Annual Report

Public Utility District No.1 of Pend Oreille County

CONT

Our Mission

Quality service at low cost.

Vision

"To Be Valued as a Trusted and Respected Public Utility District Providing the Services our Rural Communities Need at a Competitive Value in Order to Improve the Quality of Life for Generations to Come."

Values

Safety and Health

Must share a personal and professional commitment to protecting the safety and health of our customers, our employees, and our contractors in order to ensure a reliable workforce and an educated community.

Customer Focus

Must believe in respecting our employees and customers, listening to their requests and understanding their needs. Strive to exceed their expectations with regard to reliable service and affordable cost.

Community

Must help and improve the communities where we live and work. Promote the development of sustainable structures through collaborative working and volunteering.

Integrity

Must be guided by what is ethical and right and fulfill all commitments as a responsible steward of public assets and trust. Must foster open and honest communications, listen, and understand other perspectives.

Teamwork

Must value diversity and draw strength from the wealth of viewpoints that reside within the District. Must work together; demonstrate collaboration through mutual reliability, openness, empowerment, growth and flexibility. Unite the District and its departments.

Decisiveness

Must timely make hard choices and necessary changes based on the best interests of the District without partiality.

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About us

Pend Oreille Public Utility District was established in 1936 and began operations in 1948. The PUD is governed by three locally elected Commissioners. A General Manager and staff operate the utility within policies set by the Board of Commissioners.

The PUD has four operating systems: The electric system distributes electricity to the county, the production system produces power from the Box Canyon Hydroelectric Project, the water system consists of nine individual water distribution subdivisions, and the community network system provides wholesale broadband communication services.

PREPARING FOR THE FUTURE

A Message to Our Stakeholders

Pend Oreille PUD has been preparing for the future over the last few years and 2017 was no exception. Our 2017 strategic plan illuminated our age-old mission of “Quality Service at Low Cost” as a responsibility to provide services at a competitive value in order to improve the quality of life for the next generation. To continue that legacy we have remained focused on keeping power rates low through prudent financial practices, while also collaborating on economic development efforts, improving our system reliability and building reserves.

The strategic plan, which you will see laced throughout this report, really forms the backbone for our long-range preparations. It lays out the guiding vision for this utility, solidifies our core values, and provides a set of clear goals for financial reserves, customer service, and safety. Our outstanding management team worked together with guidance from the Commission to prepare the plan and ultimately supported it with multi-year planning documents from each department. The ambitious planning roadmap set the stage for a year of many accomplishments as this report demonstrates. A few highlights include:

Safety

The number one core value of the PUD remains a commitment to protecting the safety and health of our customers and employees. While we have always recognized the hazards associated with our various utility services, we know we can always do more to support our safety culture. To date, we have filled out our safety team with two additional experts. They have reformatted our safety meetings and trainings, developed a more robust Safety Committee, and rolled out an incident-reporting tool online. The goal is to create a culture that facilitates open dialogues about hazards and swift corrective actions to mitigate potential accidents. We believe it is our paramount duty as a small rural utility to set the example for safety in our community and industry.

> **“We believe it is our paramount duty as a small rural utility to set the example for safety in our community and industry.”**

Box Canyon Fish Ladder

As part of the Box Canyon license and settlement agreement, the PUD was required to install a series of fishways at the dam and other project works to facilitate the safe passage of certain target species of fish. The upstream fish passage facility is the first major in-water construction project at Box Canyon Dam since the original 1950's construction. 2017 marked the second year of the roughly $36 million project that includes several enterances that lead to raceways, an elevator and a orting facility. The project has had challenges, but is currently on schedule for completion in October 2018. The PUD is working with key stakeholders to identify alternatives to construction any future passage facilities that may yield better conservation outcomes.

LED Project

In February, the PUD began the conversion of 1600 high-pressure sodium yard and street lights to LED. Through multi-departmental coordination the project was successfully completed in June. The replacement project was primarily funded with BPA conservation dollars as well as a Relight Washington grant from the Transportation Improvement Board of Washington. This project met several of our strategic goals: safety as line crews are able to reduce the amount of time working up on a pole, customer service through reduced customer bills and better quality light, and financial prudence as it reduces our long-term maintenance costs.

Community Network Systems Hookup

2017 marked the seven-year anniversary since the PUD was awarded the American Recovery and Reinvestment Act grant that allowed for the expansion of the existing fiber optic backbone system to individual homes and businesses in southern part of Pend Oreille County. Customer count and wholesale revenues have steadily increased year after year with operating expenses remaining level. This success is attributable to the dedication of our incredible CNS team, the support of our retail service providers, and the loyalty of our customers. This investment continues to be the foundation for all economic development efforts in the county and has improved the quality of life for our customers. We look to continue this steady progress as we prepare for the future.

"This investment continues to be the foundation for all economic development efforts in the county and has improved the quality of life for our customers."

As you can see, the work achieved in 2017 will provide the spring-board for opportunities in the future. Thank you for your continued support and allowing us to be our customers' trusted utility partner.

Curt Knapp
Vice President

Dan Peterson
President

Rick Larson
Secretary

F. Colin Willenbrcok
General Manager

2017 HIGHLIGHTS

Retail Customers

Electric

9,135

Fiber end-users

1,849

Wireless end-users

56

Water customers

593

Residential Energy Rate

Service Availability Charge

$29.50

Energy Usage Charge

$0.0511/kWh

Average Residential Rate

$0.0689/kWh

Sales Statistics

Electric (MWh)

1,000,441

Peak Demand (MW)

166

Water (Gallons)

32,355,362

Calispell Power Plant

– 0.75 MW nameplate capacity
– 2 Generators
– 2,830 MWh Generated
– Mill Rate: $24 per MW

Box Canyon Hydroelectric Project

– 90 MW nameplate capacity
– 4 Kaplan Generators
– 359,364 MWh Generated
– Mill Rate: $51 per MW

LED Project

– 1,428 lights repaired
– Project Cost: $700,000
– Grants Received: $390,000
– Monthly rate to customers decreased due to reduced usage and maintenance costs.

Report of Independent Auditors
and Combined Financial Statements
with Supplemental Information

Public Utility District No. 1
of Pend Oreille County, Washington

December 31, 2017 and 2016

MOSSADAMS

Report of Independent Auditors

The Board of Commissioners
Public Utility District No. 1 of Pend Oreille County
Newport, Washington

Report on the Financial Statements

We have audited the accompanying financial statements of Public Utility District No. 1 of Pend Oreille County, Washington (the District), which comprise the combined statements of net position as of December 31, 2017 and 2016, the individual statements of net position of the Electric, Box Canyon Production, Water, and Community Network Systems as of December 31, 2017, the related combined statements of revenues, expenses, and changes in net position and cash flows for the years ended December 31, 2017 and 2016, and the individual statements of revenues, expenses, and changes in net position and cash flows for the Electric, Box Canyon Production, Water, and Community Network Systems for the year ended December 31, 2017, 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 opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

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, 2017 and 2016, 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, schedule of proportionate share of net pension liability, and schedule of employer contributions, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us 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 taken as a whole. The supplemental schedules of Electric System - revenue, customer, and energy statistics, Electric System - senior lien parity debt service coverage, and Box Canyon Production System - senior lien parity debt service coverage, as listed in the table of contents, are presented for purposes of additional analysis and are not required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and, accordingly, we express no opinion on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 19, 2018, on our consideration of Public Utility District No. 1 of Pend Oreille County's Electric, Box Canyon Production, Water, and Community Network Systems' 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 solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's 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.

Moss Adams LLP

Everett, Washington
March 19, 2018

The financial management of Public Utility District No. 1 of Pend Oreille County, Washington (the District) offers readers of these financial statements this overview and summary analysis of the financial activities of the District for the years ended December 31, 2017, 2016 and 2015. This discussion and analysis is designed to be used in conjunction with the financial statements and notes, which follow this section.

Overview of the Financial Statements

The financial section of the annual report includes the report of independent auditors, management's discussion and analysis, basic financial statements with accompanying notes, and supplemental information (unaudited).

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

The District's reporting entity consists of four primary component units, or operating systems. The Electric System distributes electricity to residential and other consumers in Pend Oreille County. The Box Canyon Production System produces hydroelectric power from the Box Canyon Hydroelectric Project. The Water System consists of nine individual water distribution subdivisions. The Community Network System supplies wholesale broadband communication services. The financial statements are reported in a combined format, meaning that each of the primary component units is reported in a columnar approach, which are combined into a District-wide total.

The combined statements of net position present information on the District's assets and liabilities and provide information regarding the nature and amount of resource investment (assets) and obligations incurred in the pursuit of such resources. These statements also provide a vehicle for evaluating the capital structure of the District and assessing liquidity and financial flexibility of the District.

The combined statements of revenues, expenses, and changes in net position report revenues and expenses, as well as change in net position for this period. These statements provide a measurement of the District's operations, help to evaluate the level of cost recovery from charges for products and services, and can be used as a partial determinant of creditworthiness.

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

The notes to the combined financial statements provide additional information that is essential to a full understanding of the financial statements, as described above, and are an integral part thereof.

Financial Analysis

Combined Statements of Net Position as of December 31

	2017	2016	2015
Assets			
Current assets	$ 81,142,445	$ 75,883,135	$ 87,238,853
Other assets	10,805,932	11,451,190	12,005,275
Net utility plant	259,010,507	252,895,896	245,511,712
Total assets	350,958,884	340,230,221	344,755,840
Deferred outflows of resources	330,916	1,360,726	975,597
Total assets and deferred outflows of resources	$ 351,289,800	$ 341,590,947	$ 345,731,437
Liabilities			
Current liabilities	$ 34,130,595	$ 21,795,642	$ 22,883,524
Other liabilities	39,485,494	42,792,159	42,430,416
Long-term debt	136,524,040	138,818,919	146,317,824
Total liabilities	210,140,129	203,406,720	211,631,764
Deferred inflows of resources	1,021,265	163,213	1,701,856
Net position			
Net investment in capital assets	110,609,842	110,020,257	112,887,459
Restricted	23,926,125	23,339,136	22,302,888
Unrestricted	5,592,439	4,661,621	(2,792,530)
Total net position	140,128,406	138,021,014	132,397,817
Total liabilities, deferred inflows of resources and net position	$ 351,289,800	$ 341,590,947	$ 345,731,437

The District's working capital decreased $7,075,643 during 2017, from a balance of $54,087,493 as of December 31, 2016 to a balance of $47,011,850 as of December 31, 2017. The decrease in working capital is primarily due to an increase in liabilities resulting from a line of credit with draws of $10,136,909 as of December 31, 2017. Draws on the line of credit began in 2017 to finance upstream fish passage construction costs for the Box Canyon Production system. The line of credit expires in September 2018 and is classified as a current liability. Costs accumulated in the line will be refunded through a revenue bond issuance expected in 2018. Working capital as of December 31, 2015 was $64,355,329, a decrease from 2015 to 2016 of $10,267,836, the majority of which is attributable to $13.5 million of construction funds used for the upstream fish passage facility during 2016.

The District had the following major capital asset expenditures during 2017, 2016 and 2015:

Acquisition and Construction of Capital Assets	2017	2016	2015
Box Canyon upstream fish passage construction	$ 12,491,301	$ 13,688,971	$ 369,975
Electric System distribution line construction	827,325	1,682,597	1,861,011
Community Network System broadband installations	451,586	285,228	224,007
All other	3,140,927	2,170,941	5,483,645
Total Capital Asset Additions	$ 16,911,139	$ 17,827,737	$ 7,938,638

Depreciation for 2017 was $10,053,969, down slightly from $10,178,021 in 2016. Depreciation in 2015 was $9,954,201.

Deferred outflows of resources primarily include pension-related items, which fluctuate based on the District's proportionate share of Washington State's Public Employees' Retirement System cost sharing pension plan activities. The District's deferred inflows balances also consist of pension plan activities.

Other liabilities include the District's net pension liability, which was $6,209,573 as of December 31, 2017, $9,059,751 as of December 31, 2016, and $8,131,776 as of December 31, 2015. Remaining costs of unearned revenue, licensing costs liability, and contract security remained fairly consistent from 2015 through 2017.

The District made debt principal payments of $5,056,638, $8,186,768, and $5,586,638 during 2017, 2016, and 2015, respectively. Payments made in 2016 included an additional $2,270,000 principal payment to pay off the 2005B Electric System bonds. The District issued a $3,500,000 bond for the Community Network System during 2017, using the funds to partially pay an intersystem loan between the Community Network System and the Box Canyon Production System. The remaining balance of the intersystem loan is eliminated upon consolidation.

Summary of Financial Condition

During 2017, the District's overall financial position improved. Total net position for the District increased $2,107,392 from $138,021,014 in 2016 to $140,128,406 in 2017.

