was effective July 1 in the amount of 6.5%; this increase was the last in a series of three similar increases. The District also passes through increased power costs to its customers using a COPA (cost of power adjustment), currently .40¢/kWh. The COPA was increased by .16¢/kWh during 2013. The most recent rate increases were approved during 2013 after extensive studies were performed by SAIC Energy, Environment & Infrastructure, LLC, with assistance from District staff.

# **PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

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## **Significant Capital Assets and Long-Term Debt**

The District anticipates issuing new debt in the future to finance projects as discussed in the following paragraphs:

During 2013, the District made the decision to use the remaining 2010 bond construction funds, in the amount of \$7,266,304, to fund other capital projects. These funds were originally earmarked to construct an approximately 26-mile transmission line to serve the Methow Valley. The project has been held up as the District tries to obtain right-of-way across land owned by the state of Washington. The District expects to fund the transmission line through existing rates and reserves, and not issue additional bonds for this project.

The District continues to invest in wholesale telecommunications infrastructure. As of December 31, 2013, the District has invested a total of \$12,092,320 in wholesale telecommunications, which is an increase of \$4,030,833 over year-end 2012. The majority of the increase is due to capital outlays for the District's ARRA broadband project. The District's telecommunications network is connected to the Northwest Open Access Network, a fiber-optic system that is member owned. The network is currently utilized by 7 retail service providers, supporting almost 1,900 end-user customers.

During 2010, the District submitted for and was awarded ARRA funding to deploy a middle-mile and last-mile broadband communication system throughout the county. ARRA funding consisted of a \$5,501,782 grant and a \$3,667,855 loan. The proposed last-mile project will bring high-speed broadband to more than 6,543 premises that currently lack such access. The proposed funded network design calls for placement of approximately 170 access nodes and extends the fiber backbone approximately 179 miles to provide necessary redundancy to the last-mile network. By year-end, the construction phase was near completion and all that remains is the closeout of the project.

The District is the current owner of the Enloe Hydroelectric Dam, a small hydroelectric project on the Similkameen River near Oroville, Washington. On July 9, 2013, the Federal Energy Regulatory Commission (FERC) issued the District a new 50-year operating license. The District is currently reviewing all options prior to moving forward with final design, bidding, and construction of the project. The current plan is to issue debt to finance construction of Enloe Dam.

Additional information is contained in the notes to the financial statements. Please refer to Note 3 - Utility Plant and Note 4 - Long-Term Debt.

## **Contacting the District's Financial Management**

This financial report is designed to provide the District's ratepayers, investors, and other readers with a general overview of the District's finances and to show the District's accountability for money it receives. If you have questions about this report or need additional information, contact the District's Director of Finance at Public Utility District No. 1 of Okanogan County, P.O. Box 912, Okanogan, WA 98840, or phone (509) 422-3310.



Don Coppock  
Director of Finance/Auditor

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**STATEMENTS OF NET POSITION**

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**ASSETS AND DEFERRED OUTFLOWS OF RESOURCES**

	December 31,	
	<u>2013</u>	<u>2012</u>
<b>CURRENT ASSETS</b>		
Cash and temporary investments		
Cash and cash equivalents	\$ 6,200,740	\$ 1,833,309
Temporary investments	6,373,976	2,582,346
Accounts receivable, less allowance for doubtful accounts of \$25,000 for 2013 and 2012	2,787,275	3,184,373
Unbilled revenue	3,428,141	2,189,345
Materials and supplies	2,759,170	2,991,637
Prepayments and other	<u>197,192</u>	<u>265,169</u>
Total current assets	<u>21,746,494</u>	<u>13,046,179</u>
<b>RESTRICTED ASSETS</b>		
Cash equivalents and investments		
Bond reserve and debt service	2,233,838	2,234,076
Board-designated reserve	8,135,000	8,135,000
Construction funds	<u>-</u>	<u>7,266,304</u>
Total restricted assets	<u>10,368,838</u>	<u>17,635,380</u>
<b>UTILITY PLANT, at cost</b>		
Plant in service	136,339,790	133,872,099
Construction work in progress	<u>31,921,619</u>	<u>23,660,494</u>
	168,261,409	157,532,593
Less accumulated depreciation and amortization	<u>62,232,575</u>	<u>59,565,058</u>
Net utility plant	<u>106,028,834</u>	<u>97,967,535</u>
<b>OTHER ASSETS</b>		
Unamortized debt issuance costs	-	370,198
Conservation loans and notes receivable	<u>377,491</u>	<u>551,207</u>
Total other assets	<u>377,491</u>	<u>921,405</u>
Total assets	<u>138,521,657</u>	<u>129,570,499</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>		
Loss on refinancing of debt	<u>620,315</u>	<u>695,260</u>
Total assets and deferred outflows of resources	<u>\$ 139,141,972</u>	<u>\$ 130,265,759</u>

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**STATEMENTS OF NET POSITION**

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**LIABILITIES AND NET POSITION**

	December 31,	
	2013	2012
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 3,943,181	\$ 2,931,656
Accrued compensated absences	1,535,323	1,350,259
Accrued taxes	1,108,562	970,502
Customer deposits	539,860	535,105
Customer prepayments	492,458	632,202
Accrued bond interest	152,254	156,243
Current portion of long-term debt	1,645,000	1,600,000
Total current liabilities	9,416,638	8,175,967
<b>LONG-TERM DEBT</b>		
Revenue bonds	34,795,000	36,440,000
Other long-term debt	3,043,705	1,393,130
Bond issue premium	384,695	398,987
Bond issue discount	(46,417)	(51,574)
Total long-term debt	38,176,983	38,180,543
Total liabilities	47,593,621	46,356,510
<b>NET POSITION</b>		
Net investment in capital assets	66,827,166	66,518,757
Restricted	8,141,401	8,327,470
Unrestricted	16,579,784	9,063,022
Total net position	91,548,351	83,909,249
Total liabilities and net position	\$ 139,141,972	\$ 130,265,759

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**

	Years Ended December 31,	
	2013	2012
<b>OPERATING REVENUES</b>		
Electric - retail	\$ 39,861,279	\$ 35,588,404
Electric - wholesale	5,132,270	3,531,677
Telecommunications	2,217,116	2,096,256
Other operating revenues	1,286,159	1,412,834
<b>Total operating revenues</b>	<b>48,496,824</b>	<b>42,629,171</b>
<b>OPERATING EXPENSES</b>		
Cost of power	23,534,220	23,198,810
Transmission	46,918	39,691
Distribution	5,072,827	5,426,765
Telecommunications	1,130,469	924,802
Customer accounts	1,487,568	1,348,668
Customer service and information	578,749	747,115
Administration and general	4,420,433	4,169,687
Depreciation and amortization	4,584,884	4,601,137
Taxes	2,413,881	2,220,161
<b>Total operating expenses</b>	<b>43,269,949</b>	<b>42,676,836</b>
<b>Net operating revenues (expenses)</b>	<b>5,226,875</b>	<b>(47,665)</b>
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Interest income	58,695	74,313
Grant revenue	2,573,201	1,618,792
Contributed capital	990,165	991,816
Interest on long-term debt	(2,356,815)	(2,018,950)
Allowance for funds used during construction	800,989	632,432
Other revenue	492,647	446,441
Other expenses	(146,655)	-
<b>Net nonoperating revenues (expenses)</b>	<b>2,412,227</b>	<b>1,744,844</b>
<b>CHANGE IN NET POSITION</b>	<b>7,639,102</b>	<b>1,697,179</b>
<b>ACCUMULATED NET POSITION</b>		
Beginning of year	83,909,249	82,212,070
<b>End of year</b>	<b>\$ 91,548,351</b>	<b>\$ 83,909,249</b>

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**STATEMENTS OF CASH FLOWS**

