Office of the Washington State Auditor
Pat McCarthy

Financial Statements Audit Report

Public Utility District No. 1 of Mason County

For the period January 1, 2016 through December 31, 2016

Published March 15, 2018

Report No. 1020918

Office of the Washington State Auditor

Pat McCarthy

March 15, 2018

Board of Commissioners
Public Utility District No. 1 of Mason County
Shelton, Washington

Report on Financial Statements

Please find attached our report on Public Utility District No. 1 of Mason County's financial statements

We are issuing this report in order to provide information on the District's financial condition.

Sincerely,

Pat McCarthy

State Auditor

Olympia, WA

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PUBLIC UTILITY DISTRICT NO.1
OF MASON COUNTY
N. 21971 Hwy. 101
Shelton, Washington 98584

BOARD OF COMMISSIONERS
MIKE SHEETZ, Commissioner
JACK JANDA, Commissioner
RON GOLD, Commissioner

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Public Utility District No 1 of Mason County
January 1, 2016 through December 31, 2016

This schedule presents the status of findings reported in prior audit periods.

Audit Period: January 1, 2015 – December 31, 2015	**Report Ref. No.:** 1018770	**Finding Ref. No.:** 2015-001

Finding Caption:
The District's internal controls over accounting and financial statement preparation were inadequate to ensure accurate financial reporting.

Background:
It is the responsibility of District management to design, implement and maintain internal controls to ensure financial statements are fairly presented and that provide reasonable assurance regarding the financial reporting's reliability. Our audit identified internal control deficiencies that adversely affected the District's ability to produce reliable and accurate financial statements and when taken together represent a material weakness:

- The District did not have adequate procedures in place to implement new accounting standards correctly.
- The financial statement review process was inadequate to ensure financial information was accurate.
- The District lacked adequate procedures to ensure adjusting journal entries were made for a valid purpose and independently reviewed, and that documentation was retained. The controls were not effective to detect journal entries related to misappropriation in a timely manner.

Status of Corrective Action: (check one)

☐ Fully Corrected ☒ Partially Corrected ☐ Not Corrected ☐ Finding is considered no longer valid

Corrective Action Taken:
For 2016, these issues were still being resolved. We onboarded a CPA firm to help us develop procedures and reconcile our 2015 & 2016 financials. They assumed the lead role in preparing the annual financial reporting, including the implementation of new accounting standards.

These are reviewed by management & board. Year end 2015 & 2016 financials were corrected and presented to the board. In 2017, we implemented processes to ensure appropriate oversight and accuracy of financial processes, preparation of financial statements and implementation of accounting standards. We are confident that the next fiscal audit will show that these bullet points have been fully corrected.

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

Public Utility District No. 1 of Mason County
January 1, 2016 through December 31, 2016

Board of Commissioners
Public Utility District No. 1 of Mason County
Shelton, Washington

We have audited, 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, the financial statements of Public Utility District No. 1 of Mason County, Washington, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated March 5, 2018.

INTERNAL CONTROL OVER FINANCIAL REPORTING

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

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

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

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of the District's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

PURPOSE OF THIS REPORT

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Pat McCarthy

Pat McCarthy

State Auditor

Olympia, WA

March 5, 2018

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

Public Utility District No. 1 of Mason County
January 1, 2016 through December 31, 2016

Board of Commissioners
Public Utility District No. 1 of Mason County
Shelton, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of Public Utility District No. 1 of Mason County, Washington, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed on page 10.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Public Utility District No. 1 of Mason County, as of December 31, 2016, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and required supplementary information listed on page 10 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 REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated March 5, 2018 on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Pat McCarthy

State Auditor

Olympia, WA

March 5, 2018

FINANCIAL SECTION

Public Utility District No. 1 of Mason County
January 1, 2016 through December 31, 2016

REQUIRED SUPPLEMENTARY INFORMATION

BASIC FINANCIAL STATEMENTS

REQUIRED SUPPLEMENTARY INFORMATION

Mason County Public Utility District #1
Management Discussion and Analysis
December 31, 2016

Introduction:

As Management of Mason County PUD #1 (the District), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ending December 31, 2016. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished.

The following Management Discussion and Analysis is intended to serve as an introduction to the Mason County PUD #1 basic financial statements, the notes to the financial statements, and if applicable, any other supplementary information required as part of the basic financial statements.

The District Commissioners adopt an annual budget as a measure of monitoring revenues and expenditures. The Commissioners also use the budget as a financial planning tool for the District's future needs.

The Statement of Net Position presents the District's assets and liabilities, with the difference between the two reported as net position. This statement provides information about the amount of investments in resources (assets), and the obligations to creditors (liabilities). The Net Position increases when revenues exceed expenses.

The Statement of Revenue, Expenses, and Changes in Fund Net Position reports the revenues and expenses during the years indicated. This statement measures the success of the District's operations over the past year and can be used to determine whether the District has successfully recovered all of its costs through user fees and other charges.

The Statement of Cash Flows provides information about the District's cash receipts and payments from operations, as well as funds provided and used in investing and financing activities.

The Notes to the Financial Statements provided additional information that is essential to gain a full understanding of the information provided in the basic financial statements.

Mason County PUD #1
Statement of MDA
For the Year Ended December 31. 2016

FINANCIAL ANALYSIS

2016 and 2015 Overview of Financial Analysis
Provided in the Following Table.

Condensed Financial Information for December 31, 2016 and 2015 (In Millions)

Statement of Net Position	2016	2015	% Change
Current Assets and Special Funds	5.70	5.63	1%
Net Capital Assets	32.69	32.14	2%
Deferred Outflow of Resources	0.37	0.23	61%
Total Assets	38.76	38.00	2%
Current Liabilities	1.49	1.46	2%
Non Current Liabilities	13.44	13.67	-2%
Total Liabilities	14.93	15.13	-1%
Deferred Inflows of Resources	0.04	0.24	100%
Net Investments in Capital Assets	21.06	20.00	5%
Restricted for Customer Deposits	0.10	0.09	11%
Restricted for Debt Service	0.89	0.69	29%
Unrestricted	1.74	1.84	-5%
Total Net Position	23.79	22.62	5%
Statement of Revenues, Expenses and Change in Net Position			
Operating Revenues	9.30	8.80	6%
Operating Expenses	-7.90	-7.64	3%
Net Operating Income	1.40	1.16	21%
Non Operating Revenues	0.12	0.18	-33%
Non Operating Expenses	-0.37	-0.41	-10%
Net Operating Revenue (Expenses)	-0.25	0.93	-127%
Change In Net Position	1.12	0.93	20%
Net Position - Beginning of Year	22.62	23.25	-3%
Prior Period Changes in Net Position	0.05	-1.56	-103%
Net Position - End of Year	23.79	22.62	5%

Mason County PUD #1
Statement of MDA
For the Year Ended December 31. 2016

ASSETS:

Current Assets:
Cash and Cash Equivalents - This account has decreased by $356,847 dollars from 2015 to 2016. The decrease was due to an increase in expenses from the previous year's activity, as well as transferring funds to the investment account for a net total of $54,877.

Investments - This account has increased by $54,877 dollars from 2015 to 2016. The increase was due to increased cash flow due to increased revenue, which allowed for cash to be transferred to the investment account.