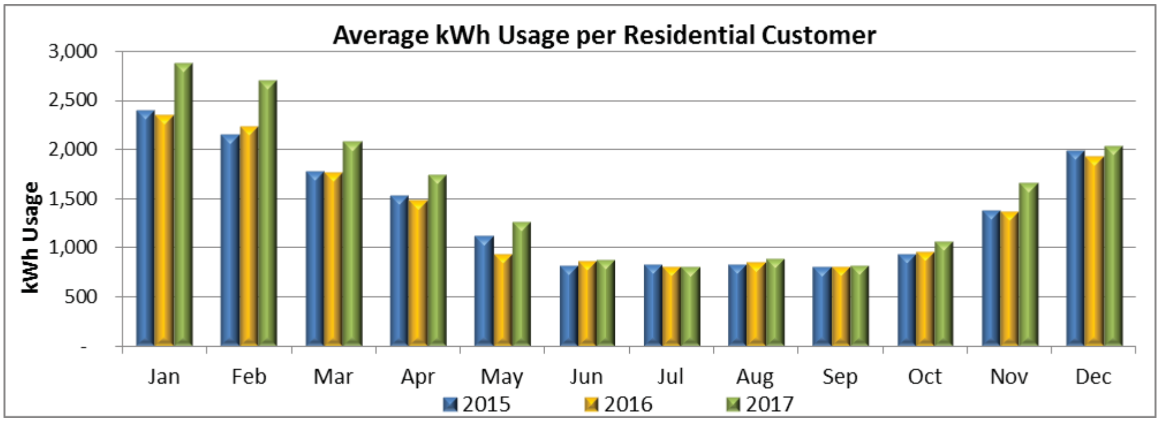
Electric System Operating Results

Electric System Change in Net Position	2017	2016	2015
Electric operating revenues			
Ponderay Newsprint Company	$ 28,858,279	$ 29,327,800	$ 23,769,699
Other retail customers	16,668,278	14,757,332	14,069,985
Sales to other utilities	1,937,010	1,492,120	5,789,699
All other	1,365,594	1,481,474	871,584
Total operating revenues	48,829,161	47,058,726	44,500,967
Electric operating expenses			
Power costs	29,703,975	25,916,023	28,121,024
All other	18,197,077	15,831,873	16,151,123
Total operating expenses	47,901,052	41,747,896	44,272,147
Net operating revenues	928,109	5,310,830	228,820
Nonoperating revenue (expenses)	(904,865)	(861,091)	1,894,943
Change in net position	$ 23,244	$ 4,449,739	$ 2,123,763
Debt Service Coverage	2.11x	2.36x	1.32x

Operating Revenues

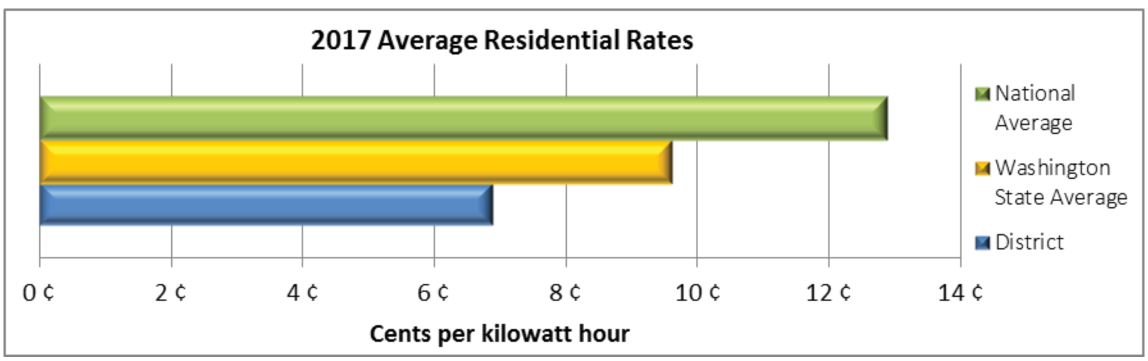
Ponderay Newsprint Company is the District's largest customer, representing 72% of the District's retail energy usage in 2017 with 724,990 megawatts of consumption, compared to 699,447 and 580,993 megawatts in 2016 and 2015, respectively. Ponderay Newsprint Company operated at a reduced capacity through October 2015, but has been at relatively full power consumption since November 2015. Ponderay Newsprint Company's billings are based on contractually agreed actual cost of service methodology rather than under a rate schedule. Accordingly, the billings increase or decrease in direct relation to the District's power supply costs. Further, Ponderay Newsprint Company receives credit for the majority of the District's wholesale power sales to other utilities; therefore, its billings decrease when sales to other utilities increase, and vice versa. The District and Ponderay Newsprint Company have been engaged in litigation surrounding a contract dispute since early 2016. Despite litigation procedures through 2016 and 2017, the operations between the two parties have remained unchanged. The District and Ponderay Newsprint Company settled the dispute in February 2018, ceasing all related litigation proceedings.

A long, cold winter resulted in higher than expected revenues from the District's electric customers during 2017. The following chart shows the comparative average residential energy usage by month for the past three years.



The District concluded the year approximately $1.38 million over budgeted revenues for retail customers excluding Ponderay Newsprint Company. The District implemented a mid-year 1% energy rate increase tied to the cost of power received from Seattle City Light's Boundary Hydroelectric project, raising the residential kilowatt hour charge from 5.08 cents per kilowatt hour to 5.11 cents. The District had increased the monthly service fee charge in July of 2016 by $5 per month, resulting in a residential monthly service fee of $29.50. The District has experienced an average residential customer growth rate of 1% in 2017, 2016, and 2015 with a total average customer count in 2017 across all classes of 9,135 meters.

At a blended rate of 6.89 cents per kilowatt hour, the District's residential rates are among the lowest in the state and the nation. The following chart shows the District's retail rate compared with other utilities across the nation.



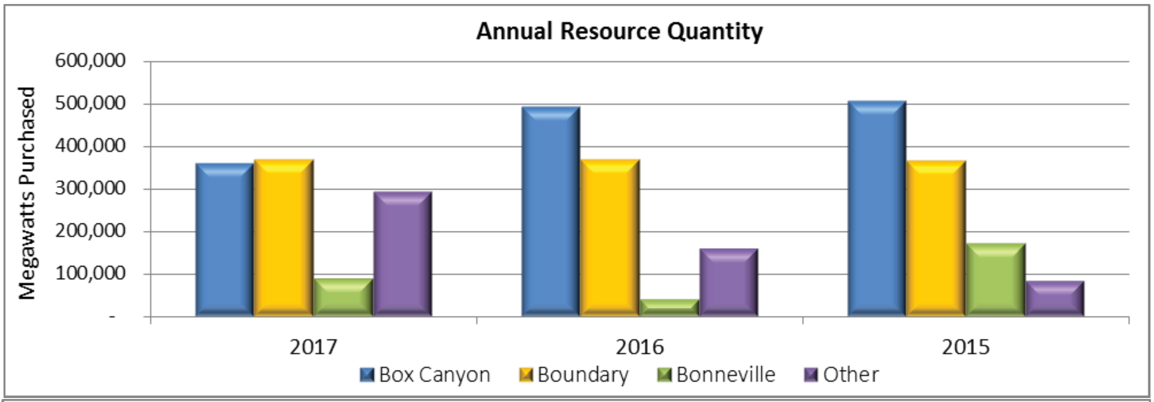
Energy Resources and Power Costs

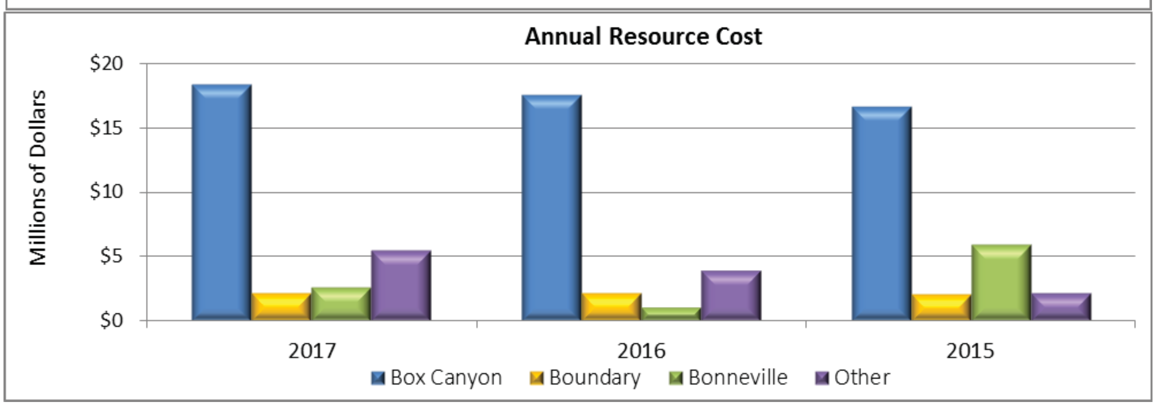
The District's largest power source is the Box Canyon Hydroelectric Project. The cost of power produced from this facility has increased significantly over the last decade, due largely to debt service costs associated with upgrading Box Canyon's four turbines and associated auxiliary components. The cost of generating Box Canyon power averaged $51 per megawatt in 2017, significantly higher than $36 per megawatt hour in 2016, and $33 in 2015, due to Pend Oreille River water levels in 2017. Box Canyon Production System costs are discussed in a later section of this report.

The District receives 48 megawatts of power capacity from the City of Seattle's Boundary Hydroelectric Project. At approximately $6 per megawatt hour in 2017, power received from the Boundary Hydroelectric Project is the District's most inexpensive power source and a key component of the District's low customer rates.

Power obtained from the Bonneville Power Administration cost $31 per megawatt hour in 2017, $29 per megawatt hour in 2016, and $35 in 2015. The District received an average of 26 megawatts from Bonneville through September 2015, which was reduced to 5.5 megawatts beginning in October 2015, and averaged 4.5 megawatts in 2016. Bonneville's average energy allocation increased with the beginning of their fiscal year on October 1, 2017 to an average allocation of 25 megawatts, resulting in 10.1 average megawatts received during 2017. Energy is delivered in monthly block amounts that are shaped to the District's load.

Other energy resources include costs to operate the Calispell Powerhouse, which produces less than 1 megawatt per hour; market power purchases necessary to balance resources to customer load; and power marketed under contract for the Kalispel Tribe.





Debt Service Coverage

The debt service coverage ratio measures cash flow from operations in comparison to annual debt service. In September 2016, the District called the Electric System 2005B bonds, and therefore only the 2010 bond debt remains outstanding for the Electric System. The District also funded a rate stabilization account during 2016, the funds of which may be classified as revenue for debt service coverage purposes in the event that the District's net operating revenues are insufficient to meet that year's debt service coverage bond covenant ratio of 1.25. The funding for this account moves cash from unrestricted to restricted; there is no deferred revenue associated with this account and it is used only for the calculation of debt service coverage. The District transferred $4.3 million into this account for the year ended December 31, 2016, and $300,000 for the year ended December 31, 2017. Net revenues available for debt service for both years is reduced by the same amount. Including the reduction in revenues available for debt service, the District's 2017 and 2016 debt service coverage ratio was 2.11 and 2.36. The 2015 debt service coverage ratio was 1.32.

The District's bonds are currently rated by Moody's Investor Services and Fitch Ratings, which have assigned ratings to the District's bonds of Baa1 and A-, respectively. Moody's Investor Services downgraded the District from an A3 rating to Baa1 as a result of depressed market prices and increased risk surrounding Ponderay Newsprint Company and its stability. Both Services have assigned a negative outlook.

Box Canyon Production System Operating Results

Box Canyon Production System Change in Net Position

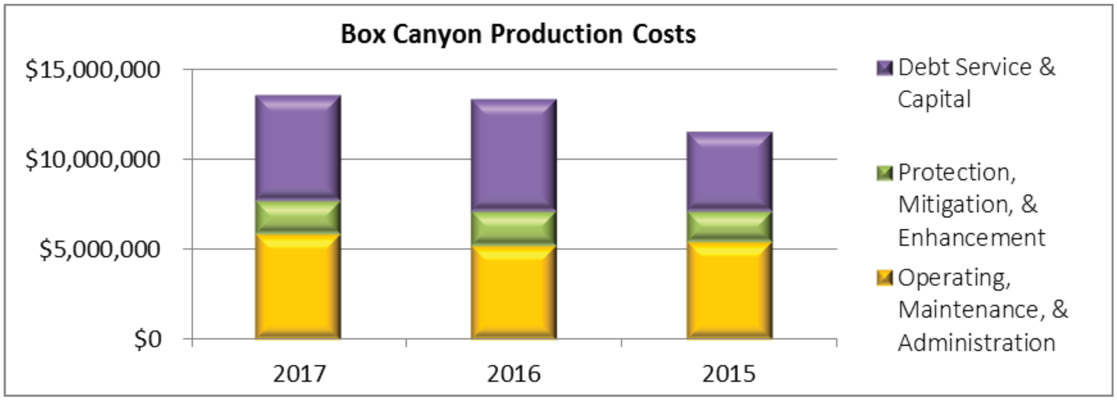
	2017	2016	2015
Production operating revenues			
Sales to Electric System	$ 18,643,961	$ 17,834,725	$ 16,887,358
All other	4,800	36,197	15,214
Total operating revenues	18,648,761	17,870,922	16,902,572
Production operating expenses	11,133,114	10,706,638	11,023,524
Net operating revenues	7,515,647	7,164,284	5,879,048
Nonoperating revenue (expenses)	(4,048,343)	(4,563,054)	(5,094,799)
Change in net position	$ 3,467,304	$ 2,601,230	$ 784,249
Debt Service Coverage	1.22x	1.19x	1.03x

Revenues for the Box Canyon Production System are calculated based on the cash expenditures to operate the Project. This includes labor and materials required to run the facility, expenditures for environmental work related to the reservoir behind the Project, principal and interest on Box Canyon's debt service, and payments for capital expenditures.

A significant cost component of Box Canyon power is debt service costs from borrowings for the upgrade of the turbines and auxiliary systems for the Project. The upgrade was included in Box Canyon's FERC license, renewed in 2005, and offers environmental mitigation as well as increased generation due to turbine blade configuration. The District is also currently constructing a FERC license mandated upstream fish ladder facility at Box Canyon. Once final financing is secured for upstream fish passage construction, expected in 2018, costs for the Box Canyon Hydroelectric Project are expected to remain level for several years. The Box Canyon Project nameplate capacity has increased from 72 megawatts to 90 megawatts due to turbine upgrade work.

Included in operating expenses for the Production System is environmental work being performed as required by FERC licensing conditions. The type and expense of environmental work will vary from year to year and consists of cultural studies, historical education, stream rehabilitation projects, recreation and wildlife projects, and water quality programs on the Pend Oreille River. Other costs, such as operations, maintenance, and administrative costs, have been relatively consistent from 2015 to 2017.

Nonoperating expenses include interest expense, net of allowance for funds used during construction (AFUDC).



Because the Box Canyon Hydroelectric System receives revenue from the Electric System sufficient to cover operating costs, including debt service and a component for capital spending, the normal senior lien debt service ratio will be slightly over 1.0x. The ratio will only be significantly above 1.0 during years the District elects to finance significant capital project work through current rates as opposed to debt financing.

