

Washington State Auditor's Office
Financial Statements Audit Report

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

Audit Period
January 1, 2009 through December 31, 2009

Report No. 1003877

Issue Date
July 12, 2010



WASHINGTON
BRIAN SONNTAG
STATE AUDITOR



**Washington State Auditor
Brian Sonntag**

July 12, 2010

Board of Commissioners
Public Utility District No. 1 of Cowlitz County
Longview, Washington

Report on Financial Statements

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

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

Sincerely,

BRIAN SONNTAG, CGFM
STATE AUDITOR

Table of Contents

Public Utility District No. 1 of Cowlitz County January 1, 2009 through December 31, 2009

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters in Accordance with <i>Government Auditing Standards</i>	1
Independent Auditor's Report on Financial Statements.....	3
Financial Section.....	5

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters in Accordance with *Government Auditing Standards*

**Public Utility District No. 1 of Cowlitz County
January 1, 2009 through December 31, 2009**

Board of Commissioners
Public Utility District No. 1 of Cowlitz County
Longview, Washington

We have audited the financial statements of each major fund of Public Utility District No. 1 of Cowlitz County, Washington, as of and for the year ended December 31, 2009, which collectively comprise the District's basic financial statements and have issued our report thereon dated June 4, 2010.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit, we considered the District's internal control over financial reporting as a basis for designing our auditing procedures 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 over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

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.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of 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*.

This report is intended for the information and use of management and the Board of Commissioners. 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.

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BRIAN SONNTAG, CGFM
STATE AUDITOR

June 4, 2010

Independent Auditor's Report on Financial Statements

Public Utility District No. 1 of Cowlitz County January 1, 2009 through December 31, 2009

Board of Commissioners
Public Utility District No. 1 of Cowlitz County
Longview, Washington

We have audited the accompanying financial statements of each major fund of Public Utility District No. 1 of Cowlitz County, Washington, as of and for the year ended December 31, 2009, which collectively comprise the District's basic financial statements as listed on page 5. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of Public Utility District No. 1 of Cowlitz County, as of December 31, 2009, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 6 through 12 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted

principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" written in a larger, more prominent script than the last name "Sonntag".

BRIAN SONNTAG, CGFM
STATE AUDITOR

June 4, 2010

Financial Section

**Public Utility District No. 1 of Cowlitz County
January 1, 2009 through December 31, 2009**

REQUIRED SUPPLEMENTAL INFORMATION

Management's Discussion and Analysis – 2009

BASIC FINANCIAL STATEMENTS

Balance Sheet – 2009

Statement of Revenues, Expenses and Changes in Net Assets – 2009

Statement of Cash Flows – 2009

Notes to Financial Statements – 2009

MANAGEMENT DISCUSSION AND ANALYSIS
For the Year Ending December 31, 2009

This discussion and analysis is designed to provide an overview of the financial activities of Public Utility District No. 1 of Cowlitz County, Washington (District) for the year ended December 31, 2009. This supplementary information is to be read in conjunction with the District's financial statements.

The District is a municipal corporation incorporated in 1936 to serve the citizens of Cowlitz County, Washington. The District is governed by a three-member board of locally elected commissioners, independent of county government. The District manages and operates three systems: Electric, Water and Production (Swift No. 2 Hydroelectric).

Financial Policies and Controls

The District's financial management system consists of financial policies, financial management strategies, and the internal control structure, including annual budgets and external audit of its financial statements. The Board has the exclusive right to determine rates and charges for services provided. Planning is guided by forecasts of balance sheet, operating, and capital items. These tools are used to identify the impacts of anticipated initiatives and to devise strategies to meet the Board's financial objectives.

ELECTRIC SYSTEM

The Electric System provides electric service throughout Cowlitz County which encompasses 1,144 square miles. During 2009 the District's customer base declined slightly, and at December 31, 2009 48,197 customers were served by the District. Among PUDs in the state of Washington, the District ranks third in total customers and total retail sales (\$176,176,680 excluding unbilled revenues). Total power sales in 2009 were 4,625,321 MWhs making the District the second largest PUD in the state from the standpoint of electric usage.

Power supplies are provided to the District through a combination of purchased power contracts, with approximately 92% of the District's 2009 power supply being purchased from the Bonneville Power Administration (BPA). Weather and economic conditions are the primary influences on electricity sales. Generally, extreme temperatures increase sales to residential customers, who use electricity for cooling and heating, and moderate temperatures decrease sales. Winter weather in the District's region was slightly milder during 2009. Combined with the overall weakening economy, District retail energy sales declined approximately 5% in 2009.

Financial Summary and Analysis

In October 2001 the District put the portion of its load that had been subject to market purchases back under its contract with BPA. This significantly stabilized the District's power supply costs compared to the sharp fluctuations which had occurred in 2000 and 2001, improved the District's financial performance, and restored stability in electric rates following two large rate increases in 2000 and 2001. The District's most recent rate action was in October 2009 when they were increased approximately 5% as a result of increased operating costs, primarily related to increases in BPA rates.

During 2008 the District settled a long-standing legal dispute with BPA over the allocation of benefits related to the Residential Exchange Program. As a result of this settlement, BPA refunded \$18,350,669 in cash and another \$3,447,261 in billing credits to the District. In turn, the District issued cash refunds of \$13,961,546 to its largest industrial customers and applied billing credits of \$5,465,712 to remaining eligible customer accounts.

Selected Financial Data – Electric System

	<u>2009</u>	<u>2008</u>
Current Assets	\$ 44,760,049	\$ 37,879,465
Net Utility Plant	142,475,025	120,293,055
Other Assets	192,124,876	176,706,935
Total Assets	379,359,950	334,879,455
Current Liabilities	80,204,643	33,862,110
Long-Term Debt	145,569,543	152,614,777
Other Liabilities	10,291,743	9,542,255
Total Liabilities	236,065,929	196,019,142
Total Net Assets	143,294,021	138,860,313
Operating Revenues	197,585,125	213,475,012
Operating Expenses	185,960,177	203,560,457
Net Operating Revenues	11,624,948	9,914,555
Other Income-(Expense)	(7,043,921)	(4,112,057)
Change in Net Assets	4,581,027	5,802,498

Capital Asset and Long-term Debt Activity

As of year-end, the Electric System had \$230.9 million invested in electric system plant in service. Utility plant net of depreciation was \$142.5 million. This represents an increase of \$22.2 million (or 18.5%) from 2008.

In 2009 the District continued on its fourth year of an enhanced construction and maintenance program in an effort to improve the reliability of the Electric System for all customers. During 2009 the District replaced more than 30 miles of deteriorated underground cable. Also in 2009, the District completed its third year of a 5-year Advanced Automated Metering project, with a total of 30,000 meters deployed to date. When complete, computers in the District offices will have the ability to communicate on a real-time basis with customer meters District wide, allowing automatic meter readings as well as the opportunity for customers to monitor their own energy usage online. In addition, in 2009 the District significantly completed the replacement of the SCADA communications system, improving reliability and upgrading system security. Other construction projects in process in 2009 include engineering and design work to upgrade four substations. Capital construction is funded by a combination of aid-to-construction paid by customers and long-term revenue bonds sold in 2001, 2006 and 2007.

Total electric distribution system utility plant in service as of December 31, 2009 and 2008 consisted of the following:

	<u>2009</u>	<u>2008</u>
Intangible	\$ 227,422	\$ 215,249
Transmission & Distribution	199,465,079	179,671,430
General Plant	<u>31,158,547</u>	<u>28,263,223</u>
Total Plant In Service	<u>\$ 230,851,048</u>	<u>\$ 208,149,902</u>

The Electric Distribution System issued \$61.5 million in revenue bonds in 2006 in order to provide for the construction needs of the District, to defease a portion of the 2001 bonds, and to pay off \$8 million owing on a line of credit to Bank of America. In November 2007 the District issued \$64.755 million in Electric System Revenue Bonds to fund further capital improvements. At the end of 2009, \$134.07 million in revenue bonds remained outstanding.

Power Supply

The Electric Distribution System power supply is provided through contracts with BPA and Grant County PUD, as well as the purchase of the output from the District's Swift No. 2 Hydroelectric Production System on the Lewis River and the power associated with 2 MW of Energy Northwest's Nine Canyon Wind Project. In 2009 approximately 92% of the District's power supply was purchased from BPA. The Grant County PUD contracts provide an entitlement to a share of the output of the Priest Rapids and Wanapum Projects on the mid-Columbia. In 2009 the District also received and sold energy from the White Creek Wind Project, and in December 2009 the Harvest Wind Project was completed placed into commercial operation.

Bonneville Power Administration Power Supply

On October 1, 2001 the District began to take deliveries from BPA under a new long-term Power Sales Contract (2001 Contract) with BPA. This 2001 Contract is for a ten-year term and is take-or-pay in nature. That is, BPA is obligated to serve and the District is obligated to purchase the quantity of power required for service to the District's load over and above what is provided by the District's own Swift resource and the firm power contracts itemized below.

During 2008 the District executed a 20-year power supply contract with BPA to service the majority of District loads beginning October 2011.

Purchases from Grant County PUD

Pursuant to contracts with Grant County PUD, the District has rights to purchase predetermined percentage amounts of output from the Priest Rapids and Wanapum Developments. The District also must pay costs and debt service on the Priest Rapids and Wanapum Developments based on a predetermined percentage. The original contract with the Priest Rapids Development terminated October 31, 2005 and the current contract with the Wanapum Development terminates October 31, 2009. Both of these contracts have been extended through September 30, 2011 at 76% of their original output share.

Purchases from Energy Northwest's Nine Canyon Wind Project

The District entered into a contract with Energy Northwest in December 2003 for the purchase of the output associated with 2 megawatts of the Nine Canyon Wind Project. The District utilizes the power to serve its customers by use of a BPA wind integration product. The "green tags" or "renewable energy credits" associated with the District's share of output are committed for sale to the Bonneville Environmental Foundation and are not used for District load at this time.