Accounts Receivable (Net) - This account has increased by $5,500 dollars from 2015 to 2016. This is a normal increase.

Accounts Receivable (Other) - This account has increased by $56,917 dollars from 2015-2016. The increase was for tax increases from the Department of Revenue for pole contacts rentals. And increases for pole attachments.

Restricted Assets - This account has increased by $212,888 dollars from 2015 to 2016. The increase was due to funding an additional year for debt reserves to long term debt.

Inventories - This account has increased by $102,062 dollars from 2015 to 2016. The increase was due to an increase in construction work in progress.

Other Current Assets - This account has decreased by $1,944 dollars from 2015 to 2016. The decrease was due to reclassify the balance up to Construction Work in Progress.

Capital Assets Not being Depreciated:
Land and Land Rights - There was no change in this account from 2015 to 2016. No land was purchased in 2016.

Construction In Progress - This account increased by $309,424 dollars from 2015 to 2016. The increase was due to an increase in activity for the year.

Capital Assets Being Depreciated:
Transmission - There were no changes to this account for 2016.

Distribution - This account increased by $653,793 dollars from 2015 to 2016. The increase is normal for the year as the District replaces poles,wire,transformers,water mains, etc..

General Plant - This account increased by $434,329 dollars from 2015 to 2016. This was due in part to improvements made to the warehouse, as well as office equipment and transportation equipment upgrades.

Capital Assets Being Depreciated (continued):

Accumulated Depreciation - This account has increased by $842,520 dollars from 2015 to 2016. This is a normal increase for the year due to depreciating capital assets.

Deferred Outflow Of Resources:

Outflows of Resources Relating to Pensions - Based on the GASB 68 calculation, the balance as of 2016 is $374,615.

LIABILITIES:

Current Liabilities:

Accounts Payable - This account decreased by $72,982 dollars from 2015 to 2016. This is considered a reasonable change, due to timing of when warrants were paid at year end.

Consumer Deposits - This account has decreased by $8,716 dollars from 2015 to 2016. The increase is due to an increase in new service accounts for consumers.

Bonds, Notes and Loans Payable - This account increased by $80,687 from 2015 to 2016. This is considered normal as principal payments will increase from year to year.

Other Current Liabilities - These accounts has increased by $16,193 from 2015 to 2016. This is considered normal for the year as these accounts increase or decrease at year end.

Non-Current Liabilities:

Accrued Vacation and Holidays - This account has increase by $2,129 from 2015 to 2016. This is normal as employees save vacation time more in one year to the next.

Long Term Debt - loans - This account has decreased by $344,239 from 2015 to 2016. This is due to paying down the principal balance in 2016.

Long Term Debt - Bonds - This account decreased by $219,999 dollars from 2015 to 2016. This was due to principal payments made in 2016.

OPEB - This account remained the same, until a new actuarial analysis will be performed in 2018.

Net Pension Liability - This account increased by $388,714 due to an increase in the percentage of the PUD's proportionate share in 2016.

Other Non-Current Assets - These accounts decreased by $48,998 from 2015 to 2016. This was a prior year balance on work orders that had already been closed.

Deferred Inflows of Resources:

Deferred Inflows related to Pensions: This account decreased by 210,494 due to the annual GASB 68 calculation for the change in proportionate share for the PUD.

LIABILITIES CONTINUED:

Net Position:

Net Investments in Capital Assets - This account has increased by $1,054,885 from 2015 to 2016. The main reason is the capital assets less LTD and debt service has increased more than the District borrowed.

Restricted for Customer Deposits - This account increased by 7,113 from 2015 to 2016

Restricted for Debt Service - This account has increased by $205,776 from 2015 to 2016. The increase in debt service from bonds and Line of credit added to the restriction.

Unrestricted - This account has decreased by $96,986 dollars from 2015 to 2016. This is a normal decrease due to the increase in net investments and restrictions for debt service

OPERATING REVENUES:

Total Operating Revenues - This account increased by $492,290 dollars from 2015 to 2016. The increase is due to an increase in sales consumption, including the 5% increase in basic service charges in 2016.

OPERATING EXPENSES:

Cost of Purchased Power - This account has increased by $175,727.36 dollars from 2015 to 2016. The increase is in part due to the rate increase by BPA in October 2015, but also due to increased consumer consumption in 2016.

Transmission Expense - This account has decreased by $10,485 dollars from 2015 to 2016. This decrease is due to less maintenance expenses in 2016.

Distribution and Maintenance Expense - This account decreased $2,838 dollars from 2015 to 2016

Customer Service Expense - This account has decreased by $20,398 from 2015 to 2016. The overall decrease was due to decreased IT expenses, as well as an increase in rebates.

Administration - This account has increased by $111,616 from 2015 to 2016. This is due to an increase in outside services for 2016.

Depreciation and Amortization - This account has increased by $39,603 dollars from 2015 to 2016. The increase was due to due the addition of capital assets in 2016.

Taxes - This account has increased by $64,473 dollars from 2015 to 2016.

Other Operating Expenses - This account has decreased by $67,915 dollars from 2015 to 2016.

NON-OPERATING REVENUE:

Merchandising and Jobbing Revenue and (Expenses) - The net decrease for these 2 accounts was $34,496 dollars from 2015 to 2016. The decrease was due to less merchandise and jobbing sales for 2016.

Interest and Dividend Income - This account has increased by $8,014 dollars from 2015 to 2016.

Interest Expense and Related Charges - The interest expense for these accounts have decreased $11,367 dollars from 2015 to 2016.

Other Non-Operating Revenues - This account increased by $1,231 dollars from 2015 to 2016.

Mason County PUD #1
Statement of Net Position
December 31, 2016

ASSETS:

Current Assets:		
Cash and Cash Equivalents	$	2,150,085.00
Investments	$	785,829.00
Accounts Receivable (net)	$	780,871.00
Accounts Receivable (other)	$	208,755.00
Inventories	$	783,349.00
TOTAL CURRENT ASSETS	$	4,708,889.00
Noncurrent Assets:		
Restricted Assets	$	993,988.00
Capital Assets Not Being Depreciated:		
Land & Land Rights	$	856,639.00
Construction In Progress	$	1,529,916.00
Total Capital Assets Not Being Depreciated	$	2,386,555.00
Capital Assets Being Depreciated:		
Transmission	$	3,295,653.00
Distribution	$	36,269,689.00
General Plant	$	4,928,965.00
Less: Accumulated Depreciation	$	(14,190,213.00)
Total Capital Assets Being Depreciated (Net)	$	30,304,094.00
Total Capital Assets	$	32,690,649.00
TOTAL NONCURRENT ASSETS	$	33,684,637.00
TOTAL ASSETS	$	38,393,526.00
Deferred Outflows Of Resources:		
Outflows of Resources Relating to Pensions	$	374,615.00
TOTAL OUTFLOWS OF RESOURCES:	$	374,615.00
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	$	38,768,141.00