Water System Operating Results

Water System Change in Net Position

	2017	2016	2015
Water System operating revenues			
Sales to retail customers	$ 453,874	$ 415,293	$ 423,677
All other	18,399	16,499	16,605
Total operating revenues	472,273	431,792	440,282
Water operating expenses	600,106	594,137	624,093
Net operating revenues (expenses)	(127,833)	(162,345)	(183,811)
Nonoperating revenue (expenses)	(3,495)	20,830	(5,242)
Change in net position	$ (131,328)	$ (141,515)	$ (189,053)

The District operates nine separate water systems throughout Pend Oreille County. The District is contractually obligated to maintain separate and distinct rates for each water system that reflect the individual system's costs. The majority of the variations in the preceding table are normal variations. Grant revenues of $25,322 are included in nonoperating revenue for 2016. The grant revenue for 2016 was received and used for a feasibility study regarding the possible acquisition of an existing water system within the County.

Community Network System Operating Results

Community Network System Change in Net Position

	2017	2016	2015
Community Network operating revenue			
Sales to retail customers	$ 1,956,820	$ 1,783,687	$ 1,499,803
Intersystem sales	281,616	276,344	276,944
All other	210,302	146,791	158,909
Total operating revenues	2,448,738	2,206,822	1,935,656
Community Network operating expenses	3,575,314	3,554,419	3,697,382
Net operating revenues (expenses)	(1,126,576)	(1,347,597)	(1,761,726)
Nonoperating revenue (expenses)	(125,252)	61,338	(8,768)
Change in net position	$ (1,251,828)	$ (1,286,259)	$ (1,770,494)

After receiving an American Recovery and Reinvestment Act grant in 2010, the District expanded its existing fiber backbone system with construction of fiber to individual homes and businesses in the southern part of Pend Oreille County. Per Washington State law, the District is authorized to be a wholesale provider of broadband, and serves residential end users through three local retail internet service providers. Standard class end users grew an average of almost 18% in both 2016 and 2017, with 1,957 end users as of December 31, 2017.

Prior to the fiber to the home buildout, the Community Network System sales were made solely to businesses. Revenues for this product in 2017, 2016, and 2015 were $979,736, $956,058, and $934,903, respectively. Intersystem sales are services provided for the internal benefit of the District itself. Other revenue includes contributed capital and miscellaneous revenues, which can vary based on new customer service requirements.

Operating expenses include operations and maintenance to maintain the fiber optic line and related equipment, labor, and contracts for control and intertie services. Depreciation, which is included in operating expenses, was $2,559,666, $2,522,121, and $2,479,053, for 2017, 2016, and 2015, respectively.

Other Significant Matters

A description of currently known facts, decisions, and conditions that are expected to have a significant effect on future financial position or results of operations follows.

Ponderay Newsprint Company - District contracts with Ponderay Newsprint Company expire in 2027. The District has no notice from Ponderay Newsprint Company of any plans to cease operations; however, the condition exists that the District has additional business risk from an unusually high concentration of sales to a single entity. The rate impact from a loss of Ponderay Newsprint Company sales could be significant to the District, cannot be accurately forecasted, and depends upon the interaction of many factors, including but not limited to then-existing cost of production of Box Canyon Project power, cost of acquisition of Bonneville power, and market or resale value of this power.

Contacting the District's Financial Management

The financial report is designed to provide interested parties with a general overview of the District's finances and to demonstrate District accountability for the money it receives. For any questions about this report, or for additional or clarifying financial information, contact the District's financial department as set forth on the last page of this Annual Report under Organizational Information—Corporate Office.

April D. Owen, CPA
Director of Finance

COMBINED STATEMENTS OF NET POSITION

Assets and Deferred Outflows of Resources	Electric System	Box Canyon Production System	Water System	Community Network System	Combined Total as of December 31, 2017	2016
Current Assets						
Cash and cash equivalents	$ 7,189,191	$ 17,194,935	$ -	$ 111,339	$ 24,495,465	$ 20,078,096
Restricted cash and cash equivalents	17,988,071	7,268,954	-	232,660	25,489,685	35,664,107
Restricted short-term investments	12,115,300	11,746,001	-	-	23,861,301	13,631,203
Receivables						
Accounts and contracts, net	2,853,376	-	19,183	180,210	3,052,769	1,912,715
Other	240,767	202,795	-	19,902	463,464	412,433
Unbilled revenue	955,673	-	-	-	955,673	1,033,936
Materials and supplies	1,612,693	-	45,092	779,140	2,436,925	2,646,615
Prepaid expenses and other	350,264	36,899	-	-	387,163	504,030
Due from other systems	29,677	205,938	-	-	-	-
Total current assets	43,335,012	36,655,522	64,275	1,323,251	81,142,445	75,883,135
Noncurrent Assets						
Contracts and notes receivable	3,438,953	-	-	-	-	387
Nonutility plant	5,261,298	-	-	-	5,261,298	5,433,075
Licensing costs - regulatory asset	-	5,544,634	-	-	5,544,634	6,017,728
Long-term intersystem investment	-	783,521	-	-	-	-
Total noncurrent assets	8,700,251	6,328,155	-	-	10,805,932	11,451,190
Utility Plant						
Land and land rights	3,434,602	789,950	77,305	61,721	4,363,578	4,503,220
Hydroelectric plant and equipment	1,526,930	148,658,752	-	-	150,185,682	149,239,243
Structures, buildings and equipment	114,990,519	-	8,667,306	43,714,195	167,372,020	165,460,450
Intangible assets	724,004	13,250,547	742	-	13,975,293	13,951,084
Construction work in progress	1,620,362	32,694,750	-	156,975	34,472,087	21,360,853
	122,296,417	195,393,999	8,745,353	43,932,891	370,368,660	354,514,850
Less accumulated depreciation and amortization	63,747,287	30,643,069	3,637,123	13,330,674	111,358,153	101,618,954
Net utility plant	58,549,130	164,750,930	5,108,230	30,602,217	259,010,507	252,895,896
Total assets	110,584,393	207,734,607	5,172,505	31,925,468	350,958,884	340,230,221
Deferred Outflows of Resources						
Loss on refinancing debt	2,056	-	-	-	2,056	6,224
Deferred pension outflows	205,202	100,125	5,599	17,934	328,860	1,354,502
Total deferred outflows of resources	207,258	100,125	5,599	17,934	330,916	1,360,726
Total assets and deferred outflows of resources	$ 110,791,651	$ 207,834,732	$ 5,178,104	$ 31,943,402	$ 351,289,800	$ 341,590,947

COMBINED STATEMENTS OF NET POSITION

Liabilities, Deferred Inflows of Resources, and Net Position	Electric System	Box Canyon Production System	Water System	Community Network System	Combined Total as of December 31, 2017	2016
Current Liabilities						
Accounts payable	$ 5,419,734	$ 4,281,838	$ -	$ -	$ 9,701,572	$ 7,836,820
Accrued compensation and benefits	1,815,773	-	-	-	1,815,773	1,785,049
Accrued taxes	940,929	76,903	1,851	7,710	1,027,393	1,117,965
Customer prepayments and deposits	895,123	-	4,317	255,106	1,154,546	866,135
Accrued bond interest	345,875	3,577,702	698	64,660	3,988,935	4,019,786
Short-term note payable	-	10,136,909	-	-	10,136,909	-
Current portion of long-term debt	1,383,333	3,780,714	37,592	523,938	5,519,639	5,056,638
Current portion of licensing cost liability and unearned revenue	-	736,240	-	49,588	785,828	1,113,249
Due to other systems	-	-	16,344	13,333	-	-
Total current liabilities	10,800,767	22,590,306	60,802	914,335	34,130,595	21,795,642
Other Liabilities						
Unearned revenue	11,153,855	-	-	3,928,283	11,736,518	11,765,171
Licensing costs liability	-	5,544,634	-	-	5,544,634	6,017,728
Contract security liability	10,114,769	5,880,000	-	-	15,994,769	15,949,509
Net pension liability	3,874,646	1,890,548	105,724	338,655	6,209,573	9,059,751
Total other liabilities	25,143,270	13,315,182	105,724	4,266,938	39,485,494	42,792,159
Long-term Debt						
Revenue bonds	12,490,508	120,827,600	-	3,798,521	136,333,108	138,577,062
Other long-term debt	93,333	-	97,599	-	190,932	241,857
Due to other systems	-	-	-	93,333	-	-
Total long-term debt	12,583,841	120,827,600	97,599	3,891,854	136,524,040	138,818,919
Total liabilities	48,527,878	156,733,088	264,125	9,073,127	210,140,129	203,406,720
Deferred Inflows of Resources						
Deferred pension inflows	637,248	310,931	17,389	55,697	1,021,265	163,213
Total deferred inflows of resources	637,248	310,931	17,389	55,697	1,021,265	163,213
Net Position						
Net investment in capital assets	49,432,317	30,005,707	4,973,039	26,198,779	110,609,842	110,020,257
Restricted for						
Sullivan contract obligation	518,341	-	-	-	518,341	494,323
Debt service	3,370,531	15,437,253	-	-	18,807,784	18,544,813
Rate stabilization fund	4,600,000	-	-	-	4,600,000	4,300,000
Total restricted	8,488,872	15,437,253	-	-	23,926,125	23,339,136
Unrestricted	3,705,336	5,347,753	(76,449)	(3,384,201)	5,592,439	4,661,621
Total net position	61,626,525	50,790,713	4,896,590	22,814,578	140,128,406	138,021,014
Total liabilities, deferred inflows of resources, and net position	$ 110,791,651	$ 207,834,732	$ 5,178,104	$ 31,943,402	$ 351,289,800	$ 341,590,947

See accompanying notes.

COMBINED STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

Combined Statements of Revenue, Expenses, and Changes in Net Position						
		Box Canyon		Community	Combined Total	
	Electric	Production	Water	Network	December 31,	
	System	System	System	System	2017	2016
Operating Revenues						
Sales to retail customers						
Ponderay Newsprint Company	$ 28,858,279	$ -	$ -	$ -	$ 28,858,279	$ 29,327,800
Other retail customers	16,668,278	-	453,874	1,956,820	19,078,972	16,956,312
Sales to other utilities	1,937,010	-	-	-	1,937,010	1,492,120
Intersystem sales	184,772	18,643,961	-	281,616	-	-
Contributed capital	594,270	-	7,225	155,121	756,616	597,650
Other	586,552	4,800	11,174	55,181	421,491	688,121
Total operating revenues	48,829,161	18,648,761	472,273	2,448,738	51,052,368	49,062,003
Operating Expenses						
Power costs	29,703,975	230,834	-	-	11,290,848	8,207,308
Operations and maintenance	6,701,580	5,098,649	262,487	847,959	12,497,665	11,413,043
Administrative and general	5,981,079	2,364,448	123,225	188,790	8,367,948	6,665,791
Taxes	2,481,606	82,786	23,075	31,608	2,619,075	2,668,953
Pension expense (credit)	(603,067)	(294,253)	(16,455)	(52,709)	(966,484)	(1,036,284)
Depreciation and amortization	3,635,879	3,650,650	207,774	2,559,666	10,053,969	10,178,021
Total operating expenses	47,901,052	11,133,114	600,106	3,575,314	43,863,021	38,096,832
Net operating revenues (expenses)	928,109	7,515,647	(127,833)	(1,126,576)	7,189,347	10,965,171
Nonoperating Revenues (Expenses)						
Interest income	79,439	258,371	917	308	296,771	261,225
Interest on debt	(647,466)	(7,101,269)	(3,433)	(125,445)	(7,836,443)	(7,992,969)
Subsidies on debt	-	1,939,311	-	-	1,939,311	1,985,749
AFUDC interest	-	924,965	-	-	924,965	432,582
Grant revenues	-	-	-	-	-	110,158
Sullivan net expense	(126,824)	-	-	-	(126,824)	(171,521)
Other, net	(210,014)	(69,721)	(979)	(115)	(279,735)	32,802
Total nonoperating expenses	(904,865)	(4,048,343)	(3,495)	(125,252)	(5,081,955)	(5,341,974)
Change in net position	23,244	3,467,304	(131,328)	(1,251,828)	2,107,392	5,623,197
Accumulated Net Position						
Beginning of year	61,603,281	47,323,409	5,027,918	24,066,406	138,021,014	132,397,817
End of year	$ 61,626,525	$ 50,790,713	$ 4,896,590	$ 22,814,578	$ 140,128,406	$ 138,021,014

See accompanying note

COMBINED STATEMENTS OF CASH FLOWS

Combined Statements of Cash Flows	Electric System	Box Canyon Production System	Water System	Community Network System	Combined Total December 31, 2017	2016
Cash Flows from Operating Activities						
Receipts from customers	$ 45,344,900	$ -	$ 462,591	$ 2,256,344	$ 48,063,835	$ 45,057,767
Receipts from other operating revenues	2,210,357	4,800	-	-	2,215,157	2,047,909
Payments to suppliers for goods and services	(16,798,108)	(3,723,346)	(153,649)	(99,616)	(20,774,719)	(16,788,744)
Payments to employees for services	(7,530,217)	(3,622,168)	(199,170)	(694,744)	(12,046,299)	(11,165,945)
Payments to (from) other systems	(18,259,985)	18,266,039	(67,944)	61,890	-	-
Net cash from operating activities	4,966,947	10,925,325	41,828	1,523,874	17,457,974	19,150,987
Cash Flows from Noncapital Financing Activities						
Nonoperating asset						
Construction of long-term asset, net	-	-	-	-	-	185,482
Receipts from Sullivan revenues and contributions in aid	22,648	-	-	-	22,648	8,828,479
Intersystem financing	158,291	-	(62)	(158,229)	-	-
Net cash from noncapital financing activities	180,939	-	(62)	(158,229)	22,648	9,013,961
Cash Flows From Capital and Related Financing Activities						
Acquisition and construction of capital assets	(2,563,201)	(12,895,499)	(528)	(558,450)	(16,017,678)	(17,435,773)
Proceeds from sale of assets	390,818	3,600	-	11,745	406,163	46,120
Proceeds from grants	-	-	-	-	-	110,158
Proceeds from issuance of revenue bond	-	-	-	3,500,000	3,500,000	-
Proceeds from issuance of note payable	-	10,136,909	-	-	10,136,909	-
Change of deferred revenue	-	-	-	(49,588)	(49,588)	(129,002)
Payments on revenue bonds	(1,300,000)	(3,705,714)	-	(3,864,876)	(5,005,714)	(8,135,844)
Interest paid on revenue bonds	(724,251)	(7,223,853)	-	(60,785)	(7,948,103)	(8,302,982)
Subsidy received on revenue bonds	-	1,939,311	-	-	1,939,311	1,985,751
Scheduled payments on notes payable	(13,334)	-	(37,590)	-	(50,924)	(50,924)
Interest paid on notes payable	-	(69,721)	(3,648)	-	(73,369)	(4,505)
Net cash from capital and related financing activities	(4,209,968)	(11,814,967)	(41,766)	(1,021,954)	(13,162,993)	(31,917,001)
Cash Flows from Investing Activities						
Purchases of investments	(10,685,779)	(3,428,390)	-	-	(14,114,169)	(10,067,517)
Sales and maturities of investments	583,910	7,126,266	-	-	3,845,299	20,879,972
Interest on investments, contracts, and notes	94,839	159,826	-	308	194,188	139,295
Net cash from investing activities	(10,007,030)	3,857,702	-	308	(10,074,682)	10,951,750
Net Change in Cash and Cash Equivalents	(9,069,112)	2,968,060	-	343,999	(5,757,053)	7,199,697
Cash and Cash Equivalents						
Beginning of year	34,246,374	21,495,829	-	-	55,742,203	48,542,506
End of year	$ 25,177,262	$ 24,463,889	$ -	$ 343,999	$ 49,985,150	$ 55,742,203

See accompanying notes.

