



Office of the Washington State Auditor
Pat McCarthy

Financial Statements Audit Report
Public Utility District No 1 of Thurston
County

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

Published November 30, 2017

Report No. 1020330





Office of the Washington State Auditor
Pat McCarthy

November 30, 2017

Board of Commissioners
Public Utility District No 1 of Thurston County
Olympia, Washington

Report on Financial Statements

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

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

Sincerely,

Pat McCarthy
State Auditor
Olympia, WA

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

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

Board of Commissioners
Public Utility District No 1 of Thurston County
Olympia, Washington

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Public Utility District No 1 of Thurston County, Washington, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated November 29, 2017.

INTERNAL CONTROL OVER FINANCIAL REPORTING

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

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

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

COMPLIANCE AND OTHER MATTERS

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

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

PURPOSE OF THIS REPORT

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



Pat McCarthy

State Auditor

Olympia, WA

November 29, 2017

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

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

Board of Commissioners
Public Utility District No 1 of Thurston County
Olympia, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of Public Utility District No 1 of Thurston County, Washington, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed on page 9.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the District's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances,

but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

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

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and required supplementary information listed on page 9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated November 29, 2017 on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts

and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Pat McCarthy". The signature is written in a cursive style with a large, stylized initial "P".

Pat McCarthy
State Auditor
Olympia, WA

November 29, 2017

FINANCIAL SECTION

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

REQUIRED SUPPLEMENTARY INFORMATION

Management's Discussion and Analysis – 2016

BASIC FINANCIAL STATEMENTS

Statement of Net Position – 2016

Statement of Revenues, Expenses and Changes in Net Position – 2016

Statement of Cash Flows – 2016

Statement of Fiduciary Net Position – Agency Funds – 2016

Notes to Financial Statements – 2016

REQUIRED SUPPLEMENTARY INFORMATION

Schedule of Proportionate Share of Net Pension Liability – PERS 1, PERS 2/3 – 2016

Schedule of Employer Contributions – PERS 1, PERS 2/3 – 2016

Public Utility District No. 1 of Thurston County

Management's Discussion and Analysis

December 31, 2016 and 2015

The management of the Public Utility District No. 1 of Thurston County (District) offers readers of these financial statements this overview and summary analysis of the financial activities of the District for the year ended December 31, 2016 with additional comparative data for 2015. This analysis is intended to supplement and be used in conjunction with the basic financial statements and accompanying notes, which follow this section, and to assist the reader in focusing on significant financial activities.

Overview of the Financial Statements

The District uses fund accounting to account for its financial activities in accordance with the standards of the Governmental Accounting Standards Board (GASB). The District is considered an Enterprise Fund and the fund type used to account for its financial activities is called a Proprietary Fund. The District provides retail water service and regional water resource activities to support its water systems.

In accordance with requirements set forth by GASB, the District's financial statements are developed using the accrual method of accounting to recognize changes in District resources. Accrual accounting recognizes revenues and expenses when earned or incurred without regard for when cash is actually received or disbursed. The financial statements presented in the following pages of this document are presented just for the year ended December 31, 2016, and are comprised of:

• **Statement of Net Position:** The Statement of Net Position reflects the assets, deferred inflows, deferred outflows, liabilities and net position of the District as of the end of the fiscal year which, for the purposes of this report, is December 31, 2016. The net position section is separated into three categories:

- net investment in capital assets
- restricted net position
- unrestricted net position

• **Statement of Revenues, Expenses, and Changes in Net Position:** This statement reflects the transactions and events that have increased or decreased the District's total resources during the period. Revenues and expenses are classified as operating or non-operating based on the nature of the transaction. The net position increases when revenues exceed expenses.

• **Statement of Cash Flow:** The statement of cash flow provides information on the sources and uses of cash separated into four categories of activities: operating, non-capital, capital and related financing, and investing.

• **Notes to the Financial Statements:** The notes to the financial statements, presented at the end of the basic financial statements, are considered an integral part of the District's presentation of financial position, results of operations, and changes in cash flows and

should be considered as part of the whole presentation. These notes are necessary to develop a full understanding of the figures provided in the basic financial statements.