The Accompanying Notes Are An Integral Part Of This Statement

Mason County PUD #1
Statement of Net Position
December 31, 2016

LIABILITIES

Current Liabilities:		
Accounts Payable	$	544,496.00
Consumer Deposits	$	97,042.00
Current Portion of Bonds, Notes and Loans Payable	$	541,595.00
Other Current Liabilities	$	253,436.00
TOTAL CURRENT LIABILITIES	$	1,436,569.00
Noncurrent Liabilities:		
Accrued Vacation And Holidays	$	358,554.00
Long Term Debt - Loans	$	7,313,296.00
Long Term Debt - Bonds	$	3,774,978.00
OPEB	$	68,085.00
Net Pension Liability	$	1,985,798.00
TOTAL NONCURRENT LIABILITIES	$	13,500,711.00
TOTAL LIABILITIES	$	14,937,280.00
Deferred Inflows of Resources:		
Deferred Inflows Related to Pensions	$	35,774.00
TOTAL DEFERRED INFLOWS OF RESOURCES	$	35,774.00
NET POSITION		
Net Investments in Capital Assets	$	21,060,780.00
Restricted for Customer Deposits	$	101,768.00
Restricted for Debt Service	$	892,220.00
Unrestricted	$	1,740,319.00
TOTAL NET POSITION	$	23,795,087.00
TOTAL NET POSITION, LIABILITIES AND DEFERRED INFLOWS OF RESOURCES	$	38,768,141.00

The Accompanying Notes Are An Integral Part Of This Statement

Mason PUD #1

Statement of Revenues, Expenses and Changes in Fund Net Position

December 31, 2016

OPERATING REVENUES:			
Sales - Residential		$	7,412,413.00
Sales - General		$	1,648,340.00
Sales - Street Lights		$	93,644.00
Other Revenues		$	142,692.00
Total Operating Revenues		$	9,297,089.00
OPERATING EXPENSES:			
Cost of Purchased Power		$	3,015,255.00
Transmission Expense		$	3,435.00
Distribution & Maintenance Expense		$	1,117,006.00
Customer Service Expense		$	245,416.00
Administration:			
General Administration		$	1,773,320.00
Conservation		$	-
Depreciation & Amortization		$	1,156,772.00
Taxes		$	610,641.00
Other Operating Expenses		$	3,212.00
Total Operating Expenses		$	7,925,057.00
OPERATING INCOME (LOSS)		$	1,372,032.00
NON-OPERATING REVENUE(EXPENSES):			
Revenue from Merchandising/Jobbing and Contract Work		$	32,020.00
(Costs and Expenses Merchandising Jobbing and Contract work)		$	(27,803.00)
Interest and Dividend Income		$	13,079.00
(Interest Expense and Related Charges)		$	(344,074.00)
Other Non-Operating Revenues		$	79,220.00
Total Non-Operating Revenues(Expenses)		$	(247,558.00)
CHANGE IN NET POSITION		$	1,124,474.00
Total Net Position	January 1, 2016	$	22,624,300.00
PRIOR PERIOD CHANGES IN NET POSITION		$	46,313.00
Total Net Position	December 31, 2016	$	23,795,087.00

The Accompanying Notes Are An Integral Part Of This Statement

Mason County PUD #1
Statement of Cash Flows
For the Year Ended December 31, 2016

CASH FLOWS from OPERATING ACTIVITIES:		
Receipts from Customers	$	9,234,672.00
Payments to Suppliers	$	(3,357,560.00)
Payments to Employees	$	(2,960,837.00)
Other Receipts or Payments	$	(521,699.00)
Net Cash Provided(used) by Operating Activities	$	2,394,576.00
CASH FLOWS from CAPITAL FINANCING ACTIVITIES:		
Acquisition and Construction of Capital Assets	$	(1,791,260.00)
Principal Paid on Capital Debt	$	(483,551.00)
Interest Paid on Capital Debt	$	(344,074.00)
Net cash Provided (Used) by Capital and Related Financing Activities	$	(2,618,885.00)
CASH FLOWS from INVESTING ACTIVITIES		
Interest and Dividends		
Net Cash Provided by Investing Activities	$	13,079.00
Net Increase (Decrease) in Cash and Cash Equivalents	$	(211,230.00)
Cash and Cash Equivalents Balances - Beginning of Year	$	4,141,132.00
Cash and Cash Equivalents Balances - End of Year	$	3,929,902.00

Mason County PUD #1
Statement of Cash Flows
For the Year Ended December 31, 2016

RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES

Operating Income (Loss)	$	1,372,032.00
Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities		
Depreciation Expense	$	1,156,772.00
Other Deductions	$	3,212.00
Change In Assets and Liabilties		
Receivables - Net	$	(62,416.00)
Inventories	$	(102,062.00)
Accounts and Other Payable	$	72,983.00
Accrued Expenses	$	(45,945.00)
Net Cash Provided by Operating Activities	$	2,394,576.00

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES

Public Utility District No. 1 of Mason County (the PUD) was incorporated on November 6, 1934 and operates under the laws of the state of Washington applicable to a public utility.

A. Reporting Entity

   The PUD is a special purpose government and provides electric, water, and sewer services to the general public. The PUD is primarily supported through user charges (or where the governing body has decided that periodic determination of net income is needed).

   An elected 3-member board governs the PUD. As required by generally accepted accounting principles, management has considered all potential component units in defining the reporting entity. The PUD has no component units.

B. Basis of Accounting and Presentation

   The accounting records of the PUD are maintained in accordance with methods prescribed by the United States Department of Agriculture, Rural Utilities Services (RUS) and the State Auditor under the authority of Chapter 43.09 RCW. The PUD uses the Uniform System of Accounts – Electric, RUS Bulletin 1767B-1.

   The PUD uses the full-accrual basis of accounting, where the revenues are recognized when earned and expenses are recognized when incurred. Capital asset purchases are capitalized and long-term liabilities are accounted for in the appropriate fund(s).

   The PUD distinguishes between operating revenues and expenses from non-operating ones. Operating revenues and expenses result from providing services and producing and delivering goods in connection with the PUD's principal ongoing operations. The principal operating revenues of the PUD are charges to customers for power, water, and sewer. Operating expenses for the PUD include cost of operations and maintenance, administrative and customer service, depreciation, taxes and debt amortization. All revenues and expenses not meeting this definition are reported as non-operating revenue and expenses.

C. Statement of Net Position

   1. Cash and Cash Equivalents

      It is the PUD's policy to invest all temporary cash surpluses, in excess of the operating reserve in the Washington State Treasurer's Investment Pool. For the purposes of the Statement of Cash Flows, the PUD considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES (Continued)

2. Investments – See Note 2.

3. Restricted Assets
   In accordance with bond resolutions (and certain related agreements) separate restricted funds are required to be established. The assets held in these funds are restricted for specific uses, including debt service and other special reserve requirements. The Restricted Net Position consists of $101,768 held for customer deposits, and $970,746 held for debt service.

4. Receivables
   Customer accounts receivable consist of amounts owed from private individuals or organizations for goods and services, including amounts owed for which billings have not been prepared. Notes and contract receivables consist of amounts owed on open accounts from private individuals or organizations for goods and services rendered.

   The PUD writes off accounts deemed to be uncollectible to the bad debt expense account.

5. Inventories
   Inventories consist of expendable supplies held for consumption. The cost is recorded as an expenditure at the time the individual inventory items are consumed. The reserve for inventory is equal to the ending amount of inventory to indicate that a portion of the balance is not available for future expenditures. A comparison market value is not necessary.