Purchases from Swift No. 2 Hydroelectric Production System

The Swift No. 2 Hydroelectric Production System is located on the Lewis River and consists of a 3.2 mile long power canal with an adjacent power house and transmission switchyard. It operates in conjunction with the Swift No. 1 Project, which is owned by PacifiCorp. Swift No. 1 consists of an earthen dam and power house, which discharges into the Swift No. 2 power canal.

Swift No. 2 is operated under contract by PacifiCorp. The operating agreement provides that the District is entitled to 26% of the combined output of Swift No. 1 and Swift No. 2. The District's share of the output is purchased by the Electric System at the cost of production of the energy, whether it is producing energy or not.

White Creek Wind Project

In 2006 the District entered into a partnership with Public Utility District No. 1 of Klickitat County, Washington (KPUD) and two Washington Electric Co-ops to participate in the White Creek Wind Project. In December 2006 the District entered into an Energy Purchase Agreement with White Creek Wind I, LLC, for 46% of the energy generated by the Project. The White Creek Project has a total of 89 2.3MW wind turbines for an expected output of 204.7MW.

In November 2007 the White Creek Wind Project began energy production and the District paid \$85,572,237 million under the Amended and Restated White Creek Wind Project Energy Purchase Agreement with White Creek Wind I, LLC (Seller) in which the District agrees to purchase and the Seller is obligated to deliver, 46% of the energy produced by White Creek Wind Project for twenty years. With certain exceptions, under the terms of the Agreement, should the Seller deliver less than the Annual Energy Quantity (225,917 MWh) the Seller shall have the obligation to deliver to the District a quantity of energy equal to the Annual Energy Quantity shortfall on or before the third anniversary of the last day of the contract year the Annual Energy Quantity shortfall accrued. In 2009 the District share of output from the project was 263,415 MWhs.

Harvest Wind Project

In 2008 the District and three other utilities developed the Harvest Wind Project, a 98.9 MW wind generating facility located in Klickitat County, WA. The Project began commercial operation in December 2009 and the District's share of the Project is 30%. Each owner shares in power output, income and expenses according to their ownership shares. The District is committed, through an energy purchase agreement, to purchase its share of the output from the Project and pay its share of project expenses through the year 2029. Additionally, the District is committed, through a transmission service agreement and a transmission payment agreement to subsidize the initial construction of transmission lines, deposit funds to ensure contract performance, and purchase transmission from the owner of the transmission lines through the year 2029.

WATER SYSTEM

The Water Distribution System provides water service in some portions of Cowlitz County adjacent to the cities of Longview and Kelso. The system served 3,883 water customers in 2009. The source of supply for the water system comes from the Longview Regional Water Treatment Plant (RWTP), a joint venture of the District and the City of Longview.

Effective January 1, 2008, the District entered into an Inter-local Agreement with the Beacon Hill Sewer District (BHSD), a Washington municipal corporation pursuant to The Cooperation Act of the Revised Code of Washington Chapter 39.34. The Agreement provides a mechanism for an orderly transfer of the operation and maintenance of the District's Water System (System) by BHSD under joint oversight by the Boards of Commissioners of both the District and BHSD, for a three year transition period with the intention of the parties, should the parties elect to complete the transfer, whereby the District will convey full ownership of the System to BHSD on or before December 31, 2012. Should ownership be transferred to BHSD it is anticipated it will be in exchange for BHSD's pledge to continue to operate the System for the benefit of current and future customers and to accept both the assets and the liabilities of the System as they exist at the time of the transfer. Should the Agreement be terminated without the parties having reached agreement for final conveyance of the assets and liabilities of the System to BHSD, the District will resume full responsibility for operations and maintenance of the System.

Financial Summary and Analysis

The District raised water service rates 15% in March 2007, 15% in December 2007 and 15% in January 2009 in an effort to offset rising operating expenses and increasing capital requirements. Retail sales increased \$422, 955 or 37% due to the rate increase and increased consumption. Consumption in 2009 was more in line with overall sales history.

Due to silt deposits in the Cowlitz River near the intake for the Regional Water Treatment Plant, the District and the City of Longview are seeking a Public Works Trust Fund Loan to replace the treatment facility with a series of wells and treatment facilities at the City's Mint Farm industrial complex. The cost of the facility will be \$27.5 million, with the District's portion being \$3.78 million.

Selected Financial Data – Water System

	<u>2009</u>	<u>2008</u>
Current Assets	\$ 724,895	\$ 698,188
Net Utility Plant	6,119,386	6,228,069
Other Assets	1,399,503	1,050,439
Total Assets	8,243,784	7,976,696
Current Liabilities	503,794	267,353
Long-Term Debt	1,562,476	1,677,483
Other Liabilities	-	-
Total Liabilities	2,066,270	1,944,836
Total Net Assets	6,177,514	6,031,860
Operating Revenues	1,644,234	1,202,632
Operating Expenses	1,427,992	1,248,962
Net Operating Revenues	216,242	(46,330)
Other Income-(Expense)	(70,588)	(57,224)
Change in Net Assets	145,654	(103,554)

Capital Asset and Long-term Debt Activity

As of year-end, the Water System had \$10.51 million invested in a variety of capital assets. Utility Plant net of depreciation was \$6.12 million. Capital construction for this year was funded by a combination of aid-to-construction paid by customers and current revenues.

Total water system utility plant in service as of December 31, 2009 and 2008 consisted of the following:

	<u>2009</u>	<u>2008</u>
Land Rights	\$ 269,147	\$ 269,147
Distribution	9,962,308	9,918,420
General Plant	<u>278,062</u>	<u>271,040</u>
Total Plant In Service	<u>\$ 10,509,517</u>	<u>\$ 10,458,607</u>

At year-end, the Water System had \$971,145 in loans outstanding from the Electric System and \$584,283 in Public Works Trust Fund Loans from the State of Washington. The debt has been incurred over the years to provide for the construction of capital facilities. In January 2008 the District received a promissory note from Beacon Hill Sewer District (BHSD) for vehicles purchased from the District. The note, which carries an annual interest rate of 5%, is payable upon closing of the Water System sale to BHSD. At year end, the balance outstanding was \$127, 866.

PRODUCTION SYSTEM

In 2009 the Electric System purchased \$9.71 million in power from the Swift No. 2 Hydroelectric Production System. This amount was used to cover operating costs, debt service and to fund reserves.

On April 21, 2002 the Swift No. 2 Hydroelectric Production System suffered a failure of the power canal embankment, which led to significant damage to the powerhouse and transmission switchyard. The casualty insurance carrier, Lloyds of London, agreed that coverage existed under the policy, and paid the \$70 million policy limit. In February 2004 the property insurance carriers, Federated Rural Electric Insurance Exchange and TIG Insurance Company denied coverage and filed a motion in Federal District Court in Tacoma, Washington seeking a judicial declaration that there was no coverage under these

insurance policies for the PUD's claimed loss. The U.S. District Court granted the District's motion for summary judgment in March 2006 agreeing with the District that Federated and TIG were obligated to provide coverage and in August 2006 the District received \$13.9 million as its portion of a \$25 million settlement from Federated. With respect to TIG's appeal, on September 19, 2008 the Ninth Circuit Court of Appeals affirmed the District Court's judgment against TIG and on October 31, 2008, the Court denied TIG's petition for rehearing and in late 2008 the District received \$16,687,088 from the insurer.

In August 2004 the District issued Production System bonds for \$42.2 million to cover the costs of the embankment rehabilitation not covered by insurance. The bonds mature serially over a 30-year period and have interest rates varying from 3.00% to 5.00%. Principal payments on these bonds began in 2006. In August 2006 the District issued Production System bonds for \$27.5 million. These bonds are to finance continuing expenditures for project reconstruction and to provide for capital expenditures associated with FERC licensing.

Selected Financial Data – Production System

	<u>2009</u>	<u>2008</u>
Current Assets	\$ 30,056,256	\$ 20,990,964
Net Utility Plant	134,446,459	119,683,153
Other Assets	28,900,318	39,351,501
Total Assets	193,403,033	180,025,618
Current Liabilities	5,932,773	2,829,987
Long-Term Debt	66,777,176	67,702,627
Other Liabilities	10,812,220	-
Total Liabilities	83,522,169	70,532,614
Total Net Assets	109,880,864	109,493,004
Operating Revenues	9,706,802	9,113,099
Operating Expenses	7,212,120	6,012,091
Net Operating Revenues	2,494,682	3,101,008
Other Income-(Expense)	(2,106,822)	14,790,498
Change in Net Assets	387,860	17,891,506

Total Production System plant in service as of December 31, 2009 and 2008 consisted of the following:

	<u>2009</u>	<u>2008</u>
Intangible	\$ 4,683,880	\$ 4,683,880
Production Plant	145,077,460	127,655,741
Transmission Plant	<u>4,624,838</u>	<u>4,624,838</u>
Total Plant In Service	<u>\$ 154,386,178</u>	<u>\$ 136,964,459</u>