COMBINED STATEMENTS OF CASH FLOWS

Combined Statements of Cash Flows

	Electric System	Box Canyon Production System	Water System	Community Network System	Combined Total December 31, 2017	Combined Total December 31, 2016
Reconciliation of Net Operating Revenues (Expenses) to Cash Flows from Operating Activities						
Net operating revenues (expenses)	$ 928,109	$ 7,515,647	$ (127,833)	$ (1,126,576)	$ 7,189,347	$ 10,965,171
Adjustments to reconcile net operating revenues (expenses) to net cash from operating activities						
Depreciation and amortization	3,635,879	3,650,650	207,774	2,559,666	10,053,969	10,178,021
Changes in operating assets and liabilities						
Receivables	(1,266,709)	85,008	(1,511)	35,754	(1,147,458)	(464,988)
Unbilled revenue	78,263	-	-	-	78,263	(115,646)
Due to (from) other systems	149,263	-	(54,177)	(95,086)	-	-
Materials and supplies	295,843	3,266	1,022	114,369	414,500	(31,193)
Prepaid expenses and other current assets	58,317	11,626	-	-	69,943	(72,056)
Deferred relicensing costs	-	(327,421)	-	-	(327,421)	(135,711)
Pension	(941,610)	(27,020)	15,042	(12,896)	(966,484)	(1,035,600)
Accounts payable, customer deposits, and prepayments	2,067,420	41,886	1,426	42,431	2,153,163	(95,713)
Accrued compensation, benefits, and taxes	(37,828)	(28,317)	85	6,212	(59,848)	(41,298)
Net cash from operating activities	$ 4,966,947	$ 10,925,325	$ 41,828	$ 1,523,874	$ 17,457,974	$ 19,150,987

See accompanying notes.

NOTES TO COMBINED FINANCIAL STATEMENTS

Note 1 - Organization and Significant Accounting Policies

Organization - Public Utility District No. 1 of Pend Oreille County, Washington (the District) is a municipal corporation governed by an elected three-person board of commissioners. The District's reporting entity consists of four primary component units, or operating systems. The Electric System distributes electricity to residential and other consumers in Pend Oreille County. The Box Canyon Production System produces hydroelectric power from the Box Canyon Hydroelectric Project (the Box Canyon Project). The Water System consists of nine individual water distribution subdivisions. The Community Network System supplies wholesale broadband communication services. The District is required by various financing and contractual arrangements to report separately on each system and maintain each system as a separate entity with separate obligations.

As required by generally accepted accounting principles (GAAP), management has considered all potential component units in defining the reporting entity and has no component units.

Basis of accounting and presentation - The accounting policies of the District conform to GAAP as applicable to proprietary funds of governments. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The District has applied all applicable GASB pronouncements. Accounting records are maintained in accordance with methods prescribed by the State Auditor under the authority of the Revised Code of Washington, Chapter 43.09; the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission (FERC) for the Electric System, Box Canyon Production System, and Community Network System; and the Uniform System of Accounts for Class C Water Utilities prescribed by the National Association of Regulatory Utility Commissioners for the Water System.

System columns presented in the financial statements do not sum to the combined totals due to the elimination of certain intersystem transactions. These transactions relate to intersystem power and broadband sales and purchases, loan balances and interest on intersystem loans, and intersystem administrative charges.

A summary of other significant accounting policies used in the preparation of the combined financial statements follows.

New accounting standards - In June 2015, the GASB issued Statement No. 75, *Financial Reporting for Postemployment Benefits Other Than Pensions,* to improve the usefulness of information about postemployment benefits other than pensions included in the financial statements. This statement is effective for financial statements for fiscal years beginning after June 15, 2017. The District is evaluating the impact of this statement on its combined financial statements.

In March 2016, the GASB issued Statement No. 82, *Pension Issues – An Amendment of GASB Statements No. 67, No. 68, and No. 73.* This statement addresses issues regarding the presentation of payroll-related measures, classification of payments made by employers to satisfy employee contribution requirements, and deviations from guidance in an Actuarial Standard of Practice. The District adopted this statement in 2017.

In November 2016, the GASB issued Statement No. 83, *Certain Asset Retirement Obligations,* which addresses valuation and disclosure of asset retirement obligations. The statement is effective for financial statements for fiscal years beginning after June 15, 2018. The District is evaluating the impact of this statement on its combined financial statements.

In January 2017, the GASB issued Statement No. 84, *Fiduciary Activities*, which clarifies when a government entity has a fiduciary responsibility and is required to present fiduciary fund financial statements. The statement is effective for financial statements for fiscal years beginning after December 15, 2018. The District is evaluating the impact of this statement on its combined financial statements.

In January 2017, the GASB issued Statement No. 86, *Certain Debt Extinguishment Issues*, which addresses the defeasance of debt using a government entities' existing resources. The statement is effective for financial statements for fiscal years beginning after June 15, 2017. The District is evaluating the impact of this statement on its combined financial statements.

In June 2017, the GASB issued Statement No. 87, *Leases*, which establishes revised standards on lease accounting and financial reporting. The statement is effective for financial statements for fiscal years beginning after December 15, 2019. The District is evaluating the impact of this statement on its combined financial statements.

Revenue recognition and unbilled revenue - The Electric System, Water System, and Community Network System recognize revenue as earned on a monthly basis based on rates established by the District's board of commissioners and, for the Electric System, in accordance with power sales contracts with Ponderay Newsprint Company (Note 5). The District estimates unbilled revenues for energy delivered to customers between their last respective meter reading date and December 31, and records that amount as unbilled revenue for the current year. The Box Canyon Production System recognizes revenue on a cost-of-service basis from sales to the Electric System.

Allowance for uncollectible accounts - Management reviews accounts receivable on a regular basis to determine whether any receivables will potentially be uncollectible. The allowance for uncollectible accounts includes amounts estimated through an evaluation of specific accounts, based on the best available facts and circumstances of customers who may be unable to meet their financial obligations, and a reserve based on historical experience. The reserve amount for the years ended December 31, 2017 and 2016 was $21,000 for each year.

Cash and cash equivalents - For purposes of the combined statements of cash flows, the District considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Restricted cash and investments - Restricted cash and investments are amounts designated by a third party for a specific purpose (Note 2). Examples of these assets include amounts held to pay debt service, bond funds designated for construction, and deposits made by vendors.

Investments - The District records investments at fair value based on quoted market rates, with changes in unrealized gains and losses reported as investment income.

Materials and supplies - Materials and supplies are recorded at average cost.

Utility plant - Utility plant assets are stated at cost, including an allowance for funds used during construction (AFUDC). Betterments and major renewals over $2,000 are capitalized, whereas maintenance and repairs are charged to operations as incurred. Depreciation is determined by the straight-line method over the estimated useful lives of the related assets, which range from 5 to 50 years. Composite rates are used for asset group depreciation, and, accordingly, no gain or loss is recorded on the disposition of an asset unless it represents a large and unusual retirement.

Nonutility plant - Nonutility plant represents capital assets that do not directly relate to the District's primary business purposes (Note 8).

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. The payments are initially recorded as liabilities, and then reclassified to operating revenue (contributed capital) when the associated facilities are constructed or acquired.

Licensing costs liability - Certain Box Canyon FERC licensing conditions require payments to various outside entities for projects and operating costs that will not be directed by, or controlled by, the District. The District has estimated and present valued these payments over the 50-year license and recorded them as a regulatory asset and licensing costs liability.

The District has not recorded the future costs of the remaining expenses related to license implementation that will be capitalized or expensed, as may be appropriate, when incurred.

Unamortized bond discounts and premiums - Unamortized bond discounts and premiums are amortized to interest expense, using the effective interest method, over the term of the bonds (Note 4). The excess of costs incurred over the carrying value of bonds refunded on early extinguishment of debt is amortized to expense over the shorter of the remaining life of the old bonds or the life of the new issue and recorded as deferred outflows of resources.

Unearned revenue - In August 2000, the District entered into an agreement with Seattle City Light concerning a cost-sharing arrangement for building fiber optic communications capability in Pend Oreille County. Among other terms and conditions, the District retained ownership of all constructed network assets with a commitment to grant Seattle City Light a 30-year right-of-use for 8 to 12 dark fiber strands along the District's network backbone. Seattle City Light made a one-time, lump-sum payment of $1,487,650 under the agreement. The District recorded this payment as unearned revenue and is amortizing the balance to Community Network System revenue on a straight-line basis over the 30-year life of the agreement. The unamortized balance was $632,251 and $681,839 as of December 31, 2017 and 2016, respectively. Also, the Community Network System unearned revenue includes an Electric System $4.25 million prepayment for future broadband services. Funds from the Electric System were used by the Community Network System as the matching cash requirement of an American Recovery and Reinvestment Act grant. The unamortized balance associated with this payment was $3,345,620 and $3,490,400 as of December 31, 2017 and 2016, respectively.

In June 2013, the District signed a Memorandum of Agreement between the District and the State of Washington Department of Ecology Office of Columbia River that committed the District to release water from Sullivan Lake according to predetermined periods and amounts to allow for improved water access for communities along the Columbia River. In exchange, the Office of Columbia River agreed to pay the District $14 million in installments over the first 3 years of an expected 30-year agreement (Note 8). The District received the final installment of $9.0 million in February 2016. Funds received were recorded as unearned revenue, and are being recognized as nonoperating revenue in an amount equal to the net cash outflow for Sullivan Project-related activities each year. The unamortized balance as of December 31, 2017 and 2016 was $11,153,855 and $11,132,920, respectively.

Net investment in capital assets - This component of net position consists of capital assets, net of accumulated depreciation; borrowed monies not yet spent, as held in restricted construction and acquisition funds; and outstanding debt balances related to the purchase or construction of capital assets.

Restricted net position - Amounts presented as restricted net position are constrained by provisions imposed by external parties and cannot be used for normal operations. Balances currently classified as restricted include bond principal and interest due for the upcoming year, less unfunded accrued interest; construction and acquisition funds net of the unspent portion of debt proceeds; bond reserve funds; funds reserved for use in the event that the District loses a major source of revenue; and deposits made by major customers net of the deposit due to these customers.

Unrestricted net position - Amounts included as unrestricted net position do not meet the definition of either net investment in capital assets or restricted net position, and are used for normal operations.

Compensated absences - Employees accrue personal leave to be used for vacation, sick, and family leave purposes. Annual leave granted to each employee varies in accordance with years of service and may be carried forward from year to year, capped at a maximum bank of 1,200 hours for employees hired before April 2011 or 700 hours for employees hired after March 2011. The District records the cost of personal leave as earned, not as taken.

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 risks and uncertainties - The District is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include weather and natural-disaster-related disruptions; collective bargaining labor disputes; changing local and national economic conditions; fish and other Endangered Species Act issues; Environmental Protection Agency regulations; reliability standards issued by the North American Electric Reliability Corporation; federal government regulations or orders concerning the operation, maintenance, licensing, and license surrender of hydroelectric facilities; the financing and completion of significant capital projects; changing federal and state laws, regulations, and requirements; concentration risk in the form of sales to a major customer, Ponderay Newsprint Company, and related potential impact on District power contracts (Note 5); and market and credit risks inherent in buying and selling of power, a commodity with inelastic demand characteristics and minimal storage capability.

Reclassifications - Certain reclassifications may be made to the prior-year financial statement presentation to conform to the current-year presentation.

Note 2 - Cash and Investments

Cash and investments are recorded in accounts as required by the District's bond indentures. Restricted assets represent accounts that are restricted by bond covenants or third-party contractual agreements.