   Inventories are expensed using the FIFO reporting method, where the inventory acquired first is expensed, over time.

6. Capital Assets and Depreciation – See Note 3.

7. Compensated Absences
   Compensated absences are absences for which employees will be paid, such as vacation (and sick) leave. The PUD accrues unpaid leave for compensated absences as an expense and liability when incurred.

   Vacation pay, which may be accumulated up to 1200 hours, is payable upon resignation, retirement, or death.

8. Pensions
   For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pension, and pension expense, and the reporting of the fiduciary's net position of all state sponsored plans and additions to / deductions from those plans' fiduciary net position have been determined on the same basis as they are

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES (Continued)

reported by the Washington State Department of Retirement Systems. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair market value.

9. Other Accrued Liabilities
These accounts consist of accrued wages and accrued employee benefits.

10. Long-Term Debt – See Note 8.

NOTE 2 – DEPOSITS AND INVESTMENTS

A. Deposits
As required by state law, all deposits and investments of the PUD's funds (except as noted below) are obligations of the U.S. Government, the State Treasurer's Investment Pool, or deposits with Washington State banks savings and loan institutions.

The PUD's deposits are entirely covered by Federal Depository Insurance (FDIC) or by collateral held in multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (WPDPC). There are no policy and no custodial credit risks.

For short term investments, cash equivalents, the PUD utilizes the Washington State Treasurer's Investment Pool. The fair value of the PUD's position in the pool is the same as the value of the pool shares, with cash available to the PUD on demand. The on-demand availability of these funds defines them as cash equivalent liquid investments.

B. Investments
The PUD measures and reports investments at fair value using the valuation input hierarchy established by generally accepted accounting principles, as follows:

- Level 1: Quoted prices in active markets for identical assets or liabilities;
- Level 2: These are quoted market prices for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, r other than quoted prices that are note observable;
- Level 3: Unobservable inputs for an asset or liability.

At December 31, 2016, the district had the following investments measured at fair value:

		Fair Value Measurements Using		
	12/31/2016	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by Fair Value Level				
Treasurer Investment Pool	$3,929,902	$ $3,929,902	$ -	$ -
Total Investments measured at fair value	$ 3,929,902	$ $3,929,902	$ -	$ -

NOTE 3- CAPITAL ASSETS AND DEPRECIATION

Capital assets are defined by the PUD as assets with individual costs of more than $2,500 and an estimated useful life in excess of 1 year.

Major expenditures for capital assets, including capital leases and major repairs that increase useful lives are capitalized. Maintenance, repairs, and minor renewals are accounted for as expenses when incurred.

Utility Plant in Service (and other capital assets) are recorded at cost (where the historical costs are known), or estimated historical cost if purchased or constructed. Donated capital assets are recorded at acquisition value at the date of donation.

Depreciation expense is charged to operations to allocate the cost of capital assets over their estimated useful lives, using the straight-line method with useful lives of 10 to 36 years.

Capital asset activity for the year ended December 31, 2016 is as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Utility Plant Not Being Depreciated				
Land	$ 856,639.00	$0.00	$0.00	$ 856,639.00
Construction in Progress	$ 1,220,492.00	$ 309,424.00	$0.00	$ 1,529,916.00
Total Utility Plant Not Being Depreciated	**$ 2,077,131.00**	**$ 309,424.00**	**$0.00**	**$ 2,386,555.00**
Utility Plant Being Depreciated				
Distribution and Transmission Plant	$ 38,911,549.00	$ 843,802.00	($190,009.00)	$ 39,565,342.00
General Plant	$ 4,494,636.00	$ 577,964.00	($143,635.00)	$ 4,928,965.00
Total Utility Plant Being Depreciated	**$ 43,406,185.00**	**$1,421,766 .00**	**($333,644.00)**	**$ 44,494,307.00**
Less Accumulated Depreciation	$ (13,347,693.00)	$1,156,722.00	($314,202.00)	$ (14,190,213.00)
Total Utility Plant Being Depreciated (Net)	**$ 30,058,492.00**	**$ 265,044.00**	**($19,442.00)**	**$ 30,304,094.00**
Total Utility Plant (Net)	**$ 32,135,623.00**	**$ 574,468.00**	**($19,442.00)**	**$ 32,690,649.00**

NOTE 4-CONSTRUCTION IN PROGRESS

Construction in progress represents expenses to date on projects for which authorizations total $1,529,916. Of the committed balance of $1,529,916, the PUD will be required to raise $0.00 in future financing.

NOTE 5 – PENSION PLANS

The following table represents the aggregate pension amounts for all plans subject to the requirements of the GASB Statement 68, *Accounting and Financial Reporting for Pensions* for the year 2016:

Aggregate Pension Amounts – All Plans	
Pension liabilities	($1,985,798)
Pension assets	$0.00
Deferred outflows of resources	$374,614
Deferred inflows of resources	($35,774)
Pension expense/expenditures	$249,666

State Sponsored Pension Plans

Substantially all PUD's full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing, multiple-employer public employee defined benefit and defined contribution retirement plans. The state Legislature establishes, and amends, laws pertaining to the creation and administration of all public retirement systems.

The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to:

Department of Retirement Systems
Communications Unit
P.O. Box 48380
Olympia, WA 98540-8380

Or the DRS CAFR may be downloaded from the DRS website at www.drs.wa.gov.

Public Employees' Retirement System (PERS)

PERS members include elected officials; state employees; employees of the Supreme, Appeals and Superior Courts; employees of the legislature; employees of district and municipal courts; employees of local governments; and higher education employees not participating in higher education retirement programs. PERS is comprised of three separate pension plans for membership purposes. PERS plans 1 and 2 are defined benefit plans, and PERS plan 3 is a defined benefit plan with a defined contribution component.

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. Members retiring from active status prior to the age of 65 may receive actuarially reduced benefits. Retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Department of Labor

NOTE 5 – PENSION PLANS (Continued)

and Industries. PERS 1 members were vested after the completion of five years of eligible service. The plan was closed to new entrants on September 30, 1977.

Contributions

The **PERS Plan 1** member contribution rate is established by State statute at 6 percent. The employer contribution rate is developed by the Office of the State Actuary and includes an administrative expense component that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates. The PERS Plan 1 required contribution rates (expressed as a percentage of covered payroll) for 2016 were as follows:

PERS Plan 1		
Actual Contribution Rates:	**Employer**	**Employee***
PERS Plan 1	6.23%	6.00%
PERS Plan 1 UAAL	4.77%	6.00%
Administrative Fee	0.18%	
Total	**11.18%**	**6.00%**

* For employees participating in JBM, the contribution rate was 12.26%.

PERS Plan 2/3 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 for Plan 2 and 1 percent of AFC for Plan 3. The AFC is the average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. 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 benefit that is reduced by a factor that varies according to age for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions:

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

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service credit. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit. Other PERS Plan 2/3 benefits include

duty and non-duty disability payments, a cost-of-living allowance (based on the CPI), capped at three percent annually and a one-time duty related death benefit, if found eligible by the Department of Labor and Industries. PERS 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service if 12 months of that service are earned after age 44.