PUBLIC UTILITY DISTRICT NO 1 OF COWLITZ COUNTY, WASHINGTON
BALANCE SHEET
December 31, 2009

	Electric System	Water System	Production System	Total
ASSETS				
CURRENT ASSETS				
Cash and investments (Notes 1 and 2)	\$ 18,945,793	\$ 371,473	\$ 19,842,094	\$ 39,159,360
Customer accounts receivable and unbilled revenues (Note 1)	19,031,376	233,254	-	19,264,630
Other accounts receivable	3,115,513	-	-	3,115,513
Less - accum. prov. for uncollectible accounts	(1,391,007)	(13,995)	-	(1,405,002)
Accounts receivable from assoc. companies (Note 1)	173,332	-	-	173,332
Interfund note receivable (Note 6)	-	-	9,000,000	9,000,000
Current portion of advances to other funds (Note 7)	69,328	-	525,473	594,801
Materials and supplies (Note 1)	4,098,850	84,855	-	4,183,705
Prepayments	569,759	49,308	352,032	971,099
Interest receivable	17,016	-	336,657	353,673
Other current assets	130,089	-	-	130,089
TOTAL CURRENT ASSETS	44,760,049	724,895	30,056,256	75,541,200
RESTRICTED ASSETS				
Cash and investments (Notes 1 and 2)	42,733,212	-	14,291,307	57,024,519
Interest receivable	199,561	-	-	199,561
TOTAL RESTRICTED ASSETS	42,932,773	-	14,291,307	57,224,080
NONCURRENT ASSETS				
UTILITY PLANT (Notes 1 and 3)				
Plant in service	230,851,048	10,509,517	154,386,178	395,746,743
Construction in progress	11,784,600	125,578	379,181	12,289,359
TOTAL UTILITY PLANT	242,635,648	10,635,095	154,765,359	408,036,102
Less - accumulated provision for depreciation and amortization	(100,160,623)	(4,515,709)	(20,318,900)	(124,995,232)
NET UTILITY PLANT	142,475,025	6,119,386	134,446,459	283,040,870
OTHER PROPERTY AND INVESTMENTS (Note 4)				
White Creek Wind Project Energy Purchase Agreement (Notes 4 and 10)	76,576,977	-	-	76,576,977
Investment in associated organizations	61,942,417	1,399,503	-	63,341,920
BPA transmission credit receivable	4,774,225	-	-	4,774,225
Note receivable	127,866	-	-	127,866
Advances to other funds	901,817	-	13,709,546	14,611,363
TOTAL OTHER PROPERTY AND INVESTMENTS	144,323,302	1,399,503	13,709,546	159,432,351
DEFERRED CHARGES (Note 5)				
Unamortized bond issue costs	1,312,500	-	899,465	2,211,965
Unamortized loss on reacquired debt	130,358	-	-	130,358
Prepaid Harvest Wind Project costs	3,374,986	-	-	3,374,986
Miscellaneous deferred charges	50,957	-	-	50,957
TOTAL DEFERRED CHARGES	4,868,801	-	899,465	5,768,266
TOTAL ASSETS	\$ 379,359,950	\$ 8,243,784	\$ 193,403,033	\$ 581,006,767

The accompanying notes are an integral part of these combined statements.

PUBLIC UTILITY DISTRICT NO 1 OF COWLITZ COUNTY, WASHINGTON
BALANCE SHEET
December 31, 2009

	Electric System	Water System	Production System	Total
<u>LIABILITIES</u>				
CURRENT LIABILITIES				
Warrants outstanding	\$ 1,010,685	\$ 348	\$ 71,227	\$ 1,082,260
Current portion of long-term debt (Note 7)	6,680,473	120,818	855,000	7,656,291
Current portion of Lewis River Cost-Share Agreement (Note 8)	-	-	3,378,818	3,378,818
Short-term borrowing (Note 6)	39,000,000	-	-	39,000,000
Accounts payable	21,038,708	273,766	317,185	21,629,659
Accounts payable to assoc. companies (Note 1)	-	53,712	119,620	173,332
Accrued wages and benefits	1,599,594	44,343	-	1,643,937
Customer deposits	4,635,610	-	-	4,635,610
Taxes payable	3,666,419	9,251	89,671	3,765,341
Interest payable	2,497,051	1,556	1,080,753	3,579,360
Other current liabilities	76,103	-	20,499	96,602
TOTAL CURRENT AND ACCRUED LIABILITIES	80,204,643	503,794	5,932,773	86,641,210
LONG-TERM DEBT (Note 7)				
Bonds payable	127,910,000	-	65,685,000	193,595,000
Premium on bonds payable	3,149,997	-	1,092,176	4,242,173
Advances from other funds	13,709,546	901,817	-	14,611,363
Loans payable	800,000	660,659	-	1,460,659
TOTAL LONG-TERM LIABILITIES	145,569,543	1,562,476	66,777,176	213,909,195
OTHER LIABILITIES AND DEFERRED CREDITS (Note 8)				
Lewis River Cost Share Agreement	-	-	10,812,220	10,812,220
Deferred revenue - rate stabilization fund	7,700,000	-	-	7,700,000
Personal leave and retirement reserves	1,090,714	-	-	1,090,714
Insurance reserves and other deferred credits	1,349,005	-	-	1,349,005
Post-retirement benefit obligation	152,024	-	-	152,024
TOTAL OTHER LIABILITIES	10,291,743	-	10,812,220	21,103,963
TOTAL LIABILITIES	236,065,929	2,066,270	83,522,169	321,654,368
COMMITMENTS AND CONTINGENCIES (Note 10)				
<u>NET ASSETS</u>				
Invested in capital assets, net of related debt	94,422,327	4,436,092	53,522,710	152,381,129
Restricted	27,719,629	1,399,503	11,291,307	40,410,439
Unappropriated	21,152,065	341,919	45,066,847	66,560,831
TOTAL NET ASSETS	143,294,021	6,177,514	109,880,864	259,352,399
TOTAL LIABILITIES AND NET ASSETS	\$ 379,359,950	\$ 8,243,784	\$ 193,403,033	\$ 581,006,767

The accompanying notes are an integral part of these combined statements.

PUBLIC UTILITY DISTRICT NO 1 OF COWLITZ COUNTY, WASHINGTON
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
For the Year Ended December 31, 2009

	Electric System	Water System	Production System	Total
OPERATING REVENUES				
Retail sales	\$ 175,971,128	\$ 1,573,104	\$ 9,706,802	\$ 187,251,034
Wholesale sales	19,018,465	-	-	19,018,465
Other operating revenues	2,595,532	71,130	-	2,666,662
TOTAL OPERATING REVENUES	197,585,125	1,644,234	9,706,802	208,936,161
OPERATING EXPENSES				
Operations expense	164,864,076	733,668	2,883,414	168,481,158
Maintenance expense	4,630,859	334,052	1,201,087	6,165,998
Depreciation and amortization	7,093,238	283,600	3,037,594	10,414,432
Taxes	9,519,323	76,672	90,025	9,686,020
TOTAL OPERATING EXPENSES	186,107,496	1,427,992	7,212,120	194,747,608
NET OPERATING REVENUES	11,477,629	216,242	2,494,682	14,188,553
OTHER INCOME-(EXPENSES)				
Interest and dividend income	882,376	2,298	1,116,210	2,000,884
Interest on long-term debt	(7,235,005)	(54,108)	(3,189,820)	(10,478,933)
Amortization of debt expense	(200,869)	-	(33,312)	(234,181)
Loss from joint venture	-	(18,778)	-	(18,778)
Miscellaneous nonoperating income-(expenses)	(490,423)	-	100	(490,323)
TOTAL OTHER INCOME-(EXPENSES)	(7,043,921)	(70,588)	(2,106,822)	(9,221,331)
CHANGE IN NET ASSETS	4,433,708	145,654	387,860	4,967,222
TOTAL NET ASSETS AT BEGINNING OF YEAR	138,860,313	6,031,860	109,493,004	254,385,177
TOTAL NET ASSETS AT END OF YEAR	\$ 143,294,021	\$ 6,177,514	\$ 109,880,864	\$ 259,352,399

The accompanying notes are an integral part of these combined statements.

PUBLIC UTILITY DISTRICT NO 1 OF COWLITZ COUNTY, WASHINGTON
STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2009

	Electric System	Water System	Production System	Total
CASH FLOWS RELATED TO OPERATING ACTIVITIES				
Cash received from customers	\$ 195,318,745	\$ 1,579,780	\$ 9,706,802	\$ 206,605,327
Cash payments to suppliers	(151,642,557)	(466,375)	(4,373,815)	(156,482,747)
Cash paid to employees for services	(10,811,009)	(387,923)	-	(11,198,932)
Taxes paid	(9,988,083)	(67,421)	(88,917)	(10,144,421)
NET CASH PROVIDED BY-(USED IN) OPERATING ACTIVITIES	22,877,096	658,061	5,244,070	28,779,227
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Intersystem financing - principal	(502,394)	-	502,394	-
Intersystem financing - interest	(652,906)	-	652,906	-
NET CASH PROVIDED BY-(USED IN) NONCAPITAL FINANCING ACTIVITIES	(1,155,300)	-	1,155,300	-
CASH FLOW FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Capital construction	(26,750,850)	(174,917)	(3,609,862)	(30,535,629)
Principal paid on long-term debt	(3,635,000)	(111,962)	(830,000)	(4,576,962)
Proceeds-(advances) from loans and notes payable	39,000,000	-	(9,000,000)	30,000,000
Interest paid on long-term debt, loans and notes payable	(6,693,919)	(54,545)	(3,269,232)	(10,017,696)
Investment in associated organizations	66,283	(367,842)	-	(301,559)
Investment in Harvest Wind Project	(51,182,471)	-	-	(51,182,471)
Prepaid Harvest Wind Project costs	(3,374,986)	-	-	(3,374,986)
Deferred charges	120,645	-	-	120,645
Deferred credits	602,169	-	-	602,169
Proceeds from insurance settlement	-	-	2,245,716	2,245,716
Miscellaneous nonoperating income	(251,227)	-	100	(251,127)
NET CASH PROVIDED BY-(USED IN) CAPITAL AND RELATED FINANCING ACTIVITIES	(52,099,356)	(709,266)	(14,463,278)	(67,271,900)
CASH FLOWS FROM INVESTING ACTIVITIES				
Purchase of investment securities	(6,876,044)	-	(2,493,134)	(9,369,178)
Proceeds from maturity of investment securities	35,759,398	-	2,493,134	38,252,532
Interest and dividends on investments	998,432	2,298	193,910	1,194,640
NET CASH PROVIDED BY-(USED IN) INVESTING ACTIVITIES	29,881,786	2,298	193,910	30,077,994
NET INCREASE-(DECREASE) IN CASH AND EQUIVALENTS	(495,774)	(48,907)	(7,869,998)	(8,414,679)
CASH AND CASH EQUIVALENTS AT BEG. OF THE YEAR	59,092,098	420,380	42,003,399	101,515,877
CASH AND CASH EQUIVALENTS AT END OF THE YEAR	\$ 58,596,324	\$ 371,473	\$ 34,133,401	\$ 93,101,198

The accompanying notes are an integral part of these combined statements.