As of December 31, 2017, the District held the following cash and investments:

Cash, Cash Equivalents and Investments	Electric System	Box Canyon Production System	Water System	Community Network System	Combined Total as of December 31, 2017	Combined Total as of December 31, 2016
Cash and cash equivalents						
Cash deposits	$ 8,905,066	$ 9,066,244	$ -	$ 343,999	$ 18,315,309	$ 24,375,529
Local government investment pool	16,272,196	15,397,645	-	-	31,669,841	31,366,674
Total Cash and Cash Equivalents	25,177,262	24,463,889	-	343,999	49,985,150	55,742,203
Investments						
U.S. Treasuries, at market	12,115,300	11,746,001	-	-	23,861,301	13,631,203
Total Investments	12,115,300	11,746,001	-	-	23,861,301	13,631,203
Total Cash and Investments	$ 37,292,562	$ 36,209,890	$ -	$ 343,999	$ 73,846,451	$ 69,373,406

The table below reconciles the cash, cash equivalents and investments listed above to the combined statements of net position:

	Electric System	Box Canyon Production System	Water System	Community Network System	Combined Total As of December 31, 2017	Combined Total As of December 31, 2016
Cash and cash equivalents						
Unrestricted assets						
Revenue funds	$ 7,189,191	$ 17,194,935	$ -	$ 111,339	$ 24,495,465	$ 20,078,096
Restricted assets						
Bond principal and interest	1,715,875	7,268,954	-	232,660	9,217,489	8,932,483
Construction and acquisition	-	-	-	-	-	734,872
Contract obligation	11,672,196	-	-	-	11,672,196	11,627,243
Contract security	-	-	-	-	-	10,069,509
Rate stabilization	4,600,000	-	-	-	4,600,000	4,300,000
Restricted funds	17,988,071	7,268,954	-	232,660	25,489,685	35,664,107
Restricted short-term investments						
Bond reserve	2,000,531	11,746,001	-	-	13,746,532	13,631,203
Contract security	10,114,769	-	-	-	10,114,769	-
	12,115,300	11,746,001	-	-	23,861,301	13,631,203
Total funds	$ 37,292,562	$ 36,209,890	$ -	$ 343,999	$ 73,846,451	$ 69,373,406

Interest rate risk - The District's investment policy limits investment maturities to less than five years from the date of purchase unless authorized by the General Manager and Director of Finance for a specific purpose. During 2017 and 2016, investments were held in federal agency securities, federal treasuries, or in the State Treasurer's Local Government Investment Pool (LGIP), described more fully in the following paragraph.

Credit risk - In accordance with the Revised Code of Washington, District bond resolutions, and District internal investment policies, all investments are direct obligations of the U.S. government, deposits in the LGIP, or deposits with financial institutions recognized as qualified public depositories of the state of Washington. U.S. government securities are held by bank trust departments as the District's agent and in the District's name.

The District's cash deposits are covered by the Federal Deposit Insurance Corporation (FDIC) or protected against loss by deposit with financial institutions recognized as qualified public depositories of the state of Washington under the guidelines of the Washington State Public Deposit Protection Commission (PDPC). The District intends to hold time deposits and securities until maturity.

Concentration of credit risk - District policies allow the entire portfolio to be invested in direct U.S. government guaranteed obligations or in the LGIP. No other investment may exceed half of portfolio market value. The LGIP, a 2a7-like pool as defined by GASB Statement No. 31 and the Securities and Exchange Commission, invests in high-quality, short-term investments and is administered by the State Treasurer. The LGIP weighted-average maturity must not exceed 90 days and no single investment may exceed 762 days in maturity. Withdrawals in excess of $10 million are available on a one-day notice. The LGIP comprehensive annual financial report is available on the State Treasurer's website at: https://tre.wa.gov.

Custodial credit risk - The District's deposits are held by public depositories authorized by the PDPC and are not subject to custodial credit risk because state law requires public depositories to fully collateralize their public entity deposits.

Bond principal and interest accounts - For each debt issue, the District is required by bond resolutions to maintain principal and/or sinking fund and interest accounts within the bond funds to provide for the next semi-annual interest and annual principal/sinking fund payments falling due, which are reported as current assets. All bond funds are restricted by bond resolution to the payment of debt service obligations.

Bond reserve funds - Box Canyon Production System and Electric System revenue bond resolutions require that reserve accounts be maintained within the bond funds. The 2010 reserve accounts require a deposit equal to 125% of the average annual debt service outstanding on each respective bond. The 2009 and 2012 reserve accounts require deposits equal to the maximum amount of principal and interest falling due in any single bond year. All deposits are currently held in federal treasuries and money market cash accounts.

Construction and acquisition fund - Proceeds from the 2009, 2010, and 2012 bond issuances were deposited into separate Box Canyon Production System Construction and Acquisition Funds and are restricted to expenditures for the replacement of the Box Canyon Project turbines, plant modernization efforts, and other capital improvements to the Box Canyon Production System.

Contract obligation - The District is obligated through a Memorandum of Agreement to release water from Sullivan Lake. In exchange, the District has received funds from the Office of Columbia River (Note 8). Monies received are restricted to construction and operations and maintenance activities related to Sullivan Lake and associated facilities.

Contract security - As discussed in Note 5, the Ponderay Newsprint Company has elected to post a $10 million contract security in lieu of a letter of credit. The contract security is subject to contractual provisions and the District's investment policy and, as of December 31, 2017 and 2016, was invested in a bank trust department deposit subject to PDPC protection.

Rate stabilization – The District's bond resolutions allow for the creation of a rate stabilization account within the District's revenue funds to affect the calculation of the District's bond debt service coverage covenant requirement. Monies deposited into the account are subtracted from net revenues used in the calculation of debt service coverage in the year deposited, and are added to net revenues in years that money is withdrawn from the account. The District deposited $300,000 and $4,300,000 into the rate stabilization account for the years ended December 31, 2017 and 2016, respectively.

Investments – The District holds investments that are measured at fair value as of December 31, 2017 and 2016. The District categorized its fair value measurements within the fair value hierarchy established by GAAP. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets, level 2 inputs are significant other observable inputs, and level 3 inputs are significant unobservable inputs. Investments in an external government investment pool, such as LGIP, are not subject to reporting within the level hierarchy.

Investments Measured at Fair Value as of December 31, 2017 and 2016

	Total as of December 31, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level				
Money market funds	$ 9,924,991	$ -	$ 9,924,991	$ -
U.S. agency securities				
U.S. government and agency obligations	9,943,350	-	9,943,350	-
Federal National Mortgage Association	1,992,820	-	1,992,820	-
Federal Home Loan Banks	2,000,140	-	2,000,140	-
	$ 23,861,301	$ -	$ 23,861,301	$ -

	Total as of December 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level				
Money market funds	$ 5,620,163	$ -	$ 5,620,163	$ -
U.S. agency securities				
U.S. government and agency obligations	2,007,160	-	2,007,160	-
Federal National Mortgage Association	4,002,780	-	4,002,780	-
Federal Home Loan Banks	2,001,100	-	2,001,100	-
	$ 13,631,203	$ -	$ 13,631,203	$ -

Note 3 - Utility Plant

The following changes occurred in the District's utility plant for the years ended December 31, 2017 and 2016:

Changes in Utility Plant	2016 Balance	Additions	Retirements/ Transfers	2017 Balance
Land and land rights	$ 4,503,220	$ 1	$ (139,643)	$ 4,363,578
Hydroelectric plant and equipment	149,239,243	174,672	771,767	150,185,682
Structures, buildings, and equipment	165,460,450	571,295	1,340,275	167,372,020
Intangible assets	13,951,084	24,209	-	13,975,293
Construction work in progress	21,360,853	16,140,962	(3,029,728)	34,472,087
	354,514,850	16,911,139	(1,057,329)	370,368,660
Less accumulated depreciation and amortization	101,618,954	10,053,969	(314,770)	111,358,153
Net Utility Plant	$ 252,895,896	$ 6,857,170	$ (742,559)	$ 259,010,507

	2015 Balance	Additions	Retirements/ Transfers	2016 Balance
Land and land rights	$ 4,277,970	$ 225,250	$ -	$ 4,503,220
Hydroelectric plant and equipment	148,755,208	3,981	480,054	149,239,243
Structures, buildings, and equipment	162,896,921	321,621	2,241,908	165,460,450
Intangible assets	13,842,000	-	109,084	13,951,084
Construction work in progress	7,448,861	17,276,885	(3,364,893)	21,360,853
	337,220,960	17,827,737	(533,847)	354,514,850
Less accumulated depreciation and amortization	91,709,248	10,178,021	(268,315)	101,618,954
Net Utility Plant	$ 245,511,712	$ 7,649,716	$ (265,532)	$ 252,895,896

The District capitalized to utility plant, as an intangible asset, costs associated with seeking the current Box Canyon Project FERC license, including legal fees for continuing litigation of various license conditions. The District is amortizing the balance of the intangible asset over the 50-year term of the license. Originally capitalized relicensing costs were $12,472,232, with accumulated amortization of $3,019,765 and $2,768,258 as of December 31, 2017 and 2016, respectively.

Note 4 - Long-Term Debt

Electric System - In February 2005, the Community Economic Revitalization Board (CERB) awarded the District a $200,000 loan for construction of communication infrastructure projects. This loan carries no interest, and principal payments were deferred for the first five years. Annual principal payments of $13,333 began in 2011 and will end in 2026. The loan covenants include a junior lien pledge of Electric System revenues, and, as such, this loan remains as Electric System debt; however, the associated communication infrastructure has been transferred to the Community Network System, which assumed the obligation to reimburse the Electric System for the debt service payments.

In November 2005, the District issued $13,240,000 Series A (subject to alternative minimum tax) and $5,430,000 Series B (tax exempt) revenue bonds to refund bonds originally issued in 1996. The District fully paid the Series A bonds in 2013 and paid the remaining $2,270,000 principal amount of the Series B bonds in September 2016, more than a year ahead of the final principal due date of January 1, 2018. There are no outstanding balances for these bond series as of December 31, 2017 and 2016.

In November 2010, the District issued $20,745,000 tax exempt Electric System revenue and refunding bonds. Proceeds from the bonds were used to repay revenue bond anticipation notes for a transmission line build, provide funds for additional Electric System capital work, fund the reserve account, and refund the 1998 Electric System revenue bonds. The net present value of the savings on refunding was approximately $264,720. The 2010 bonds consist of $9,710,000 of serial bonds that accrue interest at 4.00% to 5.00%, maturing in annual installments from January 1, 2012, through January 1, 2019, and $11,035,000 in term bonds maturing in annual sinking fund installments from January 1, 2020, to January 1, 2031. The loss from refinancing has an unamortized balance of $2,056 and $6,224 as of December 31, 2017 and 2016, respectively, which is amortized using the effective interest method over the remaining life of these bonds.

The bonds are recorded in the combined statements of net position net of unamortized premium of $25,508 and $73,960 as of December 31, 2017 and 2016, respectively.

Box Canyon Production System - In November 2008, the District issued a $1,340,000 Clean Renewable Energy Tax Credit Bond (CREB) to assist in the financing of the Box Canyon turbine upgrade project. CREB purchasers are eligible for a credit against their federal income tax. The bond carries an interest rate of 1.35% and provides for equal annual principal payments in the amount of $95,714. The bond matures in December 2021.

In October 2009, the District issued $21,295,000 Series A (tax exempt) and $49,015,000 Series B (taxable Build America Bonds - Direct Payment) Box Canyon Production System revenue bonds to provide initial financing for turbine replacement and plant upgrades for the Box Canyon Project. The Series A bonds mature in annual installments from January 1, 2011, through January 1, 2024, and accrue interest at a coupon rate of 5.00%. The true interest cost of the Series A bonds is 4.19%. The Series B bonds are term bonds maturing in annual sinking fund installments from January 1, 2025, through January 1, 2040. Interest rates on the Series B bonds range from 6.85% to 7.35%, but are subject to a subsidy payment from the federal government. This subsidy was 35% of the interest rate at the date of issuance, but has reduced to 32.6% as a result of federal sequestration. The bonds are reported in the combined statements of net position net of unamortized premium of $212,976 and $295,221 as of December 31, 2017 and 2016, respectively.

In November 2010, the District issued $34,110,000 tax exempt revenue bonds to partially fund turbine capital improvements and other plant modernizations at Box Canyon Hydroelectric Project. The 2010 bonds consist of term bonds that accrue interest at 5.25% and 5.75% and mature in annual sinking fund installments from January 1, 2030, through January 1, 2041. The bonds are reported in the combined statements of net position net of unamortized discount of $358,241 and $369,702 as of December 31, 2017 and 2016, respectively.

In October 2012, the District issued $38,000,000 taxable new Clean Renewable Energy Bonds - Direct Payment to complete the funding for turbine improvements and other plant modernizations at Box Canyon Hydroelectric Project. The District receives a credit against annual interest payments, payable by the United States Treasury, equal to approximately 70% of the interest due. This credit was also reduced due to federal sequestration beginning in 2013, resulting in a credit of approximately 65%. The 2012 bonds consist of $26,550,000 in series bonds maturing in annual installments from January 1, 2013, to January 1, 2025, and an $11,450,000 term bond maturing in annual sinking fund installments from January 1, 2026, to January 1, 2030. Interest rates on the series bonds range from 0.834% to 4.571%, but with the federal subsidy result in rates from 0.000% to 1.805%. The term bond has an interest rate of 5.000%, but net of the federal subsidy is 2.234%. The bonds are reported in the combined statements of net position net of unamortized discount of $144,279 and $155,274 as of December 31, 2017 and 2016, respectively.

In December 2016, the District issued a Box Canyon Production System Revenue Bond Anticipation Note with a bank in an amount not to exceed $20,000,000. In October 2017, the District extended the maturity date from December 13, 2017 to September 30, 2018. Similar to a line of credit, draws are made on the note for expenditures related to upstream fish passage work at Box Canyon Hydroelectric Project. The note is expected to be repaid by the issuance of revenue bonds during 2018. Interest accrues at 65% of LIBOR plus 1.35% and is payable monthly. As of December 31, 2017 draws on the Bond Anticipation Note were $10,136,909.

Water System - In 2000, the Sunvale Subdivision of the Water System received a loan for $189,607 from the State of Washington Department of Community, Trade, and Economic Development to finance the construction of new wells and distribution line. The fixed interest rate is 2.5% for a term of 20 years. Annual principal payments in the amount of $9,979 are due through October 2020.