	Years Ended December 31,	
	2013	2012
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts from customers	\$ 47,833,598	\$ 41,571,149
Payments to suppliers and employees	<u>(36,819,523)</u>	<u>(37,999,742)</u>
Net change in cash from operating activities	<u>11,014,075</u>	<u>3,571,407</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Acquisition and construction of capital assets, net	(12,707,840)	(10,304,194)
Proceeds from borrowings	1,715,467	1,079,195
Cash contributions in aid of construction	990,165	991,816
Proceeds from grants	2,573,201	1,618,792
Scheduled payments on debt	(1,664,892)	(1,570,671)
Interest paid on debt	<u>(1,086,352)</u>	<u>(878,857)</u>
Net change in cash from capital and related financing activities	<u>(10,180,251)</u>	<u>(9,063,919)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of investments	(19,375,978)	(13,661,258)
Sales and maturities of investments	22,850,890	17,135,300
Interest on investments	<u>58,695</u>	<u>74,313</u>
Net change in cash from investing activities	<u>3,533,607</u>	<u>3,548,355</u>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	4,367,431	(1,944,157)
<b>CASH AND CASH EQUIVALENTS</b>		
Beginning of year	<u>1,833,309</u>	<u>3,777,466</u>
End of year	<u><u>\$ 6,200,740</u></u>	<u><u>\$ 1,833,309</u></u>
<b>RECONCILIATION OF NET OPERATING REVENUES (EXPENSES)</b>		
<b>TO CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net operating revenues (expenses)	\$ 5,226,875	\$ (47,665)
Adjustments to reconcile net operating revenues (expenses) to net cash from operating activities		
Depreciation and amortization	4,584,884	4,601,137
Cash from changes in operating assets and liabilities		
Receivables	570,814	(830,930)
Unbilled revenue	(1,238,796)	(193,842)
Materials and supplies	232,467	88,420
Prepayments and other	(71,770)	(99,196)
Other assets	370,198	18,825
Accounts payable	1,011,524	(117,872)
Accrued compensation, benefits, customer deposits, prepayments, and taxes	<u>327,879</u>	<u>152,530</u>
<b>NET CHANGE IN CASH FROM OPERATING ACTIVITIES</b>	<u><u>\$ 11,014,075</u></u>	<u><u>\$ 3,571,407</u></u>
<b>SUPPLEMENTAL DISCLOSURES</b>		
Cash paid for interest on borrowings	<u><u>\$ 1,920,805</u></u>	<u><u>\$ 1,919,042</u></u>
Cash received as refund on interest on Build America Bonds	<u><u>\$ 407,647</u></u>	<u><u>\$ 445,515</u></u>

See accompanying notes.

# PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON

## NOTES TO FINANCIAL STATEMENTS

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### Note 1 - Summary of Significant Accounting Policies

**Organization** - Public Utility District No. 1 of Okanogan County (the District) is a municipal corporation governed by an elected three-member board of commissioners. The District owns, operates, and maintains an electric distribution system incorporating both electrical and telecommunication facilities and equipment. Financial information for both divisions is presented in a consolidated format.

**Reporting entity** - For financial reporting purposes, the District includes activities over which it exercises oversight responsibility. As required by generally accepted accounting principles (GAAP), management has considered all potential component units in defining the reporting entity. The District has no component units.

**Basis of accounting and presentation** - The accounting policies of the District conform to GAAP as applicable to proprietary funds of governmental units. The District adheres to the accounting standards and pronouncements of the Governmental Accounting Standards Board (GASB), which is the accepted standard-setting body for governmental entities and uses the Federal Energy Regulatory Commission (FERC) Uniform System of Accounts.

During 2013, the District adopted GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. The effect of the implementation of this statement to the District includes reclassifying certain items as deferred outflows of resources and further requires reclassification of certain items previously recorded as assets and liabilities to be presented as expenses or revenues. The implementation of this statement did not have a material effect on the current-year financial statements.

**Cash and cash equivalents** - The District considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

**Investments and restricted assets** - The District records investments at fair value. The District's investment portfolio consists entirely of fully insured, interest-bearing institutional deposits with terms of one year or less where the redemption value equals the purchase price plus a stated rate of interest. Therefore, the District's financial statements reflect no market adjustments.

In accordance with board resolutions and bond covenants, a number of separate funds have been established, and cash and investments held in these funds are restricted for special uses as follows:

	2013	2012
Rate stabilization fund	\$ 6,135,000	\$ 6,135,000
Employee compensated absences fund	1,400,000	1,400,000
Customer deposit fund	600,000	600,000
Sinking funds - 2003 bonds	72,737	73,017
Sinking funds - 2010 bonds	216,601	216,559
Bond reserve fund	1,944,500	1,944,500
Construction funds	-	7,266,304
	\$ 10,368,838	\$ 17,635,380

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 1 - Summary of Significant Accounting Policies (continued)**

**Accounts receivable and allowance for doubtful accounts** - The District renders billings for electrical consumption, sales, and services and for wholesale power and telecommunication sales and services on a monthly basis. Management reviews accounts receivable for collectibility on a regular basis, and an allowance for uncollectible accounts is established based on evaluation of specific accounts and historical experience. If the account is determined to be uncollectible, it is turned over to the local credit bureau for collection.

**Materials and supplies** - Materials and supplies provide for additions, maintenance, and repairs to the utility plant and are valued at weighted-average cost.

**Utility plant and depreciation** - See Note 3 for asset capitalization, depreciation, and retirement policies.

**Compensated absences** - The District accrues unpaid personal leave benefit amounts as earned. Personal leave, which may be accumulated up to 1,200 hours, is payable in full upon resignation, termination, retirement, or death.

**Revenue recognition** - The District recognizes revenue as earned on a monthly basis based on rates established by the District's board of commissioners. Because the customer meters are read and billed at various times during each month, the District estimates unbilled revenues for energy delivered to customers between their last respective cycle billing date and December 31, and it records that amount as unbilled revenue for the current year.

**Unamortized loss on debt refunding** - The difference between the cost to refund outstanding debt and the carrying value of bonds defeased by refunding bonds is deferred and amortized over the shorter of the remaining term of the refunded bonds or the term of the refunding bonds, using the straight-line or effective-interest method and recorded as deferred outflow of resources.

**Revenues and expenses** - The District distinguishes between operating and nonoperating revenues and expenses. Operating revenues and expenses are derived directly from the provision of wholesale and retail electrical generation, transmission, and distribution sales and service and from providing wholesale telecommunications sales and service. Revenues and expenses ancillary to these purposes are treated as nonoperating.

**Contributed capital** - Contributions in aid of construction are District-mandated customer connection charges used to fund construction of system properties necessary to extend service to a new customer. These payments are recognized in nonoperating revenue as contributed capital when the associated facilities are constructed or acquired.

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

## **NOTES TO FINANCIAL STATEMENTS**

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### **Note 1 - Summary of Significant Accounting Policies (continued)**

**Net position** - Net position consists of:

**Net investment in capital assets** - This component of net position consists of capital assets, net of accumulated depreciation, less outstanding balances of any borrowings that are attributable to the acquisition, construction, or improvement of those assets.

**Restricted** - This component consists of net position 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. Balances currently classified as restricted by enabling legislation include the rate stabilization fund, employee compensated absences fund, customer deposit fund, bond principal and interest (net of accrued interest) due in the upcoming year, and the debt service reserve fund.

**Unrestricted** - Unrestricted net position components are those that do not meet the definition of "restricted" or "net investment in capital assets."

**Accounting estimates** - The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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.

**Significant risk and uncertainties** - The District is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include weather and natural-disaster-related disruptions; collective bargaining labor disputes; fish and other Endangered Species Act issues; Environmental Protection Agency regulations; federal government regulations or orders; deregulation of the electrical industry; concentration risk in the form of Wells Hydroelectric Project, as described in Note 11; and market risks inherent in buying and selling of power, a commodity with inelastic demand characteristics and minimal storage capability.

**Reclassifications** - Certain reclassifications have been made to balances reported in prior-year financial statements to conform to the current-year presentation.

**Subsequent events** - Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. The District recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the statements of net position, including the estimates inherent in the process of preparing the financial statements. The District's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statements of net position but arose after the balance sheet date and before the financial statements are available to be issued.

The District has evaluated subsequent events through May 12, 2014, which is the date the financial statements are available to be issued.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 2 - Deposits and Investments**

**Custodial credit risk** - Custodial credit risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments. All District deposits and investments are either insured, registered, or held by the District or its agents in the District's name and are intended to be held until maturity.