PUBLIC UTILITY DISTRICT NO 1 OF COWLITZ COUNTY, WASHINGTON
STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2009

	Electric System	Water System	Production System	Total
RECONCILIATION OF NET OPERATING REVENUES TO NET CASH PROVIDED BY OPERATING ACTIVITIES				
Net Operating Revenues	\$ 11,477,629	\$ 216,242	\$ 2,494,682	\$ 14,188,553
ADJUSTMENTS TO RECONCILE NET OPERATING REVENUES TO NET CASH PROVIDED BY OPERATING ACTIVITIES				
Depreciation and amortization of utility plant	7,093,238	283,600	3,037,594	10,414,432
Amortization of energy purchase agreement	4,317,725	-	-	4,317,725
(Increase)-decrease in:				
Accounts receivable and unbilled revenue	319,817	(65,573)	-	254,244
Other accounts receivable	(2,773,140)	1,119	-	(2,772,021)
Accounts receivable from associated companies	251,522	-	-	251,522
Materials and supplies	(450,744)	(8,258)	-	(459,002)
Prepayments	(43,617)	(2,902)	3,865	(42,654)
Other current assets	(62,027)	-	-	(62,027)
BPA transmission credit receivable	429,900	-	-	429,900
Increase-(decrease) in:				
Warrants outstanding	(321,256)	(71)	7,461	(313,866)
Accounts payable	2,446,217	204,992	(60,884)	2,590,325
Accounts payable to associated companies	-	3,605	(255,127)	(251,522)
Accrued wages and benefits	174,062	16,056	-	190,118
Customer deposits	186,943	-	-	186,943
Taxes payable	(468,760)	9,251	1,108	(458,401)
Other accrued liabilities	4,949	-	15,371	20,320
Post-retirement benefit obligation	147,319	-	-	147,319
NET CASH PROVIDED BY -(USED IN) OPERATING ACTIVITIES	\$ 22,729,777	\$ 658,061	\$ 5,244,070	\$ 28,631,908
NONCASH CAPITAL AND FINANCING ACTIVITIES				
Plant in service	\$ -	\$ -	\$ (14,191,038)	\$ (14,191,038)
Lewis River Cost-Share Agreement	-	-	14,191,038	14,191,038
TOTAL NONCASH CAPITAL AND RELATED FINANCING ACTIVITIES	\$ -	\$ -	\$ -	\$ -

The accompanying notes are an integral part of these combined statements.

PUBLIC UTILITY DISTRICT NO. 1 OF COWLITZ COUNTY
NOTES TO THE COMBINED FINANCIAL STATEMENTS
For the Year Ended December 31, 2009

These notes are an integral part of the accompanying financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the District conform to generally accepted accounting principles (GAAP) as applicable to governmental electric utilities. Pursuant to Statement 20 of the Governmental Accounting Standards Board (GASB) "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting," the District uses as guidance Financial Accounting Standards Board (FASB) pronouncements except those that are in conflict with or contradict GASB pronouncements.

On July 1, 2009, the FASB Accounting Standards Codification became the single authoritative source of non-governmental U.S. GAAP. The codification supersedes all previous FASB guidance that was applicable to the District.

A. Reporting Entity

Public Utility District No. 1 of Cowlitz County, Washington (District) was created by vote of the qualified electors of Cowlitz County on November 3, 1936 and operates under the laws of the State of Washington applicable to a Municipal Corporation. The District is governed by an elected three member board.

As required by generally accepted accounting principles, management has considered all potential component units in defining the reporting entity. The District's financial statements include the financial position, results of operations and cash flows of all systems which the District owns and manages which include the Electric Distribution System, the Water System, and the Production System (Lewis River Swift Plant No. 2 Hydroelectric System).

B. Basis of Combined Financial Statements

The accounting records of the District are maintained in accordance with methods prescribed by the State Auditor under the authority of Chapter 43.09 RCW. The District uses the Federal Energy Regulatory Commission's (FERC) Uniform System of Accounts for Public Utilities and Licensees.

The District uses the full-accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Accordingly, revenues are recorded net of the allowance for doubtful accounts and estimated revenues are accrued for power deliveries not yet billed.

C. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities 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.

D. Reclassifications

Certain prior year amounts have been reclassified to conform to current year presentation. Such reclassifications do not effect changes in total net assets previously reported.

E. Cash and Cash Equivalents

For the purpose of the Statement of Cash Flows, the District considers highly liquid, short-term investments with original maturities of three months or less to be cash equivalents.

F. Investments

Investments are carried at cost which approximates fair market value, as the District's investments are short-term.

G. Utility Plant and Depreciation

Utility plant asset purchases are capitalized and long-term liabilities are accounted for in the appropriate funds. Major expenses for capital assets 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 cost is known. Where historical cost is not known, assets are recorded at estimated cost. Contributions by developers and customers are recorded at contract price or cost as contributions in aid-of-construction. When developers install and cover the costs of the infrastructure directly, those assets are referred to as contributed plant assets. The District records depreciation on assets acquired by contributions. Cost of assets retired are removed from the asset accounts and charged to the accumulated depreciation accounts, together with removal costs less any proceeds from sales.

Depreciation is computed on the straight-line method with useful lives of 3 to 50 years. Estimated useful lives for Production System properties are as follows: Distribution Plant - 20 to 33 years, Transmission Plant - 33 years; General Plant - 4 to 50 years, Production Plant - 10 to 50 years; FERC license - 50 years; Water Rights - 50 years.

H. Bad Debts

Bad debt expense is debited and the accumulated provision for uncollectible accounts is credited monthly with a budgeted amount that provides for losses on accounts receivable which may become uncollectible. Actual losses between twelve and fifteen months old are then charged against the provision for uncollectible accounts quarterly.

I. Materials and Supplies

Inventories of materials and supplies are valued at cost. The inventory consists of expendable supplies held for construction and maintenance on the District's Electric System and Water System. Unit cost is determined by the average cost method.

J. Compensated Absences

The District accrues personal leave benefits as the obligation is incurred.

K. Interfund Balances and Transactions

The District's Electric Distribution makes payments for goods, services, and taxes on behalf of the Water System and the Production System. This is reflected in the balance sheet as "accounts receivable from associated companies." Alternatively, the amounts due by the Water System and the Production System to the Electric System are reflected in the balance sheet as "accounts payable to associated companies." These accounts include only short-term obligations which are paid monthly and they are not interfund loans. A description of long-term advances between funds is contained in Note 7.

L. Regulatory Deferrals

The District has deferred revenues to be used in future periods as allowed by Statement of Financial Accounting Standards No. 71, *Accounting for the Effects of Certain Types of Regulation*, which states that recognition of revenues and expenses should be matched in the time periods when the revenues and expenses are included in rates.

M. Operating Revenues

Approximately 50.5% of Electric System retail sales were the result of two industrial customers.

2. DEPOSITS AND INVESTMENTS

The District's deposits and investments are entirely covered by the Federal Depository Insurance Corporation (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

Deposits and Investments as of December 31, 2009 consist of the following:

	<u>Electric System</u>	<u>Water System</u>	<u>Production System</u>	<u>Total</u>
Cash on hand	\$ 2,550	\$ -	\$ -	\$ 2,550
Cash in bank	30,198,815	12,476	13,093,113	43,304,404
Cash with Cowlitz County Treasurer	-	358,997	-	358,997
Investment in State Treasurer Investment Pool	20,041,245	-	20,541,805	40,583,050
Certificates of deposits with banks	5,206,395	-	-	5,206,395
Investments	<u>6,230,000</u>	<u>-</u>	<u>498,483</u>	<u>6,728,483</u>
 Total deposits and investments	 <u>\$61,679,005</u>	 <u>\$371,473</u>	 <u>\$34,133,401</u>	 <u>\$96,183,879</u>
 Unrestricted:				
Cash and cash equivalents	<u>\$18,945,793</u>	<u>\$371,473</u>	<u>\$19,842,094</u>	<u>\$39,159,360</u>
 Restricted:				
Cash and cash equivalents:				
Construction funds	\$19,925,048	\$ -	\$11,332,333	\$31,257,381
Bond reserve accounts	7,794,581	-	2,958,974	10,753,555
Rate stabilization fund	7,700,000	-	-	7,700,000
Customer deposits	3,045,867	-	-	3,045,867
Vacation and retirement reserve	<u>1,037,716</u>	<u>-</u>	<u>-</u>	<u>1,037,716</u>
 Total cash and cash equivalents	 <u>39,503,212</u>	 <u>-</u>	 <u>14,291,307</u>	 <u>53,794,519</u>
 Temporary cash investments:				
Construction funds	<u>3,230,000</u>	<u>-</u>	<u>-</u>	<u>3,230,000</u>
 Total restricted	 <u>\$42,733,212</u>	 <u>\$ -</u>	 <u>\$14,291,307</u>	 <u>\$57,024,519</u>
 Total deposits and investments	 <u>\$61,679,005</u>	 <u>\$371,473</u>	 <u>\$34,133,401</u>	 <u>\$96,183,879</u>

Investments as of December 31, 2009 consist of the following:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Investment Maturities</u>	
		<u>Less Than 1 Year</u>	<u>1 to 2 Years</u>
U.S. Treasury Bills	\$ 499,941	\$ 499,941	\$ -
Federal National Mortgage Association	1,000,896	1,000,896	-
Federal Home Loan Bank	3,258,522	3,258,522	-
Federal Home Loan Mortgage Corporation	1,001,973	1,001,973	-
Federal Farm Credit Bank	1,014,198	503,377	510,821
Totals	<u>\$ 6,775,530</u>	<u>\$ 6,264,709</u>	<u>\$ 510,821</u>

Custodial credit risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. All the aforementioned investments are held in the District's name by a third-party custodian. As required by state law and District policy, all investments of the District's funds are obligations of the U.S. Government or deposits with Washington State banks and savings and loan institutions. The District does not have a formal investment policy that requires diversification of investments by security type and institution or that limits its exposure to fair value losses resulting from rising interest rates.