In 2001, the State of Washington Department of Community, Trade, and Economic Development authorized a $400,070 loan to the Riverbend Subdivision of the Water System to finance system improvements, with a fixed interest rate of 2.5%. Annual principal payments in the amount of $22,018 are due through October 2020.

In July 2003, the District executed a State of Washington Public Works Board loan agreement for the Granite Shores Subdivision of the Water System, enabling a $70,551 loan to be repaid over 20 years at 1% interest. The loan financed certain system improvements, including drilling a new well. Annual principal repayments of $3,713 began in October 2005 and will end in October 2023. Subsequently, in March 2006, the District secured an additional loan with the State of Washington Public Works Board for $35,717 to cover the remaining costs of drilling the new well. The second loan also carries a 1% interest rate. Annual principal payments in the amount of $1,880 are due through October 2026.

Community Network System - During 2010, the Box Canyon Production System loaned the Community Network System $2.5 million to provide liquidity for operations while the Community Network System expanded the broadband communications infrastructure. In 2013, this loan was refunded with a new $5.25 million loan from the Box Canyon Production System. The loan is recorded as an investment by the Box Canyon Production System and accrues interest at the monthly LGIP investment rate net of administrative fees, which was an average of 0.96% for the year ended December 31, 2017. Monthly principal payments began on December 31, 2013, and are due through November 30, 2033. The balance outstanding as of December 31, 2017 is $989,459.

In May 2017, the District issued a $3,500,000 Community Network System Revenue Bond with a bank to partially repay the 2010 Box Canyon Production System loan. The bonds mature in six-month installments from July 1, 2017, through January 1, 2027, and accrue interest at a coupon rate of 3.88%.

Changes in Long-Term Debt

	2016 Balance	Additions	Reductions	2017 Balance*	Due within One Year*
Revenue bonds, face amount	$ 143,738,571	$ 3,500,000	$ 5,172,714	$ 142,065,857	$ 5,468,714
Unamortized bond premium	369,182	-	130,698	238,484	-
Unamortized bond discount	(524,977)	-	(22,458)	(502,519)	-
Other long term debt	292,781	-	50,924	241,857	50,925
Total Debt	$ 143,875,557	$ 3,500,000	$ 5,331,878	$ 142,043,679	$ 5,519,639

	2015 Balance	Additions	Reductions	2016 Balance*	Due within One Year*
Revenue bonds, face amount	$ 151,684,285	$ -	$ 7,945,714	$ 143,738,571	$ 5,005,714
Unamortized bond premium	562,744	-	193,562	369,182	-
Unamortized bond discount	(546,274)	-	(21,297)	(524,977)	-
Other long term debt	343,706	-	50,925	292,781	50,924
Total Debt	$ 152,044,461	$ -	$ 8,168,904	$ 143,875,557	$ 5,056,638

**Intercompany debt transactions have been eliminated for combined presentation*

Scheduled Maturities and Interest on Long-term Debt

	Electric System	Box Canyon Production System	Water System	Community Network System	Combined*
Principal					
2018	$ 1,383,333	$ 3,780,714	$ 37,592	$ 523,938	$ 5,519,639
2019	1,443,333	3,855,714	37,591	520,328	5,642,638
2020	708,333	3,935,714	37,591	540,061	4,998,639
2021	743,333	4,030,715	5,593	564,148	5,111,641
2022	778,333	4,040,000	5,595	440,579	5,166,928
2023-2027	4,470,000	22,060,000	11,229	1,717,000	28,258,229
2028-2032	4,415,000	25,460,000	-	-	29,875,000
2033-2037	-	31,145,000	-	-	31,145,000
2038-2041	-	26,590,000	-	-	26,590,000
	$ 13,941,665	$ 124,897,857	$ 135,191	$ 4,306,054	$ 142,307,714
Interest					
2018	$ 657,500	$ 7,091,861	$ 2,791	$ 182,226	$ 7,878,213
2019	587,500	6,949,440	1,936	167,556	7,652,948
2020	534,375	6,796,314	1,080	152,778	7,433,852
2021	498,750	6,632,588	224	137,440	7,221,209
2022	461,375	6,458,610	168	95,698	6,996,822
2023-2027	1,679,500	29,128,031	225	170,836	30,978,592
2028-2032	454,875	22,166,378	-	-	22,621,253
2033-2037	-	13,454,232	-	-	13,454,232
2038-2042	-	2,946,375	-	-	2,946,375
	$ 4,873,875	$ 101,623,829	$ 6,424	$ 906,534	$ 107,183,496

**Intercompany debt transactions have been eliminated for combined presentation*

Note 5 - Power Purchase Contractual Agreements

Ponderay Newsprint Company - In July 1986, the Electric System entered into power sales contracts with Ponderay Newsprint Company (PNC) to supply power to a fiber mill and paper plant. The District is obligated to provide all power necessary to operate both the fiber mill and paper plant. Power delivery under these contracts expires in 2027. In 2017, approximately 72% of Electric System retail energy deliveries and 66% of retail energy sale revenues were to PNC.

To fulfill this power commitment, the District delivers power from the Box Canyon Project and acquires power at cost from the Boundary Project as discussed later in this note. Power is also obtained from the Bonneville Power Administration (BPA) and other suppliers under various power purchase contracts. PNC is billed based upon the District's actual cost of service, as contractually defined, rather than under an industrial rate schedule.

PNC must provide the District $10 million in security, either in the form of a letter of credit or deposit, which the District may draw upon in the event that PNC defaults its obligations under the contracts. Cash deposits are in a District-held trust account, and draws may only be made at the District's request.

In December 2015, the District gave notice to PNC that it had breached its contractual obligations by submitting an improper power schedule. PNC disagreed, eventually filing suit against the District. Legal proceedings related to the dispute were ongoing through 2017, and were settled in February 2018, ceasing all current PNC related litigation.

The rate impact from a loss of PNC power sales cannot be forecasted accurately; it depends upon the interaction of many factors, including but not limited to existing cost of production of Box Canyon Project power, cost of acquisition of BPA and other power resources, and market or resale value of this power.

Seattle City Light - Boundary Hydroelectric Project - Seattle City Light owns and operates Boundary Hydroelectric Project (Boundary) located in northern Pend Oreille County. In Boundary's previous FERC license, the District was granted a licensed share of the Boundary Project equal to a 48-megawatt capacity. The Boundary Project was issued a new 42-year FERC license on March 20, 2013, in which the District was no longer granted a license share. During 2014, Seattle City Light and the District entered into a new agreement that extends the same operational parameters held under the previous license, including power deliveries capped at a 48-megawatt capacity and delivered at cost. The agreement term corresponds with Boundary's FERC license and expires in 2055.

Bonneville Power Administration - Effective October 1, 2011, the District renewed power purchase contracts with BPA for a 20-year period until September 30, 2028. At that time, the District received both Shaped Block purchases and Slice of the System purchases. Shaped Block purchases are predetermined monthly levels of power delivered consistently throughout the month.

The amount of power received varies from month to month, depending on the projected load levels and District power resources for each month. Slice of the System is a product wherein the District originally accepted 0.18668% of the base federal hydroelectric system, and paid equal costs thereof. In February 2013, BPA granted the District's request to make an early change to contract provisions and reduce the District's Slice of the System percentage to 0.0%, delivering all power allocation through Shaped Block purchases.

The risks and rewards associated with BPA purchases pass through to Ponderay Newsprint Company under the terms of the contracts with that customer. During 2014 and through September 2015, the District received an average of 26 megawatts of power from BPA. Due to historical reductions in Ponderay Newsprint Company load, BPA reduced the amount of power in October 2015 to an average of 5.5 megawatts through September 2016 and provided an average of 3.5 megawatts through September 2017. Due to Ponderay Newsprint Company's return to full production in 2016 and 2017, BPA recalculated the District's load allocation and will provide an average of 24.8 megawatts through September 2018. Future power allocations are dependent on the District's overall customer load.

Energy Northwest - The District is a participant in Energy Northwest's (formerly the Washington Public Power Supply System) Nuclear Project Nos. 1 and 3, both of which have terminated. The District purchased from Energy Northwest, and assigned to BPA, 0.087% of the capability of Project No. 1 and 0.078% of Energy Northwest's 70% ownership share of Project No. 3. Under the agreements, the District is unconditionally obligated to pay Energy Northwest its pro rata share of the total costs of the projects, including debt service, even though the projects are terminated. Under the Net Billing Agreements, BPA is responsible for assuming the District's cost obligation, and therefore the District had no direct payments in 2017 and 2016. The District's Electric System revenue requirements are not directly affected by the associated costs; revenue requirements are affected indirectly to the extent that the costs of the projects result in increases in BPA's wholesale power rates.

Note 6 – Pension Plans

The District is a member of the Washington State Public Employees' Retirement System (PERS) cost-sharing plan. For purposes of measuring the net pension liability, deferred outflows/inflows of resources, and pension expense, information about the fiduciary net position of the PERS and additions to/deductions from PERS' fiduciary net position have been determined on the same basis as they are reported by PERS. For this purpose, plan contributions are recognized as of employer payroll paid dates and benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Plan description - PERS was established in 1947 and its retirement benefit provisions are contained in Revised Code of Washington (RCW) chapters 41.34 and 41.40. PERS is a cost-sharing multiple-employer retirement system consisting of three separate pension plans for membership purposes. PERS Plan 1 and PERS Plan 2 are defined benefit plans, and PERS Plan 3 is a defined benefit plan with a defined contribution component. PERS members include elected officials, state employees, employees of local governments, and higher education employees not participating in higher education retirement programs.

PERS is composed of and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes. Pursuant to RCW 41.45.060, Washington State Department of Retirement Systems (DRS) will allocate a certain portion of employer contributions from Plan 2/3 to Plan 1 in order to fund its unfunded actuarially accrued liability (UAAL).

Benefits provided

PERS Plan 1 - Provides retirement, disability, and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service. The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service.

PERS Plan 1 retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. Other benefits include duty and nonduty disability payments, an optional cost-of-living adjustment (COLA), and a duty-related death benefit, if found eligible by the Department of Labor and Industries.

PERS Plan 2/3 - PERS Plan 2/3 provides retirement, disability, and death benefits. Retirement benefits for are determined as two percent of the member's AFC times the member's years of service for Plan 2 and one percent of AFC for Plan 3. The AFC is the monthly average of the member's 60 consecutive highest-paid service credit months. PERS Plan 2 members are vested after the completion of five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after 10 years of service or after five years of service if 12 months of that service was earned after age 44.

Members are eligible for retirement with a full benefit at 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by a factor that varies according to age for each year before age 65.

PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit. Plan 2/3 benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the Consumer Price Index), capped at three percent annually and a duty-related death benefit, if found eligible by the Department of Labor and Industries.

Contributions

PERS Plan 1 contributions - The PERS Plan 1 member contribution rate is established by statute at six percent. The employer contribution rate is developed by the Office of the State Actuary (OSA).

PERS Plan 2/3 contributions - The PERS Plan 2/3 employer and employee contribution rates are developed by OSA to fully fund Plan 2 and the defined benefit portion of Plan 3. The Plan 2/3 employer rates include a component to address the PERS Plan 1 unfunded actuarial accrued liability (UAAL).

Both plans include an administrative expense that is currently set at 0.18%. Required contribution rates (expressed as a percentage of covered payroll) at the close of fiscal year 2017 were as follows:

Local Governmental Units		
Actual Contribution Rates	Employer	Employee
PERS Plan1	11.18%	6.00%
PERS Plan 2/3	11.18%	6.12%
PERS Plan 3	11.18%	0%

Both the District and the employees made the required contributions during fiscal years 2017 and 2016. The District's required employer contributions for the years ended December 31 were as follows:

Required Employer Contributions	2017	2016
PERS Plan 1	$ 416,156	$ 412,225
PERS Plan 2/3	579,483	538,399
	$ 995,639	$ 950,624

Investments

The Washington State Investment Board (WSIB) has been authorized by statute as having investment management responsibility for the pension funds. The WSIB manages retirement fund assets to maximize return at a prudent level of risk.

Retirement funds are invested in the Commingled Trust Fund (CTF). The CTF is a diversified pool of investments that invests in fixed income, public equity, private equity, real estate and tangible assets. Investment decisions are made within the framework of a Strategic Asset Allocation Policy and a series of WSIB-adopted investment policies for the various asset classes.

For the fiscal year ended June 30, 2017, the annual money-weighted rate of return on PERS Plan 1 pension investments, net of pension plan investment expense, was 13.84%. This money-weighted rate of return expresses investment performance, net of pension plan investment expense, and reflects both the size and timing of cash flows. The annual money-weighted rate of return on PERS Plan 2/3 pension investments, net of pension plan investment expense, was 14.11%

Pension costs

The District reports a liability for its proportionate share of each plan's net pension liability. The net pension liability was measured as of June 30, 2017, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2016, rolled forward to June 30, 2017. The District's proportion of the net pension liability was based on the contributions received by PERS during the measurement period for employer payroll paid dates from July 1, 2016, through June 30, 2017, relative to the total employer contributions received from all of PERS' participating employers, as well as the statutorily required contributions required to fund the unfunded actuarial accrued liability. Below are the percentage proportionate shares of net pension liability, dollar value of each proportionate share of net pension liability, and the pension expense or credit recognized by the District for each respective plan.