NOTE 5 – PENSION PLANS (Continued)

PERS Plan 3 defined contribution benefits are totally dependent on employee contributions and investment earnings on those contributions. PERS Plan 3 members choose their contribution rate upon joining membership and have a chance to change rates upon changing employers. As established by statute, Plan 3 required defined contribution rates are set at a minimum of 5 percent and escalate to 15 percent with a

choice of six options. Employers do not contribute to the defined contribution benefits. PERS Plan 3 members are immediately vested in the defined contribution portion of their plan.

Contributions

The **PERS Plan 2/3** employer and employee contribution rates are developed by the Office of the State Actuary 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 UAAL and an administrative expense that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and Plan 3 contribution rates. The PERS Plan 2/3 required contribution rates (expressed as a percentage of covered payroll) for 2016 were as follows:

PERS Plan 2/3		
Actual Contribution Rates:	**Employer 2/3**	**Employee 2/3***
PERS Plan 2/3	6.23%	6.12%
PERS Plan 1 UAAL	4.77%	
Administrative Fee	0.18%	
Employee PERS Plan 3		varies
Total	**11.18%**	**6.12%**

* For employees participating in JBM, the contribution rate was 15.30%.

The PUD's actual PERS plan contributions were $92,566.92 to PERS Plan 1 and $120,912.86 to PERS Plan 2/3 for the year ended December 31, 2016.

Actuarial Assumptions

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2016 with a valuation date of June 30, 2015. The actuarial assumptions used in the valuation were based on the results of the Office of the State Actuary's (OSA) *2007-2012 Experience Study*.

Additional assumptions for subsequent events and law changes are current as of the 2015 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2016. Plan liabilities were rolled forward from June 30, 2015, to June 30, 2016, reflecting each plan's normal cost (using the entry-age cost method), assumed interest and actual benefit payments.

- **Inflation:** 3.0% total economic inflation; 3.75% salary inflation
- **Salary increases**: In addition to the base 3.75% salary inflation assumption, salaries are also expected to grow by promotions and longevity.
- **Investment rate of return:** 7.5%

NOTE 5 – PENSION PLANS (Continued)

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

There were minor changes in methods and assumptions since the last valuation.

- For all systems, except LEOFF Plan 2, the assumed valuation interest rate was lowered from 7.8% to 7.7%. Assumed administrative factors were updated.
- Valuation software was corrected on how the nonduty disability benefits for LEOFF Plan 2 active members is calculated.
- New LEOFF Plan 2 benefit definitions were added within the OSA valuation software to model legislation signed into law during the 2015 legislative session.

Discount Rate

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

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

Long-Term Expected Rate of Return

The long-term expected rate of return on the DRS pension plan investments of 7.5 percent was determined using a building-block-method. The Washington State Investment Board (WSIB) used a best estimate of expected future rates of return (expected returns, net of pension plan investment expense, including inflation) to develop each major asset class. Those expected returns make up one component of WSIB's capital market assumptions. The WSIB uses the capital market assumptions and their target asset allocation to simulate future investment returns at various future times. The long-term expected rate of return of 7.5 percent approximately equals the median of the simulated investment returns over a 50-year time horizon

Estimated Rates of Return by Asset Class

Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2016, are summarized in the table below. The inflation component used to create the table is 2.2 percent and represents the WSIB's most recent long-term estimate of broad economic inflation.

NOTE 5 – PENSION PLANS (Continued)

Asset Class	Target Allocation	% Long-Term Expected Real Rate of Return Arithmetic
Fixed Income	20%	1.70%
Tangible Assets	5%	4.40%
Real Estate	15%	5.80%
Global Equity	37%	6.60%
Private Equity	23%	9.60%
	100%	

Sensitivity of the Net Pension Liability/(Asset)

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

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
PERS 1	$1,087,880	$902,132	$742,284
PERS 2/3	$1,995,224	$1,083,666	$(564,111)

Pension Plan Fiduciary Net Position

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

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

At June 30, 2016, the PUD reported a total pension liability of $1,985,798 for its proportionate share of the net pension liabilities as follows:

	Liability (or Asset)
PERS 1	$902,132
PERS 2/3	$1,083,666
TOTAL	$1,985,798

NOTE 5 – PENSION PLANS (Continued)

At June 30, the PUD's proportionate share of the collective net pension liabilities was as follows:

	Proportionate Share 6/30/15	Proportionate Share 6/30/16	Change in Proportion
PERS 1	%.016220	%.016798	%.000578
PERS 2/3	%.020952	%.021523	%.000571

Employer contribution transmittals received and processed by the DRS for the fiscal year ended June 30 are used as the basis for determining each employer's proportionate share of the collective pension amounts reported by the DRS in the *Schedules of Employer and Nonemployer Allocations* for all plans except LEOFF 1.

LEOFF Plan 1 allocation percentages are based on the total historical employer contributions to LEOFF 1 from 1971 through 2000 and the retirement benefit payments in fiscal year 2016. Historical data was obtained from a 2011 study by the Office of the State Actuary (OSA). In fiscal year 2016, the state of Washington contributed 87.12 percent of LEOFF 1 employer contributions and all other employers contributed the remaining 12.88 percent of employer contributions. LEOFF 1 is fully funded and no further employer contributions have been required since June 2000. If the plan becomes underfunded, funding of the remaining liability will require new legislation. The allocation method the plan chose reflects the projected long-term contribution effort based on historical data.

In fiscal year 2016, the state of Washington contributed 39.46 percent of LEOFF 2 employer contributions pursuant to RCW 41.26.725 and all other employers contributed the remaining 60.54 percent of employer contributions.

The collective net pension liability (asset) was measured as of June 30, 2016, and the actuarial valuation date on which the total pension liability (asset) is based was as of June 30, 2015, with update procedures used to roll forward the total pension liability to the measurement date.

Pension Expense

For the year ended December 31, 2016, the PUD recognized pension expense as follows:

	Pension Expense
PERS 1	$80,326
PERS 2/3	$169,340
TOTAL	$249,666

NOTE 5 – PENSION PLANS (Continued)

Deferred Outflows of Resources and Deferred Inflows of Resources

At December 31, 2016, the PUD reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

PERS 1	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$	$
Net difference between projected and actual investment earnings on pension plan investments	$22,714	$
Changes of assumptions	$	$
Changes in proportion and differences between contributions and proportionate share of contributions	$	$
Contributions subsequent to the measurement date	$44,886	$
TOTAL	$67,600	$

PERS 2/3	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$57,704	$(35,774)
Net difference between projected and actual investment earnings on pension plan investments	$132,609	$
Changes of assumptions	$11,201	$
Changes in proportion and differences between contributions and proportionate share of contributions	$46,862	$
Contributions subsequent to the measurement date	$58,638	$
TOTAL	$307,014	$(35,774)

Deferred outflows of resources related to pensions resulting from the PUD's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2017. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	PERS 1 Deferred Outflows	PERS 1 Deferred Inflows
2017	($5,593)	
2018	($5,593)	
2019	$20,861	
2020	$13,039	
2021		
Thereafter		
Total	$22,741	

NOTE 5 – PENSION PLANS (Continued)

Year ended December 31:	PERS 2/3 Deferred Outflows	PERS 2/3 Deferred Inflows
2017	$29,577	($11,179)
2018	$29,577	($11,179
2019	$123,012	($11,179)
2020	($2,236)	($2,236)
2021		
Thereafter		
Total	$248,376	($35,774)

NOTE 6 – DEFERRED COMPENSATION PLAN

The PUD offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. This plan is with the State of Washington. The plan, available to eligible employees, permits them to defer a portion of their salary until future years. The assets held in the deferred compensation plan are not available to employees until termination, retirement, death, or unforeseeable emergency.