**Credit risk** - Credit risk is the risk that an issuer or counterparty to an investment will not fulfill its obligations. As required by state law, all investments of District funds are obligations of the U.S. government, bankers' acceptances, deposits in the Washington State Treasurer's Local Government Investment Pool, or deposits with Washington State banks and savings and loan institutions. All deposits are either entirely covered by the Federal Deposit Insurance Corporation or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission.

**Interest rate risk** - Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. The District manages this risk by limiting the average maturity of investments to one year or less.

Distribution of the investment portfolio was as follows:

	<u>2013</u>	<u>2012</u>
Bank certificates of deposit	\$ 8,635,000	\$ 8,635,000
Local Government Investment Pool	<u>8,107,814</u>	<u>11,582,726</u>
	<u>\$ 16,742,814</u>	<u>\$ 20,217,726</u>

**Note 3 - Utility Plant**

Utility plant in service and other capital assets are recorded at cost when the historical cost is known. When historical cost is not known, assets are recorded at estimated fair value. Costs include labor, materials, overhead, capitalized interest, and related indirect costs. The District capitalizes assets with cost in excess of \$1,000. Depreciation expense is computed using the straight-line method employing useful lives of 4 to 50 years. Repairs are charged to operating expenses.

The original cost of operating property retired or otherwise disposed of and the cost of removal, less salvage, is charged to accumulated depreciation. However, in the case of the sale of a significant operating unit or system, the original cost is removed from the utility plant accounts, accumulated depreciation is charged with the accumulated depreciation related to the property sold, and net gain or loss on disposition is credited or charged to income.

Preliminary costs incurred for proposed projects are deferred pending construction of the asset and included in construction work in process. Costs relating to projects ultimately constructed are transferred to utility plant, whereas charges that relate to abandoned projects are expensed.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 3 - Utility Plant (continued)**

Capital asset activity for the years ended December 31, 2013 and 2012, was as follows:

	Balance January 1, 2013	Additions	Retirements and Transfers	Balance December 31, 2013
Intangible plant	\$ 92,297	\$ -	\$ -	\$ 92,297
Generation plant	588,394	-	-	588,394
Transmission plant	4,720,679	159,387	(46,104)	4,833,962
Distribution plant	95,051,142	3,431,678	(732,135)	97,750,685
General plant	27,247,823	315,185	(307,346)	27,255,662
Telecommunications plant	5,539,220	470,232	(823,206)	5,186,246
Acquisition adjustment	632,544	-	-	632,544
	133,872,099	4,376,482	(1,908,791)	136,339,790
Construction work in progress	23,660,494	8,261,125	-	31,921,619
Total utility plant	157,532,593	12,637,607	(1,908,791)	168,261,409
Accumulated depreciation	(59,565,058)	(5,512,651)	2,845,134	(62,232,575)
Net capital assets	<u>\$ 97,967,535</u>	<u>\$ 7,124,956</u>	<u>\$ 936,343</u>	<u>\$ 106,028,834</u>
	Balance January 1, 2012	Additions	Retirements and Transfers	Balance December 31, 2012
Intangible plant	\$ 92,297	\$ -	\$ -	\$ 92,297
Generation plant	588,394	-	-	588,394
Transmission plant	4,713,469	18,777	(11,567)	4,720,679
Distribution plant	92,113,850	3,582,895	(645,603)	95,051,142
General plant	27,087,146	372,761	(212,084)	27,247,823
Telecommunications plant	4,816,932	896,522	(174,234)	5,539,220
Acquisition adjustment	632,544	-	-	632,544
	130,044,632	4,870,955	(1,043,488)	133,872,099
Construction work in progress	18,055,375	5,605,119	-	23,660,494
Total utility plant	148,100,007	10,476,074	(1,043,488)	157,532,593
Accumulated depreciation	(55,836,441)	(5,359,405)	1,630,788	(59,565,058)
Net utility plant	<u>\$ 92,263,566</u>	<u>\$ 5,116,669</u>	<u>\$ 587,300</u>	<u>\$ 97,967,535</u>

Plant in service balances presented above include nondepreciable land of \$1,126,051 as of December 31, 2013 and 2012, respectively.

**Note 4 - Long-Term Debt**

In 2003, the District issued \$10,565,000 in 20-year serial bonds to finance capital construction and to refund a previous short-term debt obligation. Interest rates on the 2003 issuances range from 2.46% to 5.46%.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 4 - Long-Term Debt (continued)**

During 2010, the District issued \$9,105,000 in 10-year Series A bonds with interest rates ranging from 2.00% to 4.50%, and \$23,355,000 in 30-year Series B taxable Build America Bonds with interest rates ranging between 1.095% and 6.046%. These interest rates are subject to a federal subsidy payment from the federal government that ranged from 32.5% to 35.0% of the interest rate during the current year. From this issuance, \$5,285,000 was used to defease the 2002 bonds, which were fully repaid in 2011. The remaining \$27,175,000 of the new debt was earmarked for capital projects including, but not limited to, the new District headquarters facility constructed in 2010 and the Pateros-Twisp transmission line, now in its final permitting stage. This debt is subject to certain covenants.

In 2010, the District authorized a not-to-exceed \$3,667,855 loan with the United States Department of Agriculture (USDA) for broadband improvements related to the American Recovery and Reinvestment Act (ARRA) award granted in 2010 (Note 9). During 2011, the District began drawing funds on the loan and as of December 31, 2013 and 2012, a total of \$3,124,268 and \$1,408,801, respectively, in loan funds related to this award had been received. These funds are to be paid back over a 23-year period starting one year after the initial draw. This initial draw occurred on August 15, 2011. This direct cost of money loan will bear interest at the rate applicable to each advance of loan funds based on the average yield on outstanding marketable obligations of the United States having a final maturity comparable to the final maturity of the advance. Interest rates as of December 31, 2013, ranged from 2.32% to 3.63%. Additional information describing this award can be found in Note 9.

Total revenue bonds outstanding at December 31, 2013, are \$36,440,000, for which substantially all revenues of the District are pledged as security.

The following are changes in long-term debt for the years ended December 31, 2013 and 2012:

	Balance January 1, 2013	Additions	Payments/ Amortization	Balance December 31, 2013	Current Portion
2003 revenue bonds	\$ 6,890,000	\$ -	\$ (555,000)	\$ 6,335,000	\$ 580,000
2010 revenue bonds	31,150,000	-	(1,045,000)	30,105,000	1,065,000
2011 ARRA loan	1,393,130	1,715,467	(64,892)	3,043,705	-
Unamortized bond premium	398,987	-	(14,292)	384,695	-
Unamortized bond discount	(51,574)	-	5,157	(46,417)	-
<b>Total long-term debt</b>	<b>\$ 39,780,543</b>	<b>\$ 1,715,467</b>	<b>\$ (1,674,027)</b>	<b>\$ 39,821,983</b>	<b>\$ 1,645,000</b>
	Balance January 1, 2012	Additions	Payments/ Amortization	Balance December 31, 2012	Current Portion
2003 revenue bonds	\$ 7,415,000	\$ -	\$ (525,000)	\$ 6,890,000	\$ 555,000
2010 revenue bonds	32,180,000	-	(1,030,000)	31,150,000	1,045,000
2011 ARRA loan	329,606	1,079,195	(15,671)	1,393,130	-
Unamortized bond premium	413,279	-	(14,292)	398,987	-
Unamortized bond discount	(56,731)	-	5,157	(51,574)	-
<b>Total long-term debt</b>	<b>\$ 40,281,154</b>	<b>\$ 1,079,195</b>	<b>\$ (1,579,806)</b>	<b>\$ 39,780,543</b>	<b>\$ 1,600,000</b>

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 4 - Long-Term Debt (continued)**

During 2010, the District established a \$10 million operating line of credit with a financial institution. As of December 31, 2013, there was no outstanding balance on that line of credit.