Proportionate Share of Plan Liability				
		PERS Plan 1		PERS Plan 2/3
Percent share as of June 30,2017		0.067391%		0.086683%
Percent share as of June 30, 2016		0.076635%		0.098196%
Net pension liability as of December 31, 2017	$	3,197,754	$	3,011,819
Pension expense (credit) recognized as of December 31, 2017	$	(705,730)	$	(260,754)

At December 31, 2017, the District reported its proportionate share of deferred outflows of resources and deferred inflows of resources from the following sources:

District's Proportionate Share of Plan Deferred Outflows and Inflows of Resources	PERS Plan 1		PERS Plan 2/3	
	Deferred Outflows of Resources	Deferred Inflows of Resources	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	$ -	$ -	$ 305,168	$ (99,054)
Changes in actuarial assumptions	-	-	31,991	-
Difference between projected and actual investment earnings	-	(119,331)	-	(802,880)
Changes in proportion	-	-	(535,878)	-
Contributions paid to PERS subsequent to the measurement date	213,187	-	314,392	-
Difference between actual and proportionate employer contributions	-	-	-	-
	$ 213,187	$ (119,331)	$ 115,673	$ (901,934)

The $213,187 reported as deferred outflows of resources for PERS Plan 1 and $314,392 reported as deferred outflows of resources for PERS Plan 2/3 related to pensions resulting from the District's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability for the relevant plan in the year ending December 31, 2017. Other amounts reported as deferred outflows and inflows of resources related to each plan will be recognized in pension expense as follows:

Deferred Outflows and Inflows of Resources Recognized in Pension Expense	PERS Plan 1	PERS Plan 2/3
2018	$ (80,660)	$ (410,313)
2019	25,466	(38,910)
2020	(5,913)	(168,952)
2021	(58,224)	(390,183)
2022 and Thereafter	-	(92,295)
	$ (119,331)	$ (1,100,653)

Actuarial assumptions - The total pension liability for each of the plans was determined by an actuarial valuation as of June 30, 2016, with the results rolled forward to June 30, 2017, using the following actuarial assumptions applied to all prior periods included in the measurement:

Actuarial Assumptions	
Inflation	3.00% per year
Active Member payroll growth	3.75% per year
Investment rate of return	7.50%
Discount rate	7.50%

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

The actuarial assumptions used in the June 30, 2016 valuation were based on the results OSA's 2007-2012 Experience Study and the 2015 Economic Experience Study. Additional assumptions for subsequent events and law changes are current as of the 2016 actuarial valuation report.

OSA selected a 7.50% long-term expected rate of return on pension plan investments using a building-block method. In selecting this assumption, OSA reviewed the historical experience data, considered the historical conditions that produced past annual investment returns, and considered Capital Market Assumptions (CMAs) and simulated expected investment returns the WSIB provided.

The CMAs contain three pieces of information for each class of assets WSIB currently invests in:

- Expected annual return
- Standard deviation of the annual return
- Correlations between the annual returns of each asset class with every other asset class

WSIB uses the CMAs and their target asset allocation to simulate future investment returns at various future times.

The expected future rates of return (expected returns, net of pension plan investment expense, including inflation) are developed by the WSIB for each major asset class.

Best estimates of arithmetic real rates of return for each major asset class included in the pension plans' target asset allocation as of June 30, 2017, are summarized in the following table:

Estimated Rates of Return by Asset Class

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Fixed Income	20.00%	1.70%
Tangible Assets	5.00%	4.90%
Real Estate	15.00%	5.80%
Global Equity	37.00%	6.30%
Private Equity	23.00%	9.30%

The inflation component used to create the table is 2.2% and represents WSIB's most recent long-term estimate of broad economic inflation.

Discount rate - The discount rate used to measure the total pension liability was 7.50% for PERS Plan 1 and PERS Plan 2/3. To determine the discount rate, an asset sufficiency test was completed to test whether each pension plan's fiduciary net position was sufficient to make all projected future benefit payments of current plan members. Consistent with current law, the asset sufficiency test included an assumed 7.70% long-term discount rate to determine funding liabilities for calculating future contribution rate requirements. Consistent with the long-term expected rate of return, a 7.50% future investment rate of return on invested assets was assumed for the test.

Contributions from plan members and employers are assumed to continue being made at contractually required rates (including PERS Plans 2 and 3). Based on those assumptions, the pension plans' fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.50% was applied to determine the total pension liability.

Pension liability sensitivity - The following table presents the District's proportionate share of the net pension liability for all plans it participates in, calculated using the discount rate of 7.50%, as well as what the District's proportionate share of the net pension liability would be if it were calculated using a discount rate one percentage point lower (6.50%) or one percentage point higher (8.50%) than the current discount rate:

District's Proportionate Share of Net Pension Liability Sensitivity	1% Decrease in Discount Rate (6.50%)	Discount Rate (7.50%)	1% Increase in Discount Rate (8.50%)
Proportionate share of the PERS Plan 1 net pension liability	$ 3,895,477	$ 3,197,754	$ 2,593,379
Proportionate share of the PERS Plan 2/3 net pension liability (asset)	8,114,158	3,011,819	(1,168,789)

The pension liability has been allocated to the operating systems based on a percentage of total payroll charged to each system. The total pension liability for each system as of December 31, 2017, is as follows:

Proportionate Share of Plan Net Pension Liability	PERS Plan 1	PERS Plan 2/3	Total
Electric System	$ 1,995,332	$ 1,879,314	$ 3,874,646
Box Canyon Production System	973,580	916,968	1,890,548
Water System	54,445	51,279	105,724
Community Network System	174,397	164,258	338,655
	$ 3,197,754	$ 3,011,819	$ 6,209,573

Pension plan fiduciary net position - Detailed information about each defined benefit pension plan's fiduciary net position is available in a separately-issued DRS 2017 CAFR. The DRS CAFR may be obtained by writing to: Department of Retirement Systems, Communications Unit, P.O. Box 48380, Olympia WA 98504-8380; or it may be downloaded from the DRS website at www.drs.wa.gov.

Savings plans - In addition to PERS, the District maintains a deferred compensation plan, as well as two defined contribution plans, in accordance with the Internal Revenue Code Sections 457 and 401(a), respectively. All District employees are eligible to participate in the 457 plan and one of the two available 401(a) plans. The 401(a) plans provide for an employer match of 50% of eligible employee deferral of employee straight-time wages, capped at a 2% employer match on a 4% employee deferral.

Employer contributions for 2017 and 2016 were $145,899 and $151,400, respectively. All plan assets have been placed into trust for the exclusive benefit of plan participants and their beneficiaries and are, therefore, not reflected in the combined statements of net position.

The District maintains a Health Reimbursement Arrangement for employees. Non-bargaining-unit employees receive $175 monthly contribution paid into individual employer-sponsored medical savings accounts to pay for eligible medical expenses, tax-free, whether incurred while employed or after retirement. Bargaining unit employees are eligible for a $150 monthly contribution if they participate in District-sponsored wellness programs.

Other post-employment benefits - The District provides limited reimbursement for health care insurance premiums for retired employees. Employees age 50 or older that are retiring or voluntarily separating service are eligible to receive a contribution to the employee's Health Reimbursement Arrangement account. Employees separating service during 2016 received $3 times their years of service times the number of remaining months between the employee's 60th and 65th birthdays. Employees separating service during 2017 receive $2 times their years of service, and those separating service during 2018 receive $1 times their years of service, with the subsidy expiring January 1, 2019. The estimated liability for this benefit as of December 31, 2017 and 2016, is $5,953 and $4,368, respectively. The District has elected to finance this plan under a pay-as-you-go method, disbursing $2,491 and $17,092 for the years ended December 31, 2017 and 2016, respectively. There is no past service cost to be realized in future years.

Note 7 - Self-Insurance

Public Utility Risk Management Services - The District, along with 17 other public utility districts and one joint operating agency, is a member of the Public Utility Risk Management Services (PURMS) self-insurance fund. The program provides members with various liability, property, and health insurance coverages in three separate pools. The pools operate independently of one another. All members do not participate in all pools.

The District is a participant in the liability pool, which maintains a base self-insured retention level of $1 million, funded reserves ranging from $2.75 million to $3.25 million, and individual member deductibles of $250. The liability pool provides the District with shared excess coverage of $60 million general liability, $10 million cyber security liability coverage, and $35 million directors and officers liability.

The District is also a participant in the property pool, which maintains a self-insured retention level of $250,000, funded reserves ranging from $500,000 to $750,000, and varying deductibles of $250 on most property and $75,000 on the Box Canyon, Sullivan, and Calispell Hydroelectric Projects. The property pool provides the District with $200 million shared excess coverage, attaching at the self-insured retention level for all property risks excepting flood and earthquake, which attach at 2% of total insured value. Any gap between the self-insured level and excess insurance is funded half by the property pool and half by the affected member.

As a member, the District is subject to assessments based on claims submitted by all members. The following assessments were charged during the years ended December 31:

PURMS Insurance Assessments Charged	Liability		Property	
	2017	2016	2017	2016
Electric System	$ 162,361	$ 152,402	$ 38,201	$ 32,692
Box Canyon Production System	68,118	77,232	160,149	135,961
Water System	8,576	4,734	2,825	2,940
Community Network System	14,165	17,264	522	528
	$ 253,220	$ 251,632	$ 201,697	$ 172,121

Central Washington Public Utilities - The District, with six other public utility districts, is a member of the Central Washington Public Utilities Unified Insurance Program and Trust, which is a self-insurance program providing medical, dental, life insurance, disability insurance, and similar benefits to member employees and families. Formed by a Declaration of Trust and an Interlocal Agreement under RCW Chapter 39.34, the trust is administered by a board of trustees consisting of an appointed trustee from each of the seven member districts. Further information may be obtained by contacting the District's financial department as set forth on the last page of this Annual Report under Organizational Information—Corporate Office.

Note 8 - Commitments and Contingencies

Box Canyon Project license - The Federal Energy Regulatory Commission 50-year license for the District's Box Canyon Project expires on July 1, 2055. The license contains several conditions, including environmental studies and projects initiated by state and federal agencies and the Kalispel Tribe of Indians. All projects and studies are related to Box Canyon Dam and its reservoir and include the protection, mitigation, and enhancement of fish, wildlife, recreation, erosion, and cultural preservation. Capitalized projects have included upgrade of the Box Canyon Project turbines, spillway gate modification for total dissolved gas abatement, and construction of fish passage facilities currently in process. District-directed projects that are noncapital in nature, which are expensed as incurred, include improvement of wildlife and fish habitat, water quality monitoring, erosion mitigation, and environmental studies. The license also requires payments to agencies that are used at the discretion of the receiving party, and are intended primarily for recreation and erosion although the District has no control over the final disposition of the funds. These costs have been estimated over the life of the license and recorded as a regulatory asset and licensing costs liability (Note 1).

The District is currently constructing an upstream fish passage facility at Box Canyon, expected to be completed in the fall of 2018. The anticipated cost of the project is approximately $36 million, of which the District has expended $12.5 million and $13.7 million and during 2017 and 2016, respectively.

The District opened a line-of-credit with a financial institution during 2016, and extended it in 2017 to expire in September 2018, to complete the fish passage project as well as make final payment to the District's turbine upgrade contractor.

The license includes language authorizing the District to use lands in the Kalispel Indian Reservation. Under a contract signed in 2007, payment to the Kalispel Tribe for use of their lands is based on costs to produce power at Box Canyon Dam. The Kalispel Tribe receives their payment in electrical energy, the amount of which is based on a formula using Box Canyon Dam production costs. The Kalispel Tribe chooses on an annual basis, in advance of the calendar year, to use the energy, require the District to sell the energy to a third party on the Kalispel Tribe's behalf at market prices, or require the District to purchase the power at cost of production. For 2017 and 2016, the

Kalispel Tribe chose to have the District purchase the power at generation cost. Power sales on the Kalispel Tribe's behalf totaled $229,964 and $231,406 in 2017 and 2016, respectively.

Sullivan Creek Project - The Electric System's Sullivan Creek Project consists of two dams, an abandoned conduit, a forebay, and an empty powerhouse, and is currently used solely for water storage.

The Sullivan Creek Project's 50-year FERC license expired in September 2008. In 2010, the District concluded a negotiated license surrender process with several agencies, including USFS, Department of Ecology, Washington State Department of Fish and Wildlife, United States Fish and Wildlife, several other organizations, and local citizens. The resultant settlement agreement outlines continued operation of the Sullivan Dam as a water storage facility. The agreement also outlines various environmental projects to protect and enhance fish and wildlife habitat. Through an Interlocal Agreement between Seattle City Light and the District, Seattle City Light agreed to pay the full cost to remove the Mill Pond Dam and perform other restoration and environmental work as part of the relicensing conditions for Boundary Dam. Seattle City Light also agreed to pay half of the cost of construction of a cold water pipe, which drafts cooler water from the bottom of Sullivan Lake in an effort to lower the water temperature of an outlet creek. Once the terms and conditions of the negotiated agreement and FERC Surrender Order are met and approved by FERC, which is expected in 2020, the District will become eligible to receive a 30-year USFS permit to continue to operate Sullivan Dam as a water storage facility.

Concurrent with the license surrender process, the District applied to the Department of Ecology to sell certain Sullivan-related water rights to the state of Washington through the Department of Ecology Office of Columbia River, Columbia River Water Management Program. In exchange for the release of water from Sullivan Lake at designated times and amounts over the expected USFS permit 30-year life, the Department of Ecology Office of Columbia River agreed to fund the District $14 million.

Proceeds are expected to finance Sullivan Creek Project capital and operating, maintenance, and environmental expenditures for the entirety of a USFS 30-year license term to be issued after decommissioning of the project is fully complete. The proceeds are recorded as unearned revenue and being amortized annually in an amount equal to the net cash outflow for Sullivan Project-related activities each year. The monies are restricted to use for Sullivan Creek Project-related expenditures and reflected on the statement of net position within the contract security liability category.

Because there is no operating value for the District in owning the Sullivan Project assets, the District reports the net revenues and expenses as nonoperating. Asset values, including construction costs for the cold water pipe, are recorded net of accumulated depreciation as nonutility plant. The District reports no remaining license surrender liability. Although considered unlikely, the District retains risk that the associated parties will fail to perform their agreed-upon obligations and the District will incur a considerable liability associated with the license surrender.

Rental agreement - In 1997, the District entered into a rental agreement with the Pend Oreille County Port District for use of their railroad right-of-way related to a 115-kilovolt transmission line project. Under this agreement, the District agreed to pay a consumer price index-adjusted $125,000 per year for a 20-year period commencing January 1, 1997, subject to termination by the District with a year's notice. In January 2017, the District extended the contract for a three year period, with a flat payment of $200,000 in each year. The District paid $200,000 and $193,515 under the terms of this agreement for 2017 and 2016, respectively.