3. UTILITY PLANT AND DEPRECIATION

A schedule of changes in utility plant and depreciation follows:

	<u>Balance</u>			<u>Balance</u>
	<u>Jan. 1, 2009</u>	<u>Increases</u>	<u>Decreases</u>	<u>Dec. 31, 2009</u>
<u>Electric System Utility Plant</u>				
Intangible ⁽¹⁾	\$ 215,249	\$ 12,173	\$ -	\$ 227,422
Land and Land Rights ⁽¹⁾	3,214,962	201,876	-	3,416,838
Transmission	16,121,169	2,961,864	98,286	18,984,747
Distribution	160,335,299	18,556,169	1,827,974	177,063,494
General Plant	<u>28,263,223</u>	<u>3,627,954</u>	<u>732,630</u>	<u>31,158,547</u>
Plant in Service	208,149,902	25,360,036	2,658,890	230,851,048
Construction in Progress	<u>7,344,307</u>	<u>29,800,329</u>	<u>25,360,036</u>	<u>11,784,600</u>
Total Utility Plant	215,494,209	55,160,365	28,018,926	242,635,648
Less Accumulated Depreciation	<u>(95,201,154)</u>	<u>(7,469,431)</u>	<u>(2,509,962)</u>	<u>(100,160,623)</u>
Net Electric System Utility Plant	<u>\$ 120,293,055</u>	<u>\$ 47,690,934</u>	<u>\$ 25,508,964</u>	<u>\$ 142,475,025</u>

	Balance Jan. 1, 2009	Increases	Decreases	Balance Dec. 31, 2009
<u>Water System Utility Plant</u>				
Land and Land Rights ⁽¹⁾	\$ 269,147	\$ -	\$ -	\$ 269,147
Distribution	9,918,420	43,888	-	9,962,308
General Plant	<u>271,040</u>	<u>11,740</u>	<u>4,718</u>	<u>278,062</u>
Plant in Service	10,458,607	55,628	4,718	10,509,517
Construction in Progress	<u>1,571</u>	<u>124,007</u>	<u>-</u>	<u>125,578</u>
Total Utility Plant	10,460,178	179,635	4,718	10,635,095
Less Accumulated Depreciation	<u>(4,232,109)</u>	<u>(283,600)</u>	<u>-</u>	<u>(4,515,709)</u>
Net Water System Utility Plant	<u>\$ 6,228,069</u>	<u>\$ (103,965)</u>	<u>\$ 4,718</u>	<u>\$ 6,119,386</u>
<u>Production System Utility Plant</u>				
Intangible	\$ 4,683,880	\$ -	\$ -	\$ 4,683,880
Land and Land Rights ⁽¹⁾	1,224,229	-	-	1,224,229
Production	126,431,512	17,421,719	-	143,853,231
Transmission	<u>4,624,838</u>	<u>-</u>	<u>-</u>	<u>4,624,838</u>
Plant in Service	136,964,459	17,421,719	-	154,386,178
Construction in Progress	<u>-</u>	<u>379,181</u>	<u>-</u>	<u>379,181</u>
Total Utility Plant	136,964,459	17,800,900	-	154,765,359
Less Accumulated Depreciation and Amortization	<u>(17,281,306)</u>	<u>(3,037,594)</u>	<u>-</u>	<u>(20,318,900)</u>
Net Production System Utility Plant	<u>\$ 119,683,153</u>	<u>\$ 14,763,306</u>	<u>\$ -</u>	<u>\$ 134,446,459</u>

(1) Plant not being depreciated.

4. OTHER PROPERTY AND INVESTMENTS

Other property and investments at December 31, 2009 consist of the following:

	Electric System	Water System	Production System
White Creek Wind Project Energy Purchase Agreement	\$ 76,576,977	\$ -	\$ -
Investment in associated companies	61,942,417	1,399,503	-
BPA transmission credit receivable	4,774,225	-	-
Note receivable	127,866	-	-
Advances to other funds	<u>901,817</u>	<u>-</u>	<u>13,709,500</u>
Totals	<u>\$ 144,323,302</u>	<u>\$ 1,399,503</u>	<u>\$ 13,709,500</u>

White Creek Wind Project Energy Purchase Agreement

In November 2007 the White Creek Wind Project began energy production and the District paid \$85,572,237 million under the Amended and Restated White Creek Wind Project Energy Purchase Agreement to receive a 46% share of the energy from the Project for 20 years. This payment was made with unrestricted cash and investments held by the Electric System (\$70,354,497) and from the Production System (\$15,217,740). The prepayment is being amortized on a straight-line basis over the life of the contract.

Investment in Associated Companies

Investments in associated companies at December 31, 2009 consist of the following:

	<u>Electric System</u>	<u>Water System</u>	<u>Production System</u>
Investment in Harvest Wind Project	\$ 61,802,499	\$ -	\$ -
Investment in White Creek Project, LLC	139,918	-	-
Investment in Regional Water Treatment Plant	-	1,399,503	-
Totals	<u>\$ 61,942,417</u>	<u>\$ 1,399,503</u>	<u>\$ -</u>

Investment in Harvest Wind Project

The District is a party to a Joint Ownership Agreement whereby the District made an equity investment in the Harvest Wind Project, a 98.9 MW wind generating facility located in Klickitat County, WA. The District's share of the Project is 30%. Other owners are Lakeview Light & Power, 30%, Peninsula Light Co., 20%, and Eugene Water and Electric Board, 20%. During 2009, the joint owners of Harvest Wind elected to classify the Project as a taxable corporation. At the time of the election all project assets were treated as contributed to the corporation and the joint owners received shares in proportion to their ownership. Owners share in power output, income and expenses according to their ownership shares.

The investment in Harvest Wind consists of the District's share of the costs to develop the Project, 30% of Project's net income and losses, and any preferred distributions. No distributions were received in 2009. Commercial operations began on December 15, 2009. At December 31, 2008, prior to election to incorporate, the District had recorded \$10,620,028 as preliminary survey and investigation.

The District is committed, through an energy purchase agreement, to purchase its share of the output from the Project and pay its share of project expenses through the year 2029. Additionally, the District is committed, through a transmission service agreement and a transmission payment agreement, to subsidize the initial construction of transmission lines, deposit funds to ensure contract performance, and purchase transmission from the owner of the transmission lines through the year 2029.

Investment in White Creek Project, LLC

At December 31, 2009 the District has \$139,918 residing with White Creek Project LLC (WCP, LLC), which is being carried as an equity investment. Assets of WCP, LLC consist of cash and other assets related to the White Creek Wind Project Phases I and II.

Investment in Regional Water Treatment Plant

In December 1978, the District entered into an agreement with the City of Longview to construct the Regional Water Treatment Plant (RWTP). The arrangement was organized to acquire and construct a new facility to provide treated water to the residents of the two entities at the lowest reasonable cost consistent with reliability, safety, and expedition. Ownership in this joint venture is based on total historical usage from the plant. The ratio at the end of 2009 is 14.40 percent for

the District and 85.60 percent for the City of Longview with operating and capital financing participation accordingly. A three-member board, comprised of two City representatives and one District representative, administer the joint venture. Water wheeling agreements are in effect between the District and the cities of Longview and Kelso providing for the delivery of water from the RWTP to the respective areas of the District's Water System. Complete financial statements for the RWTP can be obtained from the City of Longview. The RWTP is a joint venture reported under the equity method. The District's current share of the project at December 31, 2009 is \$1,399,503

BPA Transmission Credit Receivable

In October 2007 the White Creek Wind Project assigned 46% of its Bonneville Power Administration (BPA) transmission credit to the District. For the term of the agreement beginning January 1, 2008 and ending the sooner of the exhaustion of the assigned credit or on January 1, 2021, the District will receive amounts for use of the facilities from BPA. During 2009 the District received \$429,900 under this agreement.

Note Receivable and Advances to Other Funds

In January 2008 the District received a promissory note from Beacon Hill Sewer District (BHSD) for vehicles and equipment purchased from the District. The note, which carries an annual interest rate of 5%, is payable upon closing of the Water System sale to BHSD which is described in Note 11. A description of long-term advances to other funds is provided in Note 7.

5. DEFERRED CHARGES

Deferred charges at December 31, 2009 consist of the following:

	<u>Electric System</u>	<u>Production System</u>
Unamortized bond issue costs	\$ 1,312,500	\$ 899,465
Unamortized loss on reacquired debt	130,358	-
Prepaid Harvest Wind Project costs	3,374,986	-
Miscellaneous deferred charges	<u>50,957</u>	<u>-</u>
Totals	<u>\$ 4,868,801</u>	<u>\$ 899,465</u>

Unamortized bond issue costs are being amortized over the life of the respective bond issue. The unamortized loss on reacquired debt is being amortized over the remaining life of the original issue.

Prepaid Harvest Wind Project costs include transmission system costs of \$3,079,020 and financing costs of \$295,966. These costs are being amortized on a straight-line basis over 20 years.

6. SHORT-TERM NOTES PAYABLE

Interfund Loan – Production and Distribution Systems

On March 24, 2009 the District's Board of Commissioners authorized and approved a loan of not more than \$25 million from the Production System to the Electric System for the purpose of developing the Harvest Wind Project. The interest rate on the loan is set at 4.5% and shall be repaid from proceeds received at the closing of the sale of the Project or from proceeds of a bond sale should the District retain ownership in the project. As of December 31, 2009, \$9 million has been drawn on this loan.