The annual debt service payment requirements (principal and interest) on debt outstanding as of December 31, 2013, are as follows:

	2003 Bonds		2010 Bonds		Total
	Interest	Principal	Interest	Principal	
2014	\$ 292,847	\$ 580,000	\$ 1,534,207	\$ 1,065,000	\$ 3,472,054
2015	261,176	615,000	1,507,113	1,075,000	3,458,289
2016	227,600	650,000	1,474,863	1,105,000	3,457,463
2017	192,110	685,000	1,447,262	1,145,000	3,469,372
2018	158,219	700,000	1,418,705	1,175,000	3,451,924
2019-2023	337,001	3,105,000	6,345,097	5,305,000	15,092,098
2024-2028	-	-	5,199,306	4,425,000	9,624,306
2029-2033	-	-	3,819,828	5,360,000	9,179,828
2034-2038	-	-	2,099,109	6,485,000	8,584,109
2039-2040	-	-	270,560	2,965,000	3,235,560
	<u>\$ 1,468,953</u>	<u>\$ 6,335,000</u>	<u>\$ 25,116,050</u>	<u>\$ 30,105,000</u>	<u>\$ 63,025,003</u>

The above table does not reflect the annual debt service relating to the ARRA loan as disclosed previously in this note. In addition to the \$3,043,705 in loan funds outstanding on December 31, 2013, periodic draws on the ARRA award will be made through the project's expiration date of September 30, 2015. Any funds drawn are restricted to authorized project costs as approved in the project budget. Security for the loan is limited to net revenues, on parity with the lien granted with respect to any parity bonds, and the balance in the District's Pledged Deposit Account. The Pledged Deposit Account balance would be limited to unspent advances, if any.

**Note 5 - Retirement and Deferred Compensation Plans**

**Public Employees' Retirement System** - All full-time District employees and certain qualifying part-time employees of the District participate in the Public Employees' Retirement System (PERS), a statewide local government retirement system administered by the Department of Retirement Systems (DRS), under cost-sharing multiple-employer defined benefit and/or defined contribution plans.

**Plan description** - The state legislature established PERS in 1947 under Chapter 41.40 RCW. Membership in the system includes elected officials; state employees; employees of the supreme, appeals, and superior courts (other than judges); employees of legislative committees; college and university employees not in national higher education retirement programs; judges of district and municipal courts; and employees of local government. There were 1,316 employers participating in the PERS system as of June 30, 2013.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 5 - Retirement and Deferred Compensation Plans (continued)**

PERS contains three plans. Participants who joined the system by September 30, 1977, were enrolled in Plan I. Those joining between October 1, 1977, and May 31, 2003, were enrolled in Plan II. With the creation of Plan III, new enrollees are given the option of joining either Plan II or Plan III, and existing Plan II members, as of a fixed date, were given the option of transferring to Plan III or remaining in Plan II. Retirement benefits are financed from employee/employer contributions and investment earnings.

Plan I members are eligible for retirement after 30 years of service, or at the age of 60 with 5 years of service, or at the age of 55 with 25 years of service. The annual retirement benefit is 2% per service year of the average annual salary for the highest 2 consecutive service years, capped at 60%. If qualified, after reaching age 66, a cost-of-living allowance is granted based on years of service credit and is capped at 3% annually.

Plan II members may retire at the age of 65 with 5 years of service, or at the age of 55 with 20 years of service. The annual retirement benefit is 2% per service year of the average annual salary for the highest 5 consecutive service years with no cap on the percentage. Retirements under Plan II prior to the age of 65 are actuarially reduced; however, Plan II retirees are granted cost-of-living increases capped at 3% annually.

Plan III has a dual benefit structure. The defined benefit portion of Plan III is very similar to the Plan II benefit except that it offers only 1% (instead of 2%) per service year of the average annual salary for the highest 5 consecutive service years with no cap on the percentage. Retirements under Plan III prior to the age of 65 are also actuarially reduced, and Plan III retirees are granted cost-of-living increases capped at 3% annually. The defined contribution portion of the benefit, funded entirely by employee contributions, provides a chosen annuity payment stream that runs only until the accumulated funds are exhausted.

**Funding policy** - Each biennium, the legislature establishes employer contribution rates for all three plans and employee contribution rates for Plan II. Employee contribution rates for Plan I are established by legislative statute at 6% and do not vary from year to year. Employee rates for Plan III are an individual member choice from options ranging from 5% to 15%. Contribution rates for Plan I are not necessarily adequate to fully fund the plan. All employer rates and the employee rates for Plan II are developed by the Office of the State Actuary to fully fund the system. All employers are required to contribute at the level established by state law. The methods used to determine the contribution requirements were established under state statute in accordance with Chapters 41.40 and 41.45 RCW. Financial and operating information regarding the State of Washington Department of Retirement Systems may be obtained from the Department of Retirement Systems, Communications Unit, P.O. Box 48380, Olympia, WA 98504-8380.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 5 - Retirement and Deferred Compensation Plans (continued)**

The District's PERS-covered payroll for the year ended December 31, 2013, was \$7,156,667, with total payroll for all employees being \$7,367,721 in 2013. The District's PERS-covered payroll for the year ended December 31, 2012, was \$7,132,821, with total payroll for all employees being \$7,182,254 in 2012. The required contribution rates expressed as a percentage of current-year covered payroll at December 31, 2013 and 2012, were:

	<u>Plan I</u>	<u>Plan II</u>	<u>Plan III</u>
<b>2013</b>			
Employer	7.21% - 9.21%	7.21% - 9.21%	7.21% - 9.21%
Employee	6.00%	4.64% - 4.92%	5% - 15%
<b>2012</b>			
Employer	7.25% - 7.21%	7.25% - 7.21%	7.25% - 7.21%
Employee	6.00%	4.64%	5% - 15%

Both the District and the employees met their funding obligation, resulting in contributions for the years ended December 31, 2013 and 2012, as follows:

	<u>Plan I</u>	<u>Plan II</u>	<u>Plan III</u>	<u>Total</u>
<b>2013</b>				
Employer	\$ 3,696	\$ 552,632	\$ 32,280	\$ 588,608
Employee	<u>2,699</u>	<u>321,331</u>	<u>20,310</u>	<u>344,340</u>
Total	<u>\$ 6,395</u>	<u>\$ 873,963</u>	<u>\$ 52,590</u>	<u>\$ 932,948</u>
<b>2012</b>				
Employer	\$ 3,161	\$ 481,857	\$ 27,675	\$ 512,693
Employee	<u>2,639</u>	<u>311,053</u>	<u>19,912</u>	<u>333,604</u>
Total	<u>\$ 5,800</u>	<u>\$ 792,910</u>	<u>\$ 47,587</u>	<u>\$ 846,297</u>

**Deferred compensation plans** - The District offers its employees two deferred compensation plan options created in accordance with Internal Revenue Code Section 457, covering all eligible employees of the District, as defined in the plan document. These plans allow employees to defer a portion of their salary until future years. Plan assets are held in trust for the exclusive benefit of the plan participants and their designated beneficiaries and are not subject to the claims of the District's general creditors. Deferred compensation funds are not available to employees until retirement, termination, death, or unforeseeable emergency.

Additionally, the District adopted a 401(a) defined contribution plan (the 401(a) Plan) effective January 1, 2000. Participation in the 401(a) Plan is open to eligible employees of the District as defined in the plan document. The District makes matching contributions to the 401(a) Plan at a rate of 50% of the employee's contribution. The match is capped at 2% of gross wages for nonexempt employees and 6% of gross wages for exempt employees. During 2013 and 2012, the District contributed \$207,011 and \$203,729, respectively, to the 401(a) Plan.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 5 - Retirement and Deferred Compensation Plans (continued)**

**VEBA plan** - In August 2005, the District implemented a voluntary employees' beneficiary association (VEBA) plan designed to provide limited employer funding on a tax-free basis for employee medical premiums and benefits for all eligible employees of the District, as defined in the plan document. The District's current VEBA contribution rate is 2% of the employee's straight-time salary. Plan assets, although under District control, are held in trust for the exclusive benefit of the plan participants and their designated beneficiaries and are not subject to the claims of the District's general creditors. During 2013 and 2012, the District contributed \$135,174 and \$130,879, respectively, to the VEBA plan.