NOTE 7 – RISK MANAGEMENT

The PUD purchases their liability insurance from Federated Rural Insurance Corporation. The PUD maintains a $2,000,000 all-risk blanket with a $10,000,000 umbrella policy. No insurance settlements have exceeded insurance coverage in the past 3 years. The risk of loss to the PUD is covered by

- Liability coverage in the amount of $12,000,000. This covers general liability, property damage, automobile coverage, personal injury, medical payments, and valuable papers.
- Employee dishonesty, money, and securities in the amount of $4,000,000.
- Directors, Officers and Managers Liability and Corporate Indemnification Policy in the amount of $1,000,000.
- Workers Compensation Insurance of $100,000.

NOTE 8 – LONG-TERM DEBT

A. Long-Term Debt
   The annual requirements to amortize all debts outstanding as of December 31, 2016 including interest are as follows:

NOTE 8 – LONG TERM DEBT (Continued)

Calendar Year Ending December 31, 2016:

Year	Principal	Interest	Total
2017	$541,595	$336,635	$878,230
2018	3,501,484	322,353	3,823,837
2019	506,484	252,594	759,078
2020	516,484	238,186	754,670
2021-2025	2,130,156	968,843	3,098,999
2026-2030	1,913,367	641,238	2,554,605
2031-2035	1,393,349	276,290	1,669,639
2036-2040	596,923	112,817	709,740
2041-2045	477,538	28,935	506,473
TOTAL	$11,577,380	$3,177,891	$14,755,271

Debt issuance costs are expensed in the period incurred and bonds are displayed net of premium or discount. Annual interest expense is decreased by amortization of debt premium.

The PUD uses a combination of RUS debt, Revenue Bonds, and a Line of Credit for the electrical division for the financing its debt instruments.

RUS, Bond Loans and the Line of Credit were purchased for electrical distribution, transmission and special equipment replacement and additions. They include wire, transformers, meters, conduit, and poles, and other electrical equipment.

On June 6th, 2014, the PUD issued a $3,585,000 bond for refinancing the RUS debt of 5%. The bonds bear an average interest rate of 2% to 5% and will be redeemed over the next 20 years. This bond replaces the RUS debt that was to be amortized over the next 28 years. The total savings over the next 20 years is $874,000. The bond was sold at a premium of $55,251.50 and has a current balance of $3,390,000 and a maturity date of December 01, 2033.

The PUD uses a combination of Public Works Trust Fund Loans (PWTF) and Revenue Bonds for its water systems. The PWTF interest rate averages 1% over 20 years, with an average coupon rate for water bonds of 4% over 20 years.

PWTF Loans- $1,314,764:

System	Balance	Maturity	Loan Number
Hoodsport Water	$15,264	7/01/2017	PW-97-791-009
Lake Arrowhead Water	$227,984	10/01/2021	PW-00-65120-013
Pirates Cove Water	$56,092	10/01/2021	PW-00-65120-022
Arcadia Estates Water	$45,450	10/01/2025	PW-05-691-034
Canal Tracts Water	$83,823	10/01/2025	PW-05-691-037

NOTE 8 – LONG TERM DEBT (Continued)

Canal Mutual Water	$150,696	07/01/2027	PW-07-962-302
Hoodsport Water	$286,737	10/01/2029	PW-99-65199-035
Madrona Beach	$52,329	10/01/2030	DR-09-952-070
Hood Canal Water	$396,389	10/01/2031	PC12-951-081

2002 Revenue Bond - $635,000 Maturity Date – December 1, 2022:

System	Balance
Union Water	$25,984
Highland Park Water	$24,109
Hoodsport Water	$44,379
Hood Canal Water	$7,812
Lakewood Heights Water	$18,253
Harstene Retreat Water	$23,189
Cherry Park Water	$23,623
Tiger Lakes Water	$8,515
Bayshore Water	$16,700
Bay East Water	$27,774
View Ridge Heights Water	$106,532
Alderbrook Water	$295,198
Madrona Sewer	$12,930

PWTF and Water Bond Loans were purchased for water distribution, transmission and meter replacement and additions, including piping, pumps, well houses, reservoirs, wells and many other water related equipment.

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Water Revenue Bonds	720,000		85,000	535,000	100,000
2014 Revenue Bonds	3,390,000		135,000	3,115,000	140,000
2014 Bond Premium	52,489			52,489	
RUS Loans	3,462,154		89,538	3,223,385	149,230
PWTF Loans	1,488,777		174,013	1,162,400	152,365
Line of Credit	3,000,000			3,000,000	
OPEB	68,085			68,085	
Net Pension Liability	1,597,084	388,714		1,985,798	
Accrued Vacation & Holidays	356,426	2,129		358,554	
Other Non-Current Liabilities	48,998		48,998	0.00	
Total Non-Current Liabilities	**14,184,012**	**390,843**	**532,549**	**13,500,711**	**541,595**

NOTE 9 – CONTINGENCIES AND LITIGATION

The PUD has recorded in its financial statements all material liabilities, including an estimate for situations which are not yet resolved, but where, based on available information, management believes it is probably that the PUD will have to make payment. In the opinion of management, the PUD's insurance policies are adequate to pay all known or pending claims.

The PUD participates in a number of federal-and state assisted programs. These grants are subject to audit by the grantors or their representatives. Such audits could result in requests for reimbursement to grantor or their representatives. Such audits could result in requests for reimbursement to grantor agencies for expenditures disallowed under the terms of the grants. PUD management believes that such disallowances, if any, will be immaterial.

NOTE 10 – POST EMPLOYMENT BENEFITS OTHER THAN PENSIONS

The PUD belongs to the State of Washington's Public Employees Benefits Board (PEBB), a program which provides medical and dental through private health insurance plans to eligible retirees. Retiree benefit provisions are established by Commission resolution.

Employees are eligible for reimbursement of medical and dental coverage provided that they retire from active employment with the PUD with 15 or more years of service. Employee retiree coverage continues for a maximum of 10 years. The elected Commissioners are eligible for payment of post-retirement benefits based on 18 years of service. They are not eligible for a percentage of employment by year and must serve 18 years to receive 54 percent for 10 years. The PUD funding policy and status is a pay as you go. The PUD pays employees a portion of the premium cost based on years of service at retirement according the following schedule:

Years of service	%	Years of service	%	Years of Service	%
15	45	22	66	29	87
16	48	23	69	30	100
17	51	24	72		
18	54	25	75		
19	57	26	78		
20	60	27	81		
21	63	28	84		

The PUD's OPEB was calculated on February 26, 2016 by Menard Consulting, Inc.