Purchase Agreement – Short-term Revenue Note with Bank of America

On June 30, 2009 the District entered into a Purchase Agreement with Bank of America for a \$60 million Short-Term Revenue Note the proceeds of which are being used for construction of the

Harvest Wind Project. The interest rate on the Note is determined at the time of each draw and the District may select from between the LIBOR Daily Floating Rate and the LIBOR Fixed Option Rate. The original maturity date was December 31, 2009; however, the maturity has been extended until April 30, 2010. At December 31, 2009, the District had \$30 million outstanding on this obligation.

7. LONG-TERM DEBT

Electric System

Revenue Bonds

During 2001 the District issued \$48.675 million in Electric Distribution System Revenue Bonds. These bonds were used to pay off the existing lines of credit and to provide for capital requirements. The bonds mature serially in varying amounts and have annual interest rates ranging from 5.00% to 5.25%. Pursuant to the bond resolution, the District elected to purchase municipal bond insurance in lieu of the maintenance of bond reserve funds to guarantee the principal and interest payments to the bondholders.

In August 2006 the District issued \$61.465 million in Revenue and Refunding Bonds to fund capital improvements, repay \$8 million on the line of credit, pay for bond issuance costs, including bond insurance, fund the bond reserve account (\$2,373,256), and to refund \$11.635 million of outstanding 2001 Electric Distribution System Revenue Bonds (Series 2001 Bonds). Of the net proceeds, \$12.080 million was used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide future debt service payments on a portion of the Series 2001 Bonds maturing on September 1, 2007 through 2011. As of December 31, 2009 \$4,955,000 of Series 2001 Bonds are considered to be defeased and the liability for those bonds is not included in the District's financial statements. The primary purpose for the refunding was to restructure debt maturities. The District recorded an accounting loss of \$445,286 which is being amortized over the remaining life of the Series 2001 Bonds. Principal payments on the 2006 Revenue and Refunding Bonds are scheduled to begin in September 2012, maturing annually in varying amounts through Sept 2026. The bonds have annual interest rates ranging from 4.50% to 5.00%.

In November 2007 the District issued \$64.755 million in Electric System Revenue Bonds to fund capital improvements, pay for bond issuance costs (including bond insurance) and fund bond debt service and reserve accounts (\$5,421,325). Principal payments on these bonds are scheduled to begin in September 2010, maturing annually in varying amounts through Sept 2027. The bonds have annual interest rates ranging from 4.375 % to 5.00%.

Scheduled principal maturities and interest requirements on the Revenue Bonds are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 6,155,000	\$ 6,503,081	\$ 12,658,081
2011	6,465,000	6,195,331	12,660,331
2012	6,790,000	5,872,081	12,662,081
2013	5,625,000	5,532,581	11,157,581
2014	5,905,000	5,251,331	11,156,331
2015 - 2019	34,260,000	21,521,405	55,781,405
2020 - 2024	43,315,000	12,475,489	55,790,489
2025 - 2027	<u>25,550,000</u>	<u>2,186,301</u>	<u>27,736,301</u>
Total	<u>\$ 134,065,000</u>	<u>\$ 65,537,600</u>	<u>\$ 199,602,600</u>

Loan Payable

In 2007 the District entered into a contract for a general obligation loan in the amount of \$800,000 and a \$200,000 grant from the State of Washington Community Economic Revitalization Board. The loan is to be repaid at the rate of 1.60% per annum over a twenty-year term. The terms of the contract provide a deferral of principal and interest repayments. The District is using these funds to provide

power to a new business at the Port of Kalama. During 2007 the District received \$685,729 in loan funds and the balance of loan and grant funds were received in 2008. Scheduled principal maturities and interest requirements on the loan are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ -	\$ -	\$ -
2011	-	38,400	38,400
2012	41,322	12,800	54,122
2013	41,983	12,139	54,122
2014	42,655	11,467	54,122
2015 - 2019	223,731	46,878	270,609
2020 - 2024	242,212	28,397	270,609
2025 - 2028	<u>208,097</u>	<u>8,390</u>	<u>216,487</u>
Total	<u>\$ 800,000</u>	<u>\$ 158,471</u>	<u>\$ 958,471</u>

Water System

Since 1989 the District has received Public Works Trust Fund loans from the Washington State Department of Community Development that have been used to partially fund water system projects. Each of the loans is to be paid back over a twenty-year period at interest rates from one-half to one percent. Scheduled principal maturities and interest requirements Public Works Trust Fund loans are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 51,490	\$ 3,111	\$ 54,601
2011	51,490	2,806	54,296
2012	51,490	2,501	53,991
2013	51,490	2,197	53,687
2014	42,003	1,892	43,895
2015 - 2019	210,015	6,308	216,323
2020 - 2023	<u>126,305</u>	<u>1,370</u>	<u>127,675</u>
Total	<u>\$ 584,283</u>	<u>\$ 20,185</u>	<u>\$ 604,468</u>

Production System

In August 2004 the District issued Production System (Lewis River Swift No. 2) bonds for \$42.2 million to cover the costs of the embankment rehabilitation. The bonds mature serially over a 30-year period and have interest rates varying from 3.00% to 5.00%. Principal payments on these bonds began in 2006. In August 2006 the District issued Production System bonds for \$27.5 million. The bonds mature serially over a 30-year period and have interest rates varying from 3.00% to 5.00%. These bonds are to finance continuing expenditures for project reconstruction and to provide for capital expenditures associated with FERC licensing. Scheduled principal maturities and interest requirements on the 2004 and 2006 Production Revenue Bonds are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 855,000	\$ 3,242,256	\$ 4,097,256
2011	885,000	3,212,331	4,097,331
2012	920,000	3,181,356	4,101,356
2013	955,000	3,146,856	4,101,856
2014	1,000,000	3,099,106	4,099,106
2015 - 2019	5,750,000	14,748,532	20,498,532
2020 - 2024	7,340,000	13,159,531	20,499,531
2025 - 2029	16,955,000	10,673,780	27,628,780
2030 - 2034	25,500,000	5,377,351	30,877,351
2035 - 2036	<u>6,380,000</u>	<u>458,213</u>	<u>6,838,213</u>
Total	<u>\$ 66,540,000</u>	<u>\$ 60,299,312</u>	<u>\$ 126,839,312</u>

Interfund Advances

In prior years the District's Electric Distribution System loaned funds to the Water Distribution System for plant improvements. Principal and interest payments on these loans are due monthly and have interest rates of 4.50%. Scheduled principal maturities and interest requirements on these loans are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 69,328	\$ 42,272	\$ 111,600
2011	72,513	39,087	111,600
2012	75,738	35,862	111,600
2013	79,323	32,277	111,600
2014	82,967	28,633	111,600
2015 - 2019	326,456	90,494	416,950
2020 - 2024	245,529	33,471	279,000
2025	<u>19,291</u>	<u>187</u>	<u>19,478</u>
Total	<u>\$ 971,145</u>	<u>\$ 302,283</u>	<u>\$ 1,273,428</u>

In 2007 the District's Board of Commissioners approved a loan from the District's Production System to the District's Electric Distribution System for \$16 million. Proceeds from this loan were used to pay \$85,572,237 under the White Creek Wind Project Energy Purchase Agreement. The interest rate is 4.50% and the obligation is to be repaid over a period not to exceed twenty years. The actual amount borrowed was \$15,217,740 and the balance at December 31, 2009 is \$14,235,019. Scheduled principal maturities and interest requirements on this loan follow:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 525,473	\$ 629,827	\$ 1,155,300
2011	549,614	605,686	1,155,300
2012	574,863	580,437	1,155,300
2013	601,272	554,027	1,155,299
2014	628,894	526,405	1,155,299
2015 - 2019	3,605,316	2,171,180	5,776,496
2020 - 2024	4,513,120	1,263,376	5,776,496
2025 - 2028	<u>3,236,467</u>	<u>229,431</u>	<u>3,465,898</u>
Total	<u>\$ 14,235,019</u>	<u>\$ 6,560,369</u>	<u>\$ 20,795,388</u>

Long-term debt activity for the year ending December 31, 2009 follows:

	Date of Original <u>Issue</u>	Date of Maturity	Outstanding Debt as of <u>Jan. 1, 2009</u>	Amount Issued	Amount Redeemed	Outstanding Debt as of <u>Dec. 31, 2009</u>
<u>Electric System</u>						
Electric Revenue Bonds, 4.375% to 5.00%	Nov-07	Sep-27	\$ 64,755,000	\$ -	\$ -	\$ 64,755,000
Electric Revenue Bonds, 4.50% to 5.00%	Aug-06	Sep-26	61,465,000	-	-	61,465,000
Electric Revenue Bonds, 5.00% to 5.25%	May-01	Sep-11	11,480,000	-	3,635,000	7,845,000
Loan Payable - State of Washington, 1.60%	Jun-07	Jun-28	800,000	-	-	800,000
Loan Payable - Production System, 4.50%	Dec-07	Dec-27	<u>14,737,413</u>	<u>-</u>	<u>502,394</u>	<u>14,235,019</u>
Total Electric System Long-Term Debt			<u>\$ 153,237,413</u>	<u>\$ -</u>	<u>\$ 4,137,394</u>	<u>\$ 149,100,019</u>
<u>Water System</u>						
Loan From Electric Dist- bution Fund, 4.5%	Apr-81	May-17	\$ 392,470	\$ -	\$ 38,941	\$ 353,529
Loan From Electric Dist- bution Fund, 4.5%	Jan-99	May-25	644,958	-	27,342	617,616
Loan Payable - State of Washington, 0.5% to 1.00%	May-88	Jun-23	635,773		51,490	584,283
Note Payable - Electric Dist- bution fund, 5.0%	Jan-08	Dec-12	<u>122,055</u>	<u>5,812</u>	<u>-</u>	<u>127,867</u>
Total Water System Long-Term Debt			<u>\$ 1,795,256</u>	<u>\$ 5,812</u>	<u>\$ 117,773</u>	<u>\$ 1,683,295</u>
<u>Production System</u>						
Production System Revenue Bonds, 3.00% to 5.00%	Aug-06	Aug-36	\$ 27,540,000	\$ -	\$ -	\$ 27,540,000
Production System Revenue Bonds, 3.00% to 5.00%	Sep-04	Sep-34	<u>39,830,000</u>	<u>-</u>	<u>830,000</u>	<u>39,000,000</u>
Total Production System Long-Term Debt			<u>\$ 67,370,000</u>	<u>\$ -</u>	<u>\$ 830,000</u>	<u>\$ 66,540,000</u>