**Note 6 - Other Post-Employment Benefits**

The District provides partial reimbursement for health care insurance premiums for retired employees. Beginning August 1, 2005, retiring employees choosing to continue medical coverage under the District's plan became eligible to receive \$10 per service year per month toward post-employment medical premiums. The reimbursement begins at the later of the month of retirement or at age 60 and expires when the retiree reaches age 65. The dollar value of the reimbursement is set to decrease \$1 each year until it expires in August 1, 2018. Subsequently, employees retiring between August 1, 2007, and July 31, 2011, are eligible for \$8 per service year per month in reimbursement, with the eligible amount decreasing by \$1 per service year per month each year thereafter. The estimated future liability is \$51,110 and \$59,981 at December 31, 2013 and 2012, respectively. The District is funding this liability on a pay-as-you-go basis with contributions of \$2,784 expensed in 2013 and 2012.

**Note 7 - Self Insurance**

The District is a member of Public Utility Risk Management Services Joint Self Insurance Fund (the Fund). Chapter 48.62 RCW authorizes the governing body of one or more governmental entities to form together into or join an organization for the joint purchasing of insurance, and/or joint self-insuring, and/or joint hiring or contracting for risk management services to the same extent that they may individually purchase insurance, self-insure, or hire or contract for risk management services. The Fund was formed on December 31, 1976, when certain Washington Public Utility Districts signed an agreement to pool their self-insured losses and jointly purchase insurance and administrative services. There are currently 19 active members in the Fund.

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

## **NOTES TO FINANCIAL STATEMENTS**

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### **Note 7 - Self Insurance (continued)**

The Fund operates three separate insurance pools: the Liability Pool, the Property Pool, and the Health & Welfare Pool. Fund members may belong to one, two, or all three pools according to their insurance needs. The Liability Pool insures on a \$1,000,000 self-insured retention with a \$250 deductible. Coverage is on an occurrence basis. In addition, the Liability Pool purchases excess general liability and excess public official liability coverage. The Property Pool operates on a maximum \$500,000 self-insured retention, with a \$75,000 deductible on listed major generating units and a \$250 deductible on all other listed items of property. Coverage is on an occurrence basis and the Property Pool purchases excess property coverage above the self-insured retention level. The Health & Welfare Pool is funded by paid claims reimbursement from the member generating the claim and by pooled assessment for administration and excess stop-loss insurance coverage. In all pools, members are assessed as necessary to maintain designated minimum pool balances. Because the Fund is a cooperative program, there is joint liability among the participants of each pool. The District participates in only the Liability and Property Pools. In 2013 and 2012, the District contributed \$126,401 and \$87,792, respectively, to the Liability Pool and \$20,905 and \$63,084, respectively, to the Property Pool. Should any member terminate its affiliation with the Fund, it remains financially responsible to the Fund for any unresolved, unreported, and in-process claims for the period that it was a signatory to the agreement.

Self-insured retentions are fully funded by current and former members, and settlements have never exceeded coverage limits. Claims are processed by Pacific Underwriters Corporation, P.O. Box 68787, Seattle, WA 98168, a private entity contracted to perform administrative, claims adjustment, and loss prevention services, and which also compiles an annual financial report for the Fund. The Fund is governed by a board of directors that consists of one designated representative from each participating member. The Fund administrator and an elected six-member administrative committee (on which a District representative currently serves) are responsible for conducting the daily business affairs of the Fund.

### **Note 8 - Conservation Programs**

The District operates a number of energy conservation programs. These include both residential and commercial weatherization loan programs, appliance and water heater rebate programs, appliance loan programs, and residential and commercial energy audits. Loan programs will provide five-year loans of up to \$10,000 on residential dwellings and up to \$25,000 on commercial enterprises for qualifying conservation measures. The District incurred conservation program costs of \$192,339 and \$128,530 in 2013 and 2012, respectively, which were charged to operations.

### **Note 9 - Telecommunications**

The District has recognized the necessity of a modern and reliable communications infrastructure in managing its core electric distribution function and now operates and maintains a telecommunications network providing these services for internal use. Additionally, it provides wholesale telecommunications services, in accordance with Washington State law, to qualified retail merchants who, in turn, provide services to end users in the District's service territory.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 9 - Telecommunications (continued)**

The ongoing construction and the operations of the telecommunications network are being accomplished using the District's own workforce. The District has established separate detailed accounting for wholesale telecommunications activities and has developed a financing arrangement under which the continuing construction of telecommunications infrastructure and the operations of the telecommunications network are accomplished using funds loaned from the District's electric reserves.

Condensed telecom revenues and expenditures and assets and liabilities information follows:

	<u>2013</u>	<u>2012</u>
Operating revenues	\$ 2,251,622	\$ 2,117,106
Operating expenses	(1,953,350)	(1,745,714)
Nonoperating revenues - grant	2,573,201	1,618,792
Nonoperating expenses	<u>(306,613)</u>	<u>(239,817)</u>
Change in net position	<u>\$ 2,564,860</u>	<u>\$ 1,750,367</u>
Total assets	\$ 8,422,920	\$ 4,336,964
Total liabilities	<u>(4,720,784)</u>	<u>(3,199,690)</u>
Total net position	<u>\$ 3,702,136</u>	<u>\$ 1,137,274</u>

During 2010, the District applied for and was awarded ARRA funding to further deploy broadband communication services in the underserved areas of Okanogan County. The award package consists of \$5,501,782 in grant money and a \$3,667,855 loan. The proposed project will bring high-speed broadband to approximately 6,543 premises that currently lack access, and calls for placement of approximately 170 access nodes and 179 miles of fiber backbone. Project design and engineering began in 2011, and as of December 31, 2013, the District had received \$4,686,401 of grant funding and \$3,124,268 in loan funding against the accumulated project expenditures.

**Note 10 - Energy Northwest**

**ENW Nuclear Project Nos. 1, 2, and 3** - The District has entered into "net billing agreements" with Energy Northwest (ENW, formerly Washington Public Power Supply System) and the Bonneville Power Administration (BPA). Under terms of these agreements, the District has purchased a maximum of .255% and 1.042% of the capability of ENW's Nuclear Project Nos. 1 and 2, respectively, and .143% of the capability of ENW's 70% ownership share of its Nuclear Project No. 3, and has assigned this capability to BPA. BPA is unconditionally obligated to pay the District, and the District is unconditionally obligated to pay ENW, the pro rata share of the total annual costs of each project, including debt service on revenue bonds issued to finance the projects, whether or not the projects are completed, operable, or operating and notwithstanding the suspension, reduction, or curtailment of the projects' output.

# PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON

## NOTES TO FINANCIAL STATEMENTS

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### Note 10 - Energy Northwest (continued)

Nuclear Project Nos. 1 and 3 were approximately 63% and 75% complete, respectively, and had both been in a state of extended construction delay for many years, with all systems being maintained in condition to resume construction at any time. However, on May 13, 1994, the ENW full board of directors voted to declare termination of both projects. At this juncture, there has been no resolution concerning the final dispensation of the assets and liabilities associated therewith.

Nuclear Project No. 2 was completed and placed in operation on December 13, 1984.

The District's net billing obligations in 2013 and 2012 were as follows:

ENW Fiscal 2014 Budget Year	No. 1	No. 2	No. 3	Total
Annual budget	\$ 385,110,000	\$ 430,990,000	\$ 213,540,000	\$ 1,029,640,000
District's share	0.00255	0.01042	0.00143	
District's net billing obligation	982,031	4,490,916	305,362	5,778,309
ENW Fiscal 2013 Budget Year				
Annual budget	\$ 341,902,000	\$ 485,016,000	\$ 232,636,000	\$ 1,059,554,000
District's share	0.00255	0.01042	0.00143	
District's net billing obligation	871,850	5,053,867	332,669	6,258,386

**Hanford project** - In accordance with agreements between ENW, BPA, and 76 participants, and between ENW and the U.S. Department of Energy (DOE), ENW constructed the Hanford Project, which began commercial operation in 1966 with a capacity of approximately 860 MW.

Pursuant to an exchange agreement entered into between the District, ENW, and BPA, the District had purchased .424% of the output of the Hanford Project and is obligated to pay ENW the same percentage of the annual costs.

Under an exchange agreement with the other participants in the Hanford Project, BPA had acquired the capability of the Hanford Project, including the District's share, in exchange for power from BPA. A decision was made in February 1988 by the DOE to maintain the project in a "cold standby" mode of operation.