The PUD's annual Post-Retirement healthcare benefit is calculated based on the annual required contribution (ARC) of the employer using the Alternative Measurement Method, amount actuarially determined in accordance with GASB Statement 45. The ARC represents a level of funding that, if paid

NOTE 10 – POST EMPLOYMENT BENEFITS OTHER THAN PENSIONS (Continued)

on an on-going basis, is projected to cover normal costs each year and amortize unfunded liabilities over a 30 year period. The interest on the Net OPEB obligation is $1,055 and adjustments to the annual required contributions are ($1,742). The amortization period is for 30 years. The amortization period is opened. The following table shows the components of the PUD's annual post retirement obligations for the years ended:

	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2014
Annual Required Contribution	$147,232	$ 147,232	$125,536
Contributions made	$ 79,147	$ 79,147	$ 90,367
Net Post-Retirement Obligation	$ 68,085	$ 68,085	$ 35,169

Net OPEB Obligation – December 31, 2014	$35,169
Net OPEB Obligation - December 31, 2015	$68,085
Net OPEB Obligation - December 31, 2016	$68,085

Assumptions

The District used Menard Consulting Inc. Actuaries to provide the method and calculation for the Post retirement benefits. The discount rate used was 3.0% for cash flows from the valuation date. The discount rate is used for expected long-term yield on investments to pay benefits.

The mortality rate used was the RP-2000 combined Mortality Table for males and females. The Mortality table reflects recent rates developed by the Society of Actuaries with a generally accepted projection of future mortality improvement. (Paragraph 34d GASB 45)

Disability rates for the individuals that are being valued are not valued. The turnover assumptions were taken from the default turnover assumptions based on paragraph 35b, Table 1 of GASB 45. The retirement average age was 65.

The healthcare estimated future annual increases in premiums was estimated at an initial rate of 7.90% grading uniformly over 10 years to a 5% rate. The medical trend rate is based on the 2012 Health Plan Cost Trend Survey. The grading period and ultimate trend rates were selected using a generally accepted range (Paragraph 34f of GASB 45. For 2016, there were no changes

NOTE 10 – POST EMPLOYMENT BENEFITS OTHER THAN PENSIONS (Continued)

for post retirement benefits.

The Actuarial calculations reflect a long-term perspective. The actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and that actuarially determined amounts are subject to continual revisions as results are compared to past expectations and new estimates are made about the future.

As of December 31, 2016, the Actuarial Accrued Liability was $1,366,365.

NOTE 11 –PRIOR PERIOD ADJUSTMENT

During the review of 2016, management determined that there were errors in the accrued payroll liability accounts, resulting in a reduction of $3,079. It was also discovered that work order for the Water Division hadn't been closed properly in prior years, resulting in an increase of $49,392, for an overall change of $46,313.

NOTE 12 – ACCOUNTING AND REPORTING CHANGES

The PUD implemented GASB 72, Fair Value Measurement and Application. This statement provides guidance for determining a fair value measurement for financial reporting purposes and requires application of fair value to certain investments, in order to promote comparability of government financial statements. The standard expands the level of disclosure for fair value methodology in the notes to the financial statements. The standard also changes the recorded value of contributed capital assets from fair value to acquisition value.

NOTE 13 - SEGMENT REPORTING

	2016	2016	2016	
CURRENT ASSETS	Electric	Water	Sewer	TOTAL
Cash and Cash Equivalents	$ 1,963,469.00	$ 106,923.00	$ 1,167.00	$ 2,071,559.00
Investments	$ 263,225.00	$ 497,950.00	$ 24,654.00	$ 785,829.00
Accounts Receivable - Net Sales	$ 628,669.00	$ 152,148.00	$ 54.00	$ 780,871.00
Accounts Receivable - Other	$ 198,622.00	$ 10,133.00	$ -	$ 208,755.00
Inventories	$ 641,759.00	$ 135,705.00	$ 5,885.00	$ 783,349.00
Total Current Assets	$ 3,695,744.00	$ 902,859.00	$ 31,760.00	$ 4,630,363.00
NON-CURRENT ASSETS				
Restricted Assets	$ 732,704.00	$ 333,937.00	$ 5,873.00	$ 1,072,514.00
Capital Assets Not Being Depreciated				
Land and Land Rights	$ 814,394.00	$ 42,245.00	$ -	$ 856,639.00
Construction in Progress	$ 1,477,655.00	$ 49,857.00	$ 2,404.00	$ 1,529,916.00
Capital Assets Being Depreciated				
Transmission	$ 3,295,653.00	$ -	$ -	$ 3,295,653.00
Distribution	$ 24,328,254.00	$ 12,141,081.00	$ 64,522.00	$ 36,533,857.00
General Plant	$ 4,611,599.00	$ 53,198.00	$ -	$ 4,664,797.00
Less: Accumulated Depreciation	$ (11,008,935.00)	$ (3,167,520.00)	$ (13,758.00)	$ (14,190,213.00)
Total Capital Assets Being Depreciated (Net)	$ 21,226,571.00	$ 9,026,759.00	$ 50,764.00	$ 30,304,094.00
Total Capital Assets	$ 23,518,620.00	$ 9,118,861.00	$ 53,168.00	$ 32,690,649.00
Total Non-Current Assets	$ 24,251,324.00	$ 9,452,798.00	$ 59,041.00	$ 33,763,163.00
Total Assets	$ 27,947,068.00	$ 10,355,657.00	$ 90,801.00	$ 38,393,526.00
Outflows of Resources Relating to Pensions	$ 374,615.00	$ -	$ -	$ 374,615.00
Total Assets and Deferred Outflows of Resources	$ 28,321,683.00	$ 10,355,657.00	$ 90,801.00	$ 38,768,141.00
LIABILITIES				
Current Liabilities:				
Accounts Payable	$ 542,008.00	$ 2,488.00	$ -	$ 544,496.00
Consumer Deposits	$ 81,201.00	$ 15,841.00	$ -	$ 97,042.00
Bonds, Notes and Loans Payable	$ 334,234.00	$ 204,961.00	$ 2,400.00	$ 541,595.00
Other Current Liabilities	$ 243,606.00	$ 7,125.00	$ 2,705.00	$ 253,436.00
Total Current & Accrued Liabilities	$ 1,201,049.00	$ 230,415.00	$ 5,105.00	$ 1,436,569.00
Non-Current Liabilities:				
Accrued Vacation and Holidays	$ 358,554.00	$ -	$ -	$ 358,554.00
Long Term Debt - Loans	$ 6,163,002.00	$ 1,139,764.00	$ 10,530.00	$ 7,313,296.00
Long Term Debt - Bonds	$ 3,182,869.00	$ 592,109.00	$ -	$ 3,774,978.00
Net Pension Liability	$ 1,985,798.00	$ -	$ -	$ 1,985,798.00
OPEB	$ 68,085.00	$ -	$ -	$ 68,085.00
Other Non-Current Liability	$ -	$ -	$ -	$ -
Total Non-Current Liabilties	$ 11,758,308.00	$ 1,731,873.00	$ 10,530.00	$ 13,500,711.00
Total Liabilities	$ 12,959,357.00	$ 1,962,288.00	$ 15,635.00	$ 14,937,280.00
Deferred Inflow Related to Pensions	$ 35,774.00	$ -	$ -	$ 35,774.00
Net Position				
Net Investments in Capital Assets	$ 13,838,515.00	$ 7,182,027.00	$ 40,238.00	$ 21,060,780.00
Restricted for Customer Deposits	$ 81,201.00	$ 20,567.00	$ -	$ 101,768.00
Restricted for Debt Service	$ 651,503.00	$ 313,370.00	$ 5,873.00	$ 970,746.00
Unrestricted	$ 755,333.00	$ 877,405.00	$ 29,055.00	$ 1,661,793.00
Total Net Position	$ 15,326,552.00	$ 8,393,369.00	$ 75,166.00	$ 23,795,087.00
TOTAL NET POSITION, LIABILITIES AND DEFERRED	$ 28,321,683.00	$ 10,355,657.00	$ 90,801.00	$ 38,768,141.00