8. OTHER LIABILITIES AND DEFERRED CREDITS

Other liabilities and deferred credits at December 31, 2009 consist of the following:

	<u>Electric System</u>	<u>Production System</u>
Lewis River Cost-Share Agreement	\$ -	\$ 14,191,038
Deferred revenue - rate stabilization fund	7,700,000	-
Personal leave and retirement reserves	1,090,714	-
Insurance reserves and other deferred credits	1,349,005	-
Post-retirement benefit obligation	<u>4,705</u>	<u>-</u>
Totals	<u>\$ 10,144,424</u>	<u>\$ 14,191,038</u>

Lewis River Cost-Share Agreement

The District reached a cost-sharing agreement with PacifiCorp, assigning the operational and capital expenditure payments to be made by the District for fish passage and other aquatic measures which are required under the Lewis River Settlement Agreement and under the FERC License for Swift No. 2. Operational payments are made annually for each year of the 50 year license and range from \$197,000 to \$291,000 (2003 dollars) indexed for inflation. During 2009 the District paid \$231,434 on this obligation. Also during 2009 the District paid \$3,230,681 on the capital portion of this obligation. The Agreement requires these capital payments be made according to the following schedule which has been indexed for inflation using 2003 dollars.

2010	\$ 3,378,818
2011	3,378,818
2015	225,255
2020	2,252,546
2021	2,252,546
2022	2,252,546
2035	<u>450,509</u>
Total	<u>\$ 14,191,038</u>

Deferred Revenue – Rate Stabilization Fund

For 2008, the District’s Board of Commissioners deferred revenues of \$7,700,000 representing White Creek Project net margins (\$5.3 million) and a portion of BPA Residential Exchange Program settlement proceeds (\$2.4 million). The transaction was recorded following FAS Statement 71 and future withdrawals from the fund will be considered revenue or a power cost reduction in the year the funds are withdrawn.

Personal Leave and Retirement Reserves

Pursuant to Governmental Accounting Standards Board Statement No. 16, the District uses the accrual basis of accounting for recognizing earned employee personal leave and floating holidays. Personal leave is limited to sixty days at the end of any calendar year. Personal leave accruals may be transferred, according to the District’s Banked Personal Leave Plan, into the Banked Personal Leave Fund. Employee amounts in the Banked Personal Leave Fund are no longer tied to the employee’s wage rate, but accrue interest according to the earnings of the Banked Personal Leave Fund investments. At December 31, 2009 the values of the accrued liabilities, which reflect a calculation for Social Security and Medicare taxes are \$703,573.

Effective August 1, 1984, the District established a Retirement Reserve Fund in response to the Washington State Legislature's SHB 843 which was signed into law on March 15, 1984. SHB 843 reduced the maximum days of accrued vacation applied to retirement payable by the State to 30 days, with the balance of the maximum accrued vacation and floating holidays applied to retirement payable by the employer under the average compensation formula for Plan 1 employees. The District has elected to fund the financial liability for Plan 1 employees for those days in excess of the 30 days funded by the State. When the District pays the lump sum due for days in excess of 30, the District has no future liability for that retiree's payments. As of December 31, 2009 the amount in the Retirement Reserve Fund was \$387,141.

Insurance Reserves and Other Deferred Credits

Electric System deferred credits totaled \$1,349,252 on December 31, 2009 and consist of insurance reserves, contract retentions, reserves for obsolete material losses and other miscellaneous deferred credits.

Post-Retirement Benefit Obligation

Plan Description

In addition to the pension benefits, the District provides post-retirement health care benefits, in accordance with the District's Collective Bargaining Agreement, to its retirees from the age of 55 until the age of 65. Currently, forty retirees meet those eligibility requirements. The District covers the medical insurance premium for those eligible retirees. The District does not pay for a Medicare supplement for any retiree eligible for Medicare.

Funding Policy

The District pays medical insurance premiums for employees that voluntarily retire under the Washington State Retirement System after employee reaches age 55, limited to premiums for coverage not in excess of coverage made available for active employees and limited to payments for the number of months not to exceed the number of months the employee has actually worked for the District; provided, however, such employee may pay their own premiums for the balance of time up to age 65 or when they become eligible for Medicare, whichever occurs first.

Annual OPEB Cost and Net OPEB Obligation

The District's annual post-retirement benefit obligation (PRBO) cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an on-going basis, is projected to cover normal costs each year and amortize any unfunded liabilities (or funding excess) over a 15-year period. The following table shows the components of the District's annual PRBO cost for the year ended December 31, 2009 the amount actually contributed to the plan and the changes in the District's net PRBO obligation:

Annual required contribution (ARC)	\$ 541,449
Interest on OPEB obligation	212
Adjustments to ARC	<u>(438)</u>
Annual OPEB cost	541,223
Benefit payments	<u>393,904</u>
Net increase in OPEB	147,319
Post-Retirement benefit obligation - January 1, 2009	<u>4,705</u>
Post-Retirement benefit obligation - December 31, 2009	<u><u>\$ 152,024</u></u>

Funding Status and Funding Progress

As of December 31, 2009, the unfunded actuarial accrued liability (UAAL) was \$3,870,091 million. The annual payroll of active employees covered by the plan was \$12,846,150 and the ratio of UAAL to covered payroll was 30%.

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

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. In the actuarial valuation conducted December 31, 2009, the projected unit credit actuarial cost method was used. Actuarial assumptions include a discount rate of 4.5%. The medical trend rate is estimated to gradually decrease from 11.0% in 2009 to 5.0% in 2021 and remain level thereafter.

9. RETIREMENT PLANS

Public Employees Retirement System – Plans 1, 2 and 3

Substantially all District 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 (DRS), under cost-sharing multiple employer public employee defined benefit and defined contribution retirement plans. The DRS, a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to: Department of Retirement Systems, Communications Unit, P.O. Box 48380, Olympia, WA 98504-8380. The following disclosures are made pursuant to GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers*.

Plan Descriptions

PERS is a cost-sharing multiple employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans, and Plan 3 is a combination defined benefit/defined contribution plan. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior Courts (other than judges in a judicial retirement system); employees of legislative committees; college and university employees (not in national higher education retirement programs); judges of district and municipal courts; and employees of local government. Participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977 and by either February 28, 2002 for state and higher education employees, or August 31, 2002 for local government employees, are Plan 2 members unless they exercise an option to transfer their membership to Plan 3. PERS participants joining the system on or after March 1, 2002 for state and higher education employees, or September 1, 2002 for local government employees have the option of choosing membership in either PERS Plan 2 or PERS Plan 3. The option must be exercised within 90 days of employment. An employee is reported to Plan 2 until a choice is made. Employees who fail to choose within 90 days default to Plan 3. PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PERS retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

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

Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 65 with 5 years of service, or at 55 with 20 years of service, with an allowance of two percent per year of service of the average final compensation. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Plan 2 retirements prior to age 65 receive reduced benefits. If retirement is at or after age 55 but before age 65 with at least 30 years of service, a three percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit; and a cost-of-living allowance is granted, (indexed to the Seattle Consumer Price Index), capped at three percent annually.

Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit portion provides a benefit calculated at one percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Effective June 7, 2006, Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service, if twelve months of that service are earned after age 44; or after five service credit years earned in PERS Plan 2 prior to June 1, 2003. Plan 3 members are immediately vested in the defined contribution portion of their plan. Vested Plan 3 members are eligible to retire with full benefits at age 65, or at age 55 with 10 years of service. Retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a three percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit, and Plan 3 provides the same cost-of-living allowance as Plan 2.

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

Funding Policy

Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at 6 percent for state agencies and local government unit employees, and at 7.5 percent for state government elected officials. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the Legislature. Under PERS Plan 3, employer contributions finance the defined benefit portion of the plan, and member contributions finance the defined contribution portion. The Employee Retirement Benefits Board sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee's age. The methods used to determine the contribution requirements are established under state statute in accordance with Chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of current year covered payroll, as of December 31, 2009 were:

	<u>Plan 1</u>	<u>Plan 2</u>	<u>Plan 3</u>
Employer *	5.31%	5.31%	5.31%
Employee	6.00%	3.90%	***

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

** Plan 3 defined benefit portion only.

*** Variable from 5.0% minimum to 15.0% maximum based on rate selected by the PERS 3 member.

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

	<u>Plan 1</u>	<u>Plan 2</u>	<u>Plan 3</u>
2009	\$ 61,137	\$ 757,455	\$ 43,742
2008	\$ 63,174	\$ 697,094	\$ 52,069
2007	\$ 60,065	\$ 484,778	\$ 33,933

Deferred Compensation – 401(k) and 457(k) Plans

The District offers its employees a 401(k) Deferred Compensation Plan created in accordance with Internal Revenue Code Section 401(k) which permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. Assets of the plan in 2009 were deposited, as specified by each participating employee, with Fidelity Investments as trustee. Effective January 1, 2008, the District began matching employee contributions to the plan up to 3 percent of eligible employee compensation. During 2009, the District made matching contributions of \$301,424.

The District also offers its employees the State of Washington Department of Retirement System's Deferred Compensation Program. This Deferred Compensation Plan is in accordance with Internal Revenue Code Section 457, which permits employees to defer a portion of their salary until future years. Distributions from the plan can be made after separation from service or upon the death of the participant. Participants can elect to receive an in-service distribution once every two years for an amount not to exceed \$5,000.