ENW has evaluated alternative energy uses for the plant to no avail. Current options include a transfer to DOE for removal and site restoration, or removal and site restoration by ENW. At this time, it is unknown what the eventual disposition of the Hanford Project will be. ENW has reduced the project's assets to net realizable value and accrued the estimated cost of removal and site restoration.

**Nine Canyon Wind Project** - On October 1, 2001, the District entered into a power purchase agreement with ENW for output from the Nine Canyon Wind Project. The original project consisted of 37 wind turbines with an aggregate generating capacity of approximately 48 MW, and was launched into commercial operation in fall 2002. During 2003, a second phase of the project was completed, adding an additional 12 turbines and bringing the project capacity up to about 63.7 MW. During 2006, a third phase of the project was completed, adding an additional 14 turbines and bringing the current total project capacity up to about 96 MW.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 10 - Energy Northwest (continued)**

The District is currently one of 10 public utility districts participating in the power purchase agreements for project output. The District purchased a 25% share of the generation output from Phases 1 and 2 and no output at all from Phase 3, bringing its combined share of total project output to 16.61%. The District is committed to paying its pro rata share of debt service on the Nine Canyon Wind Project Revenue Bonds issued by ENW for Phases 1 and 2. A bond refunding/reissuance process commenced in 2004 and completed in 2005, thereby establishing the District's estimated liability for project bond principal at \$23,312,500. That amount could escalate to as much as \$29,140,625 after a step-up provision that could trigger in the event that other purchasers defaulted on their contractual obligations. The District pays its share of the ongoing project operational costs through monthly power purchase agreement assessment invoices.

**Note 11 - Other Power Supply Agreements**

**Wells Hydroelectric Project** - Since the initial construction of the Wells Hydroelectric Project, the District has been a party to a power sales contract governing the apportionment of the project output. However, during the 1980s, both the District and Public Utility District No. 1 of Douglas County (Douglas PUD) contested several provisions of the 1963 agreement and sought resolution of the disputed issues in Chelan County Superior Court. Disputes between the parties were resolved with a Memorandum of Understanding signed on August 5, 1991, requiring the two Districts to negotiate a new power sale contract commencing on September 2018 and extending for an additional 50 years. Negotiations on this contract are currently in process. The District's current share of the total output from Wells Hydroelectric Project is 7.64%, which represents 35.85% and 36.0% of the District's total power purchases in 2013 and 2012, respectively.

**Enloe Hydroelectric Project** - For many years, the District has been pursuing the possible rehabilitation of Enloe Hydroelectric Dam on the Similkameen River near Oroville, Washington. The District is the present owner of the dam, and relicensing attempts prior to 2005 were intended to revive an existing facility with its original output of 26,000 MWh annually and installed capacity of 4,100 KW.

On March 3, 1983, the District was issued a license by FERC for renovation and resumed operation of the Enloe project. The District subsequently appealed 14 of the licensing provisions. After extensive review, on March 6, 1986, FERC repealed the license previously granted to the District and placed the license in a "License Application Pending File" until all outstanding issues were resolved. FERC dismissed the license application in December 1987.

In February 1988, the District submitted a new application for a preliminary permit on the project. FERC granted the permit on June 8, 1988, and the District began the required preliminary studies. The District then submitted a license application to FERC on June 1, 1991, and FERC prepared an environmental assessment with the possibility of issuing an operating license.

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

### **NOTES TO FINANCIAL STATEMENTS**

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#### **Note 11 - Other Power Supply Agreements (continued)**

On September 13, 1996, FERC again issued a license to the District for restoration of the project. Although fish passage was not a stated requirement of the license, the licensing language left an open-ended opportunity for certain federal agencies to intervene and require fish passage at a later date. The uncertainty of this language made it impossible to accurately forecast the project costs or determine feasibility, so the District, along with several other entities, appealed the licensing conditions. A stay of the license was issued as a result of the pending listing of the Upper Columbia Steelhead under the Endangered Species Act and a determination of the Enloe project's negative impact upon them. On February 23, 2000, FERC rescinded the license because the National Marine Fisheries Service (NMFS) continued to require upstream fish passage as a condition of the license, while the British Columbia Provincial and Tribal Authorities remain opposed to any such passage requirements.

On January 21, 2005, the District again submitted a new application to FERC for a preliminary permit on the project. Using the FERC Traditional Licensing Process (TLP), the District filed the license application with FERC on August 22, 2008. The proposed configuration would approximately double the project output to 47,300 MWh of energy per year and 9,000 KW of capacity.

Since then, the District has spent the better part of a decade on environmental assessments, resource studies, permitting issues, and litigation. On August 31, 2011, FERC issued the Final Environmental Assessment for the Enloe Hydroelectric Project, and the District continued in the development of the state and local permitting processes. The District received its Section 401 Water Quality Permit in late 2012, but it was immediately appealed by various environmental groups before finally being settled by the Washington State Pollution Control Hearing Board. FERC issued the District a new 50-year operating license on July 9, 2013, and the District is now reviewing its final step prior to commencement of final design, financing, bidding, and construction.

#### **Note 12 - Northwest Open Access Network**

The District is a member of Northwest Open Access Network (NoaNet), a nonprofit mutual corporation formed by the District in collaboration with several other public utilities in the state of Washington. NoaNet was incorporated in February 2000 to facilitate the construction of a communications backbone to accommodate the increasing broadband needs of the member utilities and their customers. The NoaNet network began commercial operation in early 2001.

In July 2001, NoaNet issued \$27 million in Telecommunications Network Revenue Bonds (taxable) to finance the repayment of startup funds advanced by founding members and the initial costs of construction and commissioning. The bonds began maturing in December 2003 and will continue through December 2016, with interest due semi-annually at rates ranging from 5.05% to 7.09%. The District has entered into a repayment agreement to guarantee its 5.45% portion of the NoaNet bond debt, which totaled \$8,185,000 and \$10,835,000 as of December 31, 2013 and 2012, respectively.

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 12 - Northwest Open Access Network (continued)**

In 2008, NoaNet established a line of credit in the amount of \$1.5 million to finance capital expenditures and network upgrades. There was no outstanding balance on this credit line as of December 31, 2013, because it was fully repaid. In 2012, the outstanding balance was \$0.3 million.

In 2009, NoaNet established another nonrevolving line of credit in the amount of \$1.5 million to finance capital expenditures and network upgrades for new customers. The outstanding balance on this credit line as of December 31, 2013 and 2012, was \$166,667 and \$500,000 respectively.

In 2012, NoaNet established yet another nonrevolving line of credit in the amount of \$5 million for capital financing of sales opportunities. Draws were made throughout 2013 and 2012, leaving balances of \$5 million and \$756,400 as of December 21, 2013 and 2012, respectively.

The District's ownership interest in NoaNet was 5.5% as of December 31, 2012. During 2013, NoaNet incurred a net profit from operations of \$3,753,955. This operating margin, when combined with the approximately \$22 million in state and federal grant revenue brought the entity from a \$74,128,591 net position in 2012 to a net position of \$99,474,750 as of December 31, 2013. NoaNet financial results for 2013 are estimated; however, any variance will not have a material impact on the District's financial position.

Financial and operating information regarding NoaNet may be obtained from the NoaNet Financial Center, 5802 Overlook Ave NE, Tacoma, WA 98422.

**Note 13 - Pending Litigation**

**Pateros-Twisp Transmission Line** - For many years, the District has sought to construct a second transmission line into the Methow Valley. This project, along with a proposed new substation, would alleviate the current issues of both marginal electrical capacity and reliability. A coalition of local citizens and environmental groups has been consistently opposing the project and challenged the validity of the District's Final Environmental Impact Statement (FEIS) on grounds of various alleged deficiencies. On November 22, 2006, a ruling by an Okanogan County Superior Court judge upheld the validity of the FEIS; however, that decision was appealed by the plaintiffs to the Washington State Court of Appeals and spent the entire year of 2007 undergoing further review. On May 1, 2008, the appellate court upheld Okanogan County Superior Court's ruling on all counts. The plaintiffs then filed a petition for review with the Washington State Supreme Court on June 5, 2008, which was subsequently denied on December 2, 2008.