NOTE 13 - SEGMENT REPORTING (CONTINUED)

STATEMENT OF REVENUE, EXPENSES AND CHANGES IN FUND NET POSITION	2016 ELECTRIC	2016 WATER	2016 SEWER	TOTAL
OPERATING REVENUES				
Sales - Residential	$ 5,919,625.00	$ 1,482,709.00	$ 10,079.00	$ 7,412,413.00
Sales - General	$ 1,648,340.00	$ -	$ -	$ 1,648,340.00
Sales - Street Lights	$ 93,644.00	$ -	$ -	$ 93,644.00
Miscellaneous Other Revenues	$ 135,492.00	$ 7,200.00	$ -	$ 142,692.00
Total Operating Revenues	$ 7,797,101.00	$ 1,489,909.00	$ 10,079.00	$ 9,297,089.00
OPERATING EXPENSES				
Cost of Purchased Power	$ 2,925,690.00	$ 89,102.00	$ 463.00	$ 3,015,255.00
Transmission Expenses	$ 3,435.00	$ -		$ 3,435.00
Distribution & Maintenance Expense	$ 890,969.00	$ 225,545.00	$ 492.00	$ 1,117,006.00
Customer Service Expense	$ 203,006.00	$ 42,366.00	$ 44.00	$ 245,416.00
Administrative and General	$ 1,607,071.00	$ 166,240.00	$ 9.00	$ 1,773,320.00
Depreciation	$ 894,073.00	$ 262,699.00	$ -	$ 1,156,772.00
Taxes	$ 534,146.00	$ 76,107.00	$ 388.00	$ 610,641.00
Other Deductions	$ 3,212.00	$ -		$ 3,212.00
Total Operating Expenses	$ 7,061,602.00	$ 862,059.00	$ 1,396.00	$ 7,925,057.00
NET OPERATING INCOME	$ 735,499.00	$ 627,850.00	$ 8,683.00	$ 1,372,032.00
NON-OPERATING REVENUE (EXPENSES)				
Revenue from Merchandising, Jobbing And Contract Work	$ 14,694.00	$ 17,326.00	$ -	$ 32,020.00
Costs and Expenses of Merchandising, Jobbing and Contract Work	$ (27,777.00)	$ (26.00)	$ -	$ (27,803.00)
Interest and Dividend Income	$ 10,780.00	$ 2,189.00	$ 110.00	$ 13,079.00
Other Revenues	$ -	$ 79,220.00	$ -	$ 79,220.00
Interest on Long-Term Debt	$ (295,574.00)	$ (46,887.00)	$ (1,613.00)	$ (344,074.00)
Total Non-Operating Revenue (Expenses)	$ (297,877.00)	$ 51,822.00	$ (1,503.00)	$ (247,558.00)
Change In Net Position	$ 437,622.00	$ 679,672.00	$ 7,180.00	$ 1,124,474.00
Total Net Posisiton January 1	$ 14,892,009.00	$ 7,664,305.00	$ 67,986.00	$ 22,624,300.00
Prior Period Change in Net Position	$ (3,079.00)	$ 49,392.00	$ -	$ 46,313.00
Total Net Position December 31	$ 15,326,552.00	$ 8,393,369.00	$ 75,166.00	$ 23,795,087.00

Required Supplementary Information

Mason County PUD #1
Schedule of Employer Contributions
As of December 31, 2016

Last 10 Fiscal Years *	2016		2015		2014		2013	
	PERS 1	PERS 2/3	PERS 1	PERS 2/3	PERS 1	PERS 2/3	PERS 1	PERS 2/3
Statutorily or contractually required contribution	92,567.00	120,913.00	0.00	190,334.00	5,876.00	163,398.00	8,335.00	125,530.00
Contributions in relation to the statutorily or Contractually required Contributions	(92,567.00)	(120,913.00)	0.00	(190,334.00)	(5,876.00)	(163,398.00)	(8,335.00)	(125,530.00)
Contribution deficiency (excess)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Covered employer payroll	1,941,779.00	1,941,779.00		1,956,229.00	63,803.00	1,774,135.00	102,109.00	1,531,525.00
Contributions as a percentage of covered employee payroll	5%	6%	0%	10%	9%	9%	8%	8%

*As this is a newly adopted standard, information is only available for the last 4 years

Mason County PUD #1
Schedule of Proportionate Share of the Net Pension Liability
As of December 31, 2016

Last 10 Fiscal Years	2016		2015		2014	
	PERS 1	PERS 2/3	PERS 1	PERS 2/3	PERS 1	PERS 2/3
Employer's Proportion of Net Pension Liability	0.016798%	0.021523%	0.016220%	0.020952%	0.017656%	0.019682%
Employer's Proportionate Share of Net Pension Liability	902,132.00	1,083,666.00	848,457.00	748,627.00	889,429.00	397,844.00
Employer's Covered Employee Payroll	2,008,066.00	2,008,066.00	0	1,871,695.00	112,638.00	1,694,622.00
Employer's Proportionate Share of Net Pension Liability as a Percentage of Covered Employee Payroll	45%	54%	0%	40%	789.63%	23.48%
Plan Fiduciary Net Position as a Percentabe of Total Pension Liability	57%	86%	59.10%	89.20%		

*As this is a newly adopted standard, information is only available for the last 3 years

Required Supplementary Inforamtion

Other Post Retirement Benefits

Schedule of Funding Progress (December 31, 2016)

Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (AAL)*	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll	UAAL as a Percentage of Covered Payroll [(b-a)/c]
12/31/2011	0	$ 967,845.00	$ 967,845.00	0%	$ 1,640,596.00	59.00%
12/31/2012	0	$ 1,147,497.00	$ 1,147,497.00	0%	$ 1,703,702.00	67.40%
12/31/2013	0	$ 1,147,497.00	$ 1,147,497.00	0%	$ 1,777,913.00	64.50%
12/31/2014	0	$ 1,147,497.00	$ 1,147,497.00	0%	$ 1,906,000.00	60.22%
12/31/2015	0	$ 1,366,365.00	$ 1,366,365.00	0%	$ 1,956,229.00	69.84%
12/31/2016	0	$ 1,366,365.00	$ 1,366,365.00	0%	$ 1,956,229.00	69.84%

*Based on Projected unit credit actuarial cost method

ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

In fulfilling our mission to hold state and local governments accountable for the use of public resources, we also hold ourselves accountable by continually improving our audit quality and operational efficiency and developing highly engaged and committed employees.

As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments as well as fraud, state whistleblower and citizen hotline investigations.

The results of our work are widely distributed through a variety of reports, which are available on our website and through our free, electronic subscription service.

We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

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