10. COMMITMENT AND CONTINGENCIES

Bonneville Power Administration Power Supply

On October 1, 2001 the District began to take deliveries from BPA under a new long-term Power Sales Contract (2001 Contract) with BPA. This 2001 Contract is for a ten-year term and is take-or-pay in nature. That is, BPA is obligated to serve and the District is obligated to purchase the quantity of power required for service to the District's load over and above what is provided by the District's own Swift resource and the firm power contracts itemized below.

During 2008 the District entered into agreements with Bonneville for Block and Slice running from October 1, 2011 through September 30, 2028. The Block Product provides a set amount of energy delivered in a flat block over all hours of the month, with the blocks of energy varying from month-to-month to correspond to seasonal variations in the District's loads. The Slice Product represents a specified percentage (or "slice") of the output of the Federal System, so that the District receives increased or decreased energy supply depending on the output of the Federal System. The District is required to pay a corresponding percentage of the costs of the portion of the Federal System allocated to the Slice product. The amounts payable by the District under the 2011 Power Sales Agreement are subject to adjustment from time to time by Bonneville to recover the costs of the Federal System.

Swift Plant No. 2 Power Contract

The Swift No. 2 Hydroelectric Production System is located on the Lewis River and consists of a 3.2 mile long power canal with an adjacent power house and transmission switchyard. It operates in

conjunction with the Swift No. 1 Project, which is owned by PacifiCorp. Swift No. 1 consists of an earthen dam and power house, which discharges into the Swift No. 2 power canal.

Swift No. 2 is operated under contract by PacifiCorp. The operating agreement provides that the District is entitled to 26% of the combined output of Swift No. 1 and Swift No. 2. The District's share of the output is purchased by the Electric System at the cost of production of the energy, whether or not it is producing energy.

Purchases from Grant County PUD

Pursuant to contracts with Grant County PUD, the District has rights to purchase predetermined percentage amounts of output from the Priest Rapids and Wanapum Developments. The District also must pay costs and debt service on the Priest Rapids and Wanapum Developments based on a predetermined percentage. The original contract with the Priest Rapids Development terminated October 31, 2005 and the current contract with the Wanapum Development terminated October 31, 2009. Both of these contracts have been extended through September 30, 2011 at 76% of their original output share.

Purchases from Energy Northwest's Nine Canyon Wind Project

The District entered into a contract with Energy Northwest in December 2003 for the purchase of the output associated with 2 megawatts of the Nine Canyon Wind Project. The District utilizes the power to serve its customers by use of a BPA wind integration product. The "green tags" or "renewable energy credits" associated with the District's share of output are committed for sale to the Bonneville Environmental Foundation and are not used for District load at this time.

White Creek Wind Project

White Creek Wind Project Energy Purchase Agreements

The District has entered into a partnership with Public Utility District No. 1 of Klickitat County, Washington (KPUD) and two Washington Electric Co-ops to participate in the White Creek Wind Project. In December 2006 the District entered into an Energy Purchase Agreement with White Creek Wind I, LLC, for 46% of the energy generated by the Project. The White Creek Project has a total of 89 2.3MW wind turbines for an expected output of 204.7MW.

In November 2007 the White Creek Wind Project began energy production and the District paid \$85,572,237 million under the Amended and Restated White Creek Wind Project Energy Purchase Agreement with White Creek Wind I, LLC (Seller) in which the District agrees to purchase and the Seller is obligated to deliver, 46% of the energy produced by White Creek Wind Project for twenty years. With certain exceptions, under the terms of the Agreement, should the Seller deliver less than the Annual Energy Quantity (225,917 MWh) the Seller shall have the obligation to deliver to the District a quantity of energy equal to the Annual Energy Quantity shortfall on or before the third anniversary of the last day of the contract year the Annual Energy Quantity shortfall accrued.

White Creek Wind Project Transmission Service Agreement

In 2006 the District entered into a Transmission Service Agreement with KPUD for power transmission from the White Creek Project Substation to the Rock Creek Substation where the transmission line and the facilities of BPA are connected. The District is billed and pays for services under this agreement monthly. In accordance with the Agreement, in 2007 the District provided KPUD an irrevocable standby Letter of Credit, which currently stands at \$3,615,342, for the District's performance of its obligation under the Agreement. The Agreement allows for a reduction in the amount of the Letter of Credit in accordance with a calculation contained in the Agreement. For the contract year commencing August 1, 2010 and for the contract years thereafter, the District may petition KPUD to waive the requirement for a Letter of Credit or an alternate Letter of Credit if the District's debt service coverage ratio is greater than 1.5.

White Creek Wind Project Energy Storage and Shaping Capacity Agreement

In 2007 the District entered into a White Creek Wind Energy Storage and Shaping Capacity Agreement with BPA for its share of White Creek Project generation. The Agreement is through September 30, 2016. The District is billed and pays for services under this agreement monthly.

White Creek Wind Project Scheduling and Marketing Services Agreement

In 2007 the District entered into an agreement with The Energy Authority, Inc., for the scheduling and marketing of the District's share of energy generated from the White Creek Wind Project. Fees for these services are billed and paid monthly.

Harvest Wind Project

As discussed in Note 4, the District is a party to a Joint Ownership Agreement whereby the District made an equity investment in the Harvest Wind Project, a 98.9 MW wind generating facility located in Klickitat County, WA. The District's share of the Project is 30%, with the balance owned by three other utilities. Each owner shares in power output, income and expenses according to their ownership shares. The District is committed, through an energy purchase agreement, to purchase its share of the output from the Project and pay its share of project expenses through the year 2029. Additionally, the District is committed, through a transmission service agreement and a transmission payment agreement to subsidize the initial construction of transmission lines, deposit funds to ensure contract performance, and purchase transmission from the owner of the transmission lines through the year 2029.

Beacon Hill Sewer District Inter-local Agreement

Effective January 1, 2008, the District entered into an Interlocal Agreement with the Beacon Hill Sewer District (BHSD), a Washington municipal corporation pursuant to The Cooperation Act of the Revised Code of Washington Chapter 39.34. The Agreement provides a mechanism for an orderly transfer of the operation and maintenance of the District's Water System (System) by BHSD under joint oversight by the Boards of Commissioners of both the District and BHSD, for a three year transition period with the intention of the parties, should the parties elect to complete the transfer, whereby the District will convey full ownership of the System to BHSD on or before December 31, 2012. Should ownership be transferred to BHSD it is anticipated it will be in exchange for BHSD's pledge to continue to operate the System for the benefit of current and future customers and to accept both the assets and the liabilities of the System as they exist at the time of the transfer. Should the Agreement be terminated without the parties having reached agreement for final conveyance of the assets and liabilities of the System to BHSD, the District will resume full responsibility for operations and maintenance of the System.

Claims and Litigation

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

11. SUBSEQUENT EVENTS:

Electric Distribution System Revenue Bond Issue

On February 23, 2010 the District issued Electric System Revenue Bonds consisting of \$17,805 million in tax-exempt bonds (2010A) and \$46,180 million in taxable "Build America Bonds" (2010B) to fund capital improvements, pay for bond issuance costs and fund bond debt service and reserve accounts. Principal payments on these bonds are scheduled to begin in September 2013, maturing annually in varying amounts though Sept 2032. The 2010A bonds are not subject to redemption prior to maturity and carry a coupon rate of 5.00% with an all-in true interest cost of 3.59%. The 2010B bonds are subject to redemption by the District prior to their stated maturities and carry coupon rates of 2.52 – 6.884% before a thirty-five percent subsidy payment from the United States Treasury, subject to certain conditions. The all-in true interest cost for the 2010A and 2010B bonds is 4.26%.

Water System Loan

In 2009 the District entered into an Interlocal Agreement with the City of Longview, Washington for supplemental financing of a new regional water treatment facility in which the District obtain a Public Works Trust Fund loan from the Washington State Department of Community, Trade and Economic Development in an amount not to exceed \$1 million. No loan funds were received in 2009; however, in January 2010, the District received \$750,000 of loan funds at an interest rate of .5% per annum payable over a period not to exceed 20 years with the final payment due July 1, 2028. The loan funds were turned over to the BHSD in accordance with District's Interlocal Agreement with BHSD and BHSD turned these funds over to the City of Longview in accordance with the Interlocal Agreement with the City.

The Energy Authority Membership

On March 30, 2010 the District became a member of The Energy Authority (TEA), a nonprofit corporation that provides power energy trading, RTO market services, natural gas procurement and management services, risk management and hedging services, and power management services to 45 public utilities across the nation.

The Membership Agreement required: (a) payment of a \$1 million Membership Fee; (b) payment of a \$2.8 million Capital Contribution, representing the District's ownership interest in TEA; and (c) the Advance Agreement of \$9,642,857, consisting of a \$1 million Bank Guarantee, and a Trade Guarantee of \$8,642,857. The Bank Guarantee makes certain credit representations and guarantees to Bank of America, which will then be able to issue a letter of credit to any counter-party requiring a letter of credit as a condition of any particular transaction. Like the Bank Guarantee, the Trade Guarantee makes certain credit assurances up to \$8,642,857.00 allowing TEA this amount of unsecured credit to trade on behalf of its members.

Should the District separate from TEA within two years, it will receive the \$1 million membership fee in return, less TEA's transactional costs attendant with District becoming a member. Under TEA Bylaws, at any time upon separation the District will receive all of its then existing interest in the corporation, which would include its Capital Contribution.

Short-term Revenue Note with Bank of America - Payoff

On March 31, 2010 the District repaid \$12 million of the \$30 million Short-term Revenue Note Purchase Agreement with Bank of America. On April 8, 2010 the District received a preferred distribution of \$18 million from the Harvest Wind Project and on that day paid the remaining \$18 million Revenue Note obligation.