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

### **NOTES TO FINANCIAL STATEMENTS**

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#### **Note 13 - Pending Litigation (continued)**

During 2009, the District started the process of acquiring right-of-way easements and various other permits required for construction. Condemnation proceedings were initiated against two landowners, one being a private individual and one being a state entity, to obtain the remaining easements necessary to complete the route. In 2010, Okanogan County Superior Court granted “public use and necessity” against the two landowners. The condemnation process moved to the appraisal stage and a court date was set for July 5, 2011, to determine values for the take. This hearing date was subsequently stayed when the Washington State Department of Natural Resources (DNR) appealed to the Washington State Supreme Court for review of the District’s authority and ability to exercise condemnation authority against a State Agency. The Washington State Supreme Court heard the case on February 25, 2014, but a ruling on the matter has yet to be issued.

**Other litigation** - The District is involved in various claims arising in the normal course of business. The District does not believe that the ultimate outcome of these matters will have a material adverse impact on its financial position or results of operations.

**REPORT OF INDEPENDENT AUDITORS ON INTERNAL CONTROL OVER FINANCIAL  
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT  
AUDITING STANDARDS***

To the Commissioners  
Public Utility District No. 1  
of Okanogan County, Washington  
Okanogan, Washington

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the statements of net position as of December 31, 2013 and 2012, and the related statements of revenues, expenses, and changes in net position and cash flows of Public Utility District No. 1 of Okanogan County, Washington (the District) as of and for the year ended December 31, 2013, and have issued our report thereon dated May 12, 2014.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Purpose of This Report**

The purpose of this report is solely to describe the scope of testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in blue ink that reads "Mess Adams HP".

Everett, Washington  
May 12, 2014

## **REPORT OF INDEPENDENT AUDITORS ON COMPLIANCE FOR THE MAJOR PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE**

To the Commissioners  
Public Utility District No. 1  
of Okanogan County, Washington  
Okanogan, Washington

### **Report on Compliance for the Major Federal Program**

We have audited Public Utility District No. 1 of Okanogan County, Washington (the District) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on the District's major federal program for the year ended December 31, 2013. The District's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

### ***Management's Responsibility***

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal program.

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on compliance for the District's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the District's compliance.

### ***Opinion on the Major Federal Program***

In our opinion, the District complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2013.

### **Report on Internal Control over Compliance**

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the District's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

A handwritten signature in blue ink that reads "Mess Adams HP".

Everett, Washington  
May 12, 2014

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**

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**Section I - Summary of Auditor's Results**

**Financial Statements**

Type of auditor's report issued: *Unmodified*

Internal control over financial reporting:

- Material weakness identified?  Yes  No
- Significant deficiency identified?  Yes  None reported
- Noncompliance material to financial statements noted?  Yes  No

**Federal Awards**

Internal control over major program:

- Material weakness(es) identified?  Yes  No
- Significant deficiency(ies) identified?  Yes  None reported
- Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133?  Yes  No

**Identification of Major Program**

CFDA Numbers	Name of Federal Program or Cluster	Type of Auditor's Report Issued
ARRA - 10.787	ARRA - Broadband Initiative Program	<i>Unmodified</i>

Dollar threshold used to distinguish between type A and type B program: \$ 300,000

Auditee qualified as low-risk auditee?  Yes  No

**Section II - Financial Statement Findings**

None reported

**Section III - Federal Award Findings and Questioned Costs**

None reported

**SUPPLEMENTARY INFORMATION**

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**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED DECEMBER 31, 2013**

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<u>Federal Grant or Program Title</u>	<u>Federal CFDA Number</u>	<u>Federal EXP</u>
U.S. Department of Agriculture Rural Development		
ARRA - Broadband Initiatives Program (BIP)	ARRA - 10.787	<u>\$ 3,714,938</u>
Total U.S. Department of Agriculture		<u>\$ 3,714,938</u>
Total expenditures of federal awards		<u><u>\$ 3,714,938</u></u>

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED DECEMBER 31, 2013**

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**Note 1 - Basis of Presentation**

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes the federal grant activity of Public Utility District No. 1 of Okanogan County (the District) under programs of the federal government for the year ended December 31, 2013. The information presented in this Schedule is presented in accordance with the requirement of the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of the District, it is not intended to and does not present the financial position, changes in net position, or cash flows of the District.

**Note 2 - Summary of Significant Accounting Policies**

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

**Note 3 - Loan Award**

The matching portion of the grant was awarded in the form of a loan. These funds are to be paid back over a 23-year period starting one year after the initial draw, which occurred on August 15, 2011. This direct cost of money loan will bear interest at the rate applicable to each advance of loan funds based on the average yield on outstanding marketable obligations of the United States having a final maturity comparable to the final maturity of the advance. During 2013, \$1,715,467 was drawn on the loan and as of December 31, 2013, a total of \$3,124,268 in loan funds related to this award had been received.

**Note 4 - Relationship to the Financial Statements**

Federal awards are reported in the financial statements as an increase in value of electric plant assets and grant revenue.

**SUPPLEMENTARY INFORMATION (Unaudited)**

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**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**COMPARATIVE RESULTS OF OPERATIONS AND DEBT SERVICE COVERAGE (Unaudited)**

	Years Ended December 31,				
	2013	2012	2011	2010	2009
<b>OPERATING REVENUES</b>					
Electric - retail	\$ 39,861,279	\$ 35,588,404	\$ 33,355,835	\$ 29,102,331	\$ 30,564,662
Electric - wholesale	5,132,270	3,531,677	6,741,527	5,801,904	4,198,885
Telecommunications	2,217,116	2,096,256	1,955,276	1,912,283	1,622,655
Other operating revenue	1,286,159	1,412,834	1,041,958	1,024,195	1,176,193
<b>Total operating revenue</b>	<b>48,496,824</b>	<b>42,629,171</b>	<b>43,094,596</b>	<b>37,840,713</b>	<b>37,562,395</b>
<b>OPERATING EXPENSES</b>					
Cost of power	23,534,220	23,198,810	24,860,599	24,501,801	22,334,570
Electric operations and maintenance	5,119,745	5,466,456	4,754,468	5,463,131	5,309,984
Telecommunications operations and maintenance	1,130,469	924,802	601,857	638,124	690,763
Customer accounting and information	2,066,317	2,095,783	1,859,707	1,962,667	1,962,851
Administration and general	4,420,433	4,169,687	3,956,286	3,863,210	3,767,340
Depreciation and amortization	4,584,884	4,601,137	4,258,323	3,428,771	3,118,253
Taxes	2,413,881	2,220,161	2,138,550	1,839,338	1,876,404
<b>Total operating expenses</b>	<b>43,269,949</b>	<b>42,676,836</b>	<b>42,429,790</b>	<b>41,697,042</b>	<b>39,060,165</b>
<b>Net operating revenue (expense)</b>	<b>5,226,875</b>	<b>(47,665)</b>	<b>664,806</b>	<b>(3,856,329)</b>	<b>(1,497,770)</b>
<b>NONOPERATING REVENUE (EXPENSE)</b>					
Interest income	58,695	74,313	113,944	214,510	964,500
Grant revenue	2,573,201	1,618,792	494,408	-	-
Contributed capital	990,165	991,816	974,691	996,025	884,846
Interest on long-term debt	(2,356,815)	(2,018,950)	(2,068,361)	(992,488)	(767,365)
Allowance for funds used during construction (AFUDC)	800,989	632,432	661,140	-	-
Other revenue	492,647	446,441	524,741	140,331	214,852
Impairment of investment	-	-	-	-	(1,147,139)
Other expenses	(146,655)	-	(726,596)	(253,270)	(418,676)
<b>Net nonoperating revenue (expense)</b>	<b>2,412,227</b>	<b>1,744,844</b>	<b>(26,033)</b>	<b>105,108</b>	<b>(268,982)</b>
<b>CHANGE IN NET ASSETS</b>	<b>\$ 7,639,102</b>	<b>\$ 1,697,179</b>	<b>\$ 638,773</b>	<b>\$ (3,751,221)</b>	<b>\$ (1,766,752)</b>
<b>DEBT SERVICE COVERAGE ADJUSTMENTS</b>					
Interest charges (net AFUDC)	\$ 1,555,826	\$ 1,386,518	\$ 1,407,221	\$ 992,488	\$ 767,365
Depreciation and amortization	4,584,884	4,601,137	4,258,323	3,428,771	3,118,253
Capital grant	(2,573,201)	(1,618,792)	(494,408)	-	-
Impairment of investment	-	-	-	-	1,147,139
Rate stabilization transfer (to) from	-	-	-	1,400,000	(535,000)
<b>AVAILABLE FOR DEBT SERVICE</b>	<b>\$ 11,206,611</b>	<b>\$ 6,066,042</b>	<b>\$ 5,809,909</b>	<b>\$ 2,070,038</b>	<b>\$ 2,731,005</b>
<b>TOTAL DEBT SERVICE</b>	<b>\$ 3,589,687</b>	<b>\$ 3,508,662</b>	<b>\$ 3,434,230</b>	<b>\$ 1,428,314</b>	<b>\$ 1,557,495</b>
<b>DEBT SERVICE COVERAGE</b>	<b>3.12</b>	<b>1.73</b>	<b>1.69</b>	<b>1.45</b>	<b>1.75</b>