NoaNet - The District guaranteed certain NoaNet debt obligations and participates in assessments (Note 9).

Other contingencies - The District is subject to various claims, possible legal actions, and other matters arising out of the normal course of business. When it is possible to make a reasonable estimate of the District's liability with respect to probable claims, an appropriate provision is made. Although the ultimate outcome of litigation against the District cannot be determined, management intends to continually defend all claims against the District and believes the District is adequately reserved for all known events.

Note 9 - Broadband Services

Community Network System - The District owns a fiber optic backbone extending from Spokane north past Metaline Falls and includes fiber into all District substations. The District built this system primarily for Electric System operation and control, but allowed others to use the system and thereby help local businesses, as well as develop revenues to offset infrastructure costs.

With the acceptance of a federal grant, the District expanded its broadband services to the residents of Pend Oreille County, changing the scope of the utility services offered by the Community Network System. The Community Network System operates in accordance with state wholesale laws, which authorize the District to build infrastructure and enable open-access use of that infrastructure to internet service providers and entities authorized to provide retail telecommunications services within the state of Washington, who may then, in turn, provide retail services to customers.

Northwest Open Access Network - The District, along with nine other Washington public utility districts and Energy Northwest, is a member of Northwest Open Access Network (NoaNet), a Washington nonprofit mutual corporation. NoaNet uses a high-speed fiber optic transmission system, largely located within Washington State, to provide Ethernet and other advanced telecommunications services on a wholesale basis to its members and retail telecommunications companies. NoaNet has first right-of-refusal to lease four strands, designated as public purpose, from fiber optic lines the BPA owns on transmission lines.

In December 2014, NoaNet established a $13 million variable rate, junior lien, nonrevolving line of credit and transferred the balances of two previous lines of credit to the new note. The balance of the line was $9,350,638 as of December 31, 2016. This line was refinanced in March 2017 with a $10.2 million term loan. The balance on the loan as of December 31, 2017 was $9,228,014.

NoaNet also opened a $5 million line of credit to fund capital expenditures in April 2017, which had a balance of $2,280,000 as of December 31, 2017, and a $2 million operating line of credit, which had a balance of $700,000 as of December 31, 2017.

In 2016, NoaNet reported a net operating loss of $6,886,847, $319,785 of nonoperating expense, and a total decrease in net position of $7,206,632.

The District's Electric System reports no investment or liability account balance reflecting NoaNet membership.

A NoaNet annual report may be obtained by writing to Northwest Open Access Network, 3511 Norfolk Court, Olympia, WA 98501. NoaNet's website is available at www.noanet.net.

Note 10 - Grants

The District reports most grant revenue as nonoperating. Occasionally, grant proceeds are received in reimbursement for operating expenses. In such cases, the grant revenue is classified as operating.

Washington State Department of Health - In 2015, the Washington State Department of Health awarded a $30,000 grant to perform a feasibility study to consider the consolidation of a water system located in the County. $25,322 in funds were expended primarily on engineering services to evaluate the infrastructure revisions and upgrades that would be required to consolidate the system. $25,322 is recorded as grant revenue for 2016. No decision was made to consolidate the system as of December 31, 2017.

REQUIRED SUPPLEMENTARY INFORMATION

Schedule of Proportionate Share of Net Pension Liability as of June 30

	2017		2016		2015		2014	
	PERS 1	PERS 2/3	PERS 1	PERS 2/3	PERS 1	PERS 2/3	PERS 1	PERS 2/3
Employer's proportion of the net pension liability (asset)	0.067391%	0.086683%	0.076635%	0.098196%	0.082596%	0.106666%	0.078204%	0.100688%
Employer's proportionate share of the net pension liability	$ 3,197,754	$ 3,011,819	$ 4,115,660	$ 4,944,091	$ 4,320,539	$ 3,811,237	$ 3,939,563	$ 2,035,268
Employer's covered employee payroll	$ 8,498,422	$ 8,498,422	$ 9,167,431	$ 9,167,431	$ 9,471,100	$ 9,471,100	$ 8,618,199	$ 8,618,199
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	37.63%	35.44%	44.89%	53.93%	45.62%	40.24%	45.71%	23.62%
Plan fiduciary net position as a percentage of the total pension liability	61.24%	90.97%	57.03%	85.82%	59.10%	89.20%		

Schedule of Employer Contributions as of December 31

	2017		2016		2015		2014	
	PERS 1	PERS 2/3	PERS 1	PERS 2/3	PERS 1	PERS 2/3	PERS 1	PERS 2/3
Statutorily or contractually required contributions	$ 416,156	$ 579,483	$ 412,225	$ 538,399	$ 405,744	$ 520,400	$ 372,964	$ 461,531
Contributions in relation to the statutorily or contractually required contributions	(416,156)	(579,483)	(412,225)	(538,399)	(405,744)	(520,400)	(372,964)	(461,531)
Contribution deficiency (excess)	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Covered employer payroll	$ 8,519,240	$ 8,519,240	$ 8,526,028	$ 8,526,028	$ 9,384,967	$ 9,384,967	$ 9,268,074	$ 9,268,074
Contributions as a percentage of covered employee payroll	4.88%	6.80%	4.83%	6.31%	4.32%	5.54%	4.02%	4.98%

*As this is a newly adopted standard, information is only available for the last four years.

SUPPLEMENTAL INFORMATION (UNAUDITED)

Electric System - Revenue, Customer and Energy Statistics

	For the Years Ended December 31,				
	2017	2016	2015	2014	2013
Average number of customers					
Residential	8,205	8,126	8,042	7,957	7,912
Commercial	842	843	842	841	836
Industrial	8	8	8	8	8
Other	80	79	77	77	62
Total District customers	9,135	9,056	8,969	8,883	8,818
Sales for resale	2	2	2	2	2
Total	9,137	9,058	8,971	8,885	8,820
Revenues from sale of energy (000s)					
Residential	$ 10,577	$ 9,372	$ 8,899	$ 8,963	$ 9,052
Commercial	2,836	2,507	2,401	2,391	2,434
Industrial	32,081	32,165	26,500	28,541	32,122
Other	34	40	40	39	38
Total District customers	45,527	44,085	37,840	39,934	43,646
Intersystem sales	185	164	132	140	142
Sales for resale	1,937	1,492	5,790	6,057	3,920
Total energy sales	47,648	45,741	43,762	46,131	47,708
Other operating revenues	1,181	1,317	739	825	950
Total	$ 48,829	$ 47,059	$ 44,501	$ 46,956	$ 48,658
Energy (MWh)					
Residential	153,606	132,802	133,059	143,037	143,077
Commercial	51,337	45,462	44,696	46,806	47,340
Industrial	795,231	762,914	643,009	719,194	808,082
Other	267	302	291	299	301
Total District customers	1,000,441	941,480	821,055	909,336	998,800
Intersystem sales	3,319	2,805	2,867	3,229	3,534
Sales for resale	85,580	84,592	282,410	202,618	131,358
Total sales	1,089,341	1,028,877	1,106,332	1,115,183	1,133,692
Peak demand (MW)	166	161	145	162	153
Energy requirements (MWh)					
Ponderay Newsprint Company	724,990	699,447	580,993	675,145	765,225
All other retail customers	278,771	244,838	242,929	237,420	237,109
Total retail sales	1,003,761	944,285	823,922	912,565	1,002,334
Sales for resale	85,580	84,592	282,410	202,618	131,358
Total sales	1,089,341	1,028,877	1,106,332	1,115,183	1,133,692
Electric System losses	16,707	30,544	19,760	16,345	16,790
Total energy requirements	1,106,048	1,059,422	1,126,093	1,131,528	1,150,482
Energy resources (MWh)					
Box Canyon Project	359,364	490,907	505,850	462,530	433,381
Boundary Project	366,350	368,828	366,005	366,993	372,221
Bonneville and other sources	380,334	199,687	254,237	302,005	344,880
Total energy resources	1,106,048	1,059,422	1,126,093	1,131,528	1,150,482

SUPPLEMENTAL INFORMATION (UNAUDITED)

Electric System - Senior Lien Parity Debt Service Coverage					
	For the Years Ended December 31,				
	2017	2016	2015	2014	2013
Operating revenues (000s)					
Energy sales	$ 47,648	$ 45,742	$ 43,762	$ 46,131	$ 47,708
Other	1,181	1,317	739	825	950
Total operating revenues	48,829	47,059	44,501	46,956	48,658
Operating expenses (1)					
Power costs	29,704	25,916	28,121	30,090	30,849
Operations and maintenance	6,701	5,782	6,191	6,433	5,287
Administrative and general	5,981	4,433	3,586	3,385	3,066
Taxes	2,482	2,525	2,157	2,190	2,394
Pension Expense	(603)	(691)	477	(193)	-
Total operating expenses	44,265	37,965	40,532	41,905	41,596
Investment income (2)	79	56	-	18	110
Net revenue available for debt service	4,644	9,150	3,969	5,069	7,172
Funds transferred to rate stabilization fund	(300)	(4,300)	-	-	-
Net revenue for debt service coverage	4,344	4,850	3,969	5,069	7,172
Senior lien debt service	2,062	2,057	3,005	3,011	2,467
Net revenue available for capital	$ 2,282	$ 2,793	$ 964	$ 2,058	$ 4,705
Debt service coverage ratio (3)	2.11x	2.36x	1.32x	1.68x	2.91x

(1) Total operating expenses exclude depreciation for purposes of determining parity debt service coverage ratios.

(2) Investment income varies depending on many factors, including unrealized gains and losses on long-term investments.

(3) Debt service coverage ratio on senior lien debt service.

Box Canyon Production System - Senior Lien Parity Debt Service Coverage

	For the Years Ended December 31,				
	2017	2016	2015	2014	2013
Operating revenues (000s)					
Energy sales					
Electric System	$ 18,414	$ 17,603	$ 16,669	$ 16,993	$ 17,883
Tribal use of lands	230	232	219	215	215
All other (1)	5	36	15	138	59
Total operating revenues	18,649	17,871	16,903	17,346	18,157
Operating expenses (2)					
Power costs	231	126	114	717	917
Operations and maintenance	5,099	4,904	4,643	4,582	5,365
Administrative and general	2,364	2,190	2,454	2,510	2,249
Taxes	83	111	114	105	99
Pension Expense	(294)	(280)	200	(81)	-
Total operating expenses	7,483	7,051	7,525	7,833	8,630
Investment income	258	229	10	59	125
Other nonoperating (3)	1,939	1,986	2,021	2,045	2,049
Net revenue available for debt service (4)	13,363	13,035	11,409	11,617	11,701
Senior lien debt service (5)	10,942	10,993	11,037	11,069	11,095
Junior lien debt service	-	-	-	-	-
Net revenue available for capital	$ 2,421	$ 2,042	$ 373	$ 547	$ 606
Debt service coverage ratio (6)	1.22x	1.19x	1.03x	1.05x	1.05x

(1) "All other" includes miscellaneous revenue such as logging activities on project properties.

(2) Excludes depreciation for purposes of determining senior lien debt service coverage.

(3) Internal Revenue Service interest reimbursement for 2009 Series B, Taxable Build America Bonds, and 2012 Taxable Clean Renewable Energy Bonds, Direct Payment.

(4) The District controls net revenue available by adjusting the power sales transfer price to the Electric System based on Box Canyon Production System cash flow requirements for debt service and capital investment.

(5) Senior lien debt service includes the 2008 CREB bonds, the 2009 bonds, the 2010 bonds, and 2012 CREB bonds.

(6) Debt service coverage ratio on senior lien debt service.

Community Network System - Senior Lien Parity Debt Service Coverage

	For the Year Ended December 31, 2017
Operating revenues (000s)	
Broadband Sales	$ 1,957
Other	492
Total operating revenues	2,449
Operating expenses (1)	
Operations and maintenance	847
Administrative and general	189
Taxes	32
Pension Expense	(53)
Total operating expenses	1,015
Investment income (2)	0
Net revenue available for debt service	1,434
Senior lien debt service	419
Net revenue available for capital	$ 1,015
Debt service coverage ratio	3.42x

2017 is the first year of senior lien parity debt service coverage requirements.

(1) Total operating expenses exclude depreciation for purposes of determining parity debt service coverage ratios.

(2) Investment income varies depending on many factors, including unrealized gains and losses on long-term investments.

ORGANIZATIONAL INFORMATION

Date of organization	November 1936
Nature of business	A municipal corporation supplying public utility services in Pend Oreille County, Washington
Board of Commissioners	
President	Daniel L. Peterson
Vice President	Curt J. Knapp
Secretary	Richard A. Larson
Key District Management	
General Manager	F. Colin Willenbrock
Director of Finance/Auditor	April D. Owen
Treasurer	Sarah L. Holderman
Senior Accountant	Kelly J. Scherf
Director, Regulatory and Environmental Affairs	Mark J. Cauchy
Director, Operations and Line Superintendent	Christopher W. Jones
Director, Engineering	Amber E. Orr
Director, Power and Risk Management	Kimberly D. Gentle
Director, Power Production	Mark D. Cleveland
Director, Safety and Human Resources	Lloyd B. Clark
Systems	
Electrical power distribution	Electric System
Hydroelectric power generation at Box Canyon Project	Box Canyon Production System
Water distribution in residential subdivisions and the town and vicinity of Metaline Falls	Water System
Wholesale broadband communications services	Community Network System
Corporate Office	P.O. Box 190 130 N. Washington Newport, Washington 99156 (509) 447-3137 Telephone (509) 447-5824 Facsimile www.popud.org
Paying Agent and Registrar Information	U.S. Bank National Association 111 Fillmore Avenue East St. Paul, Minnesota 55107-1402

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PEND OREILLE
PUBLIC UTILITY DISTRICT

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2017
Annual Report

Quality Service at Low Cost