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**CUSTOMER STATISTICAL DATA (Unaudited)**

	Years Ended December 31,				
	2013	2012	2011	2010	2009
<b>ACTIVE CUSTOMER ACCOUNTS</b>					
Residential	16,999	17,001	16,892	16,828	16,869
General service	2,389	2,387	2,369	2,370	2,374
Industrial	3	4	4	4	4
Irrigation and frost control	1,345	1,336	1,331	1,337	1,346
Street lighting	20	21	21	21	21
Sales for resale	4	6	2	5	3
Telecommunications	16	19	21	21	20
<b>Total active customer accounts</b>	<b><u>20,776</u></b>	<b><u>20,774</u></b>	<b><u>20,640</u></b>	<b><u>20,586</u></b>	<b><u>20,637</u></b>
<b>REVENUES BILLED</b>					
Residential	\$ 21,328,142	\$ 18,862,658	\$ 18,089,701	\$ 14,961,740	\$ 15,156,514
General service	13,854,328	12,425,572	11,717,785	10,872,507	10,963,211
Industrial	1,347,794	1,135,306	1,052,677	982,599	1,720,197
Irrigation and frost control	3,194,235	3,029,476	2,371,177	2,158,725	2,597,766
Street lighting	136,782	135,393	124,495	126,761	126,974
Sales for resale	5,132,270	3,531,677	6,741,527	5,801,904	4,198,885
Telecommunications	2,217,116	2,096,256	1,955,276	1,912,283	1,622,655
Other operating revenue	1,286,159	1,412,834	1,041,958	1,024,195	1,176,193
<b>Total revenues billed</b>	<b><u>\$ 48,496,826</u></b>	<b><u>\$ 42,629,172</u></b>	<b><u>\$ 43,094,596</u></b>	<b><u>\$ 37,840,714</u></b>	<b><u>\$ 37,562,395</u></b>
<b>ENERGY CONSUMED (kWh)</b>					
Residential	293,419,767	289,639,794	324,538,087	289,163,326	312,799,371
General service	211,564,358	204,212,439	202,556,775	197,732,966	206,753,800
Industrial	23,517,840	20,583,710	21,141,320	21,602,188	40,935,028
Irrigation and frost control	62,319,197	65,131,338	60,835,173	60,258,036	75,416,713
Street lighting	1,363,740	1,359,672	1,359,877	1,340,152	1,326,639
Sales for resale	193,128,000	267,366,000	357,255,000	213,866,000	171,965,000
<b>Total energy consumed (kWh)</b>	<b><u>785,312,902</u></b>	<b><u>848,292,953</u></b>	<b><u>967,686,232</u></b>	<b><u>783,962,668</u></b>	<b><u>809,196,551</u></b>
<b>ANNUAL AVERAGE REVENUE PER CUSTOMER</b>					
Residential	\$ 1,255	\$ 1,110	\$ 1,071	\$ 889	\$ 898
General service	5,799	5,206	4,946	4,588	4,618
Industrial	449,265	283,827	263,169	245,650	430,049
Irrigation and frost control	2,375	2,268	1,782	1,615	1,930
Street lighting	6,839	6,447	5,928	6,036	6,046
Sales for resale	1,283,068	588,613	3,370,764	1,160,381	1,399,628
Telecommunications	138,570	110,329	97,764	91,061	85,403
<b>Total annual average revenue per customer</b>	<b><u>\$ 2,272</u></b>	<b><u>\$ 1,984</u></b>	<b><u>\$ 2,037</u></b>	<b><u>\$ 1,788</u></b>	<b><u>\$ 1,763</u></b>
<b>AVERAGE ANNUAL kWh PER CUSTOMER</b>					
Residential	17,261	17,037	19,213	17,183	18,543
General service	88,558	85,552	85,503	83,432	87,091
Industrial	7,839,280	5,145,928	5,285,330	5,400,547	10,233,757
Irrigation and frost control	46,334	48,751	45,706	45,070	56,030
Street lighting	68,187	64,746	64,756	63,817	63,173
<b>Total annual average kWh per customer</b>	<b><u>28,531</u></b>	<b><u>27,998</u></b>	<b><u>29,608</u></b>	<b><u>27,728</u></b>	<b><u>30,913</u></b>

**PUBLIC UTILITY DISTRICT NO. 1 OF OKANOGAN COUNTY, WASHINGTON**  
**OTHER FINANCIAL DATA (Unaudited)**

	Years Ended December 31,				
	2013	2012	2011	2010	2009
<b>COST OF POWER</b>					
Bonneville Power Administration	\$ 15,235,772	\$ 15,407,149	\$ 17,100,497	\$ 17,357,446	\$ 14,602,775
Douglas County PUD - Wells Hydroelectric Project	3,646,318	3,551,725	3,593,090	3,143,054	3,483,584
Energy NW - Nine Canyon Wind Project	3,008,055	3,029,067	3,060,855	2,963,835	2,953,233
Other cost of power, including market purchases	1,644,075	1,210,869	1,106,157	1,037,466	1,294,978
<b>Total cost of purchased power</b>	<b>\$ 23,534,220</b>	<b>\$ 23,198,810</b>	<b>\$ 24,860,599</b>	<b>\$ 24,501,801</b>	<b>\$ 22,334,570</b>
<b>ENERGY RESOURCES MWh</b>					
Bonneville Power Administration	472,322	509,404	605,088	530,461	549,191
Douglas County PUD - Wells Hydroelectric Project	296,743	319,040	313,857	228,442	242,781
Energy NW - Nine Canyon Wind Project	37,724	43,321	44,620	37,178	38,961
Other cost of power, including market purchases	20,975	13,587	10,816	11,545	22,101
<b>Total energy resources MWh</b>	<b>827,764</b>	<b>885,352</b>	<b>974,381</b>	<b>807,626</b>	<b>853,034</b>
<b>AVERAGE COST PER MWh</b>					
Bonneville Power Administration	\$ 32.26	\$ 30.25	\$ 28.26	\$ 32.72	\$ 26.59
Douglas County PUD - Wells Hydroelectric Project	12.29	11.13	11.45	13.76	14.35
Energy NW - Nine Canyon Wind Project	79.74	69.92	68.60	79.72	75.80
Other cost of power, including market purchases	78.38	89.12	102.27	89.86	58.59
<b>Average cost per MWh (all resources)</b>	<b>\$ 28.43</b>	<b>\$ 26.20</b>	<b>\$ 25.51</b>	<b>\$ 30.34</b>	<b>\$ 26.18</b>
<b>PEAK DEMAND MW</b>	<b>-</b>	<b>154</b>	<b>149</b>	<b>155</b>	<b>166</b>
<b>NET UTILITY PLANT</b>	<b>\$ 106,028,834</b>	<b>\$ 97,967,535</b>	<b>\$ 97,967,535</b>	<b>\$ 88,003,113</b>	<b>\$ 75,506,178</b>
<b>EMPLOYEE DATA</b>					
Full-time employees	90	92	90	91	91
Part-time employees	2	2	2	4	4
<b>Total employees</b>	<b>92</b>	<b>94</b>	<b>92</b>	<b>95</b>	<b>95</b>