The following table provides a summary of the financial data discussed in the next few pages of this report:

Public Utility District No. 1 of Thurston County, Washington
Condensed Financial Information for December 31, 2016, and 2015

STATEMENT OF NET POSITION	Combined Total As of December 31		Increase (Decrease) 2016 - 2015	% Change 2016 - 2015
	2016	2015		
Current Assets	\$ 2,095,509	\$ 1,668,321	\$ 427,188	25.61%
Other Non-Current Assets	9,627,431	8,817,665	809,765	9.18%
Total Assets	<u>\$ 11,722,940</u>	<u>\$ 10,485,987</u>	<u>\$ 1,236,953</u>	11.80%
DEFERRED OUTFLOWS of RESOURCES	\$ 177,205	\$ 94,234	\$ 82,971	88.05%
Current Liabilities	\$ 868,134	\$ 731,072	\$ 137,062	18.75%
Noncurrent Liabilities	6,025,958	5,683,404	342,554	6.03%
Total Liabilities	<u>\$ 6,894,092</u>	<u>\$ 6,414,476</u>	<u>\$ 479,615</u>	7.48%
DEFERRED INFLOWS of RESOURCES	15,989	382,682	(366,693)	-95.82%
Net Investment in Capital Assets	\$ 3,518,538	\$ 2,890,435	\$ 628,103	21.73%
Restricted Net Position	806,545	680,650	125,895	18.50%
Unrestricted Net Position	664,981	211,977	453,004	213.70%
Total Net Position	<u>\$ 4,990,064</u>	<u>\$ 3,783,062</u>	<u>\$ 1,207,002</u>	31.91%

Public Utility District No. 1 of Thurston County, Washington
Condensed Financial Information for December 31, 2016, and 2015

STATEMENT OF CHANGES IN NET POSITION	Combined Total As of December 31		Increase (Decrease) 2016 - 2015	% Change 2016 - 2015
	2016	2015		
Operating Revenues	\$ 2,915,579	\$ 2,779,490	\$ 136,089	4.90%
Non-Operating Revenues	486,479	418,456	68,023	16.26%
Total Revenues	<u>\$ 3,402,058</u>	<u>\$ 3,197,946</u>	<u>\$ 204,112</u>	6.38%
Operating Expenses	\$ 2,797,763	\$ 2,470,630	\$ 327,133	13.24%
Non-Operating Expenses	134,469	149,706	(15,237)	-10.18%
Total Expenses	<u>\$ 2,932,231</u>	<u>\$ 2,620,338</u>	<u>\$ 311,893</u>	11.90%
Capital Contributions	737,174	180,653	556,521	308.06%
Change in Net Position	<u>\$ 1,207,001</u>	<u>\$ 758,261</u>	<u>\$ 448,740</u>	59.18%
Net Position Balance, BOY	\$ 3,783,064	\$ 3,722,359	\$ 60,705	1.63%
Current Year Change in Net Position	1,207,000	758,263	448,737	59.18%
Prior Period Adjustment	-	(697,560)	697,560	
Balance, EOY	<u>\$ 4,990,064</u>	<u>\$ 3,783,062</u>	<u>\$ 1,207,002</u>	31.91%

Financial Analysis

Operating Revenues

In 2016, operating revenue for the District increased \$136,089 or 4.90% from that of 2015. This increase in revenue is primarily attributable to a 2016 increase in the capital surcharge implemented in 2015 to fund capital improvements. The District also implemented a 4% increase on all water rates, however the impact on water revenue was much less due to a reduction in customer consumption in 2016 when compared to 2015.

Operating Expenses

Overall operating expenses increased in 2016 \$327,133 or 13.24%. The largest contributor to this increase in expense was Salaries & Benefits Employee increasing \$284,148 or 26.74%, due to extra staffing to assist during extended employee leave as well as an increase in field positions that were filled for almost an entire year. Another element of this increase was a large increase in claims experienced by our Health Plan in 2016. System Repairs & Maintenance increased \$18,221 or 17.86% over 2015, due primarily to maintenance on the additional systems purchased in 2015 and 2016.

Non-Operating Revenues & Expenses

Non-operating revenue recognized in 2016 increased \$624,544 or 104.25% over 2015. The District received \$192,209 in grant revenues and \$737,174 in capital contributions in 2016, which was an increase of 189.88% over that received in 2015. The rest of the non-operating revenue recognized in 2016 is primarily the District's tax levy. The District, like all public utility districts organized in the State of Washington, has taxing authority. The District exercises this authority at a minimum level, collecting \$277,161 in property tax assessments in 2016, compared to \$268,195 in 2015, representing a 3.34% increase from 2015 to 2016. Property tax revenues are used by the District to support general District operations which can be tied to a benefit to taxpayers, rather than ratepayers of the District.

Election of PUD Commissioners is held each even year; the cost of the election is paid out of the property tax revenues, and is reported as a non-operating expense. The District's share of the 2016 election was \$58,082. The District requested and received an extension to pay this expense over two years, and therefore incurred election costs in 2016 of \$29,041 and deferred the remainder of the 2016 costs, \$29,041 to 2017.

Interest income and interest expense are included as non-operating revenue and expense. Interest income increased from \$15,292 in 2015 to \$17,109 due to an increase in investment earnings. Interest expense decreased to \$105,428 in 2016 from \$109,894 in 2015 due to the reduced interest costs payments resulting from paying down the debt obligations of the District.

Net position

The District's total net position increased in 2016 by \$1,207,001 or 31.91%.

Capital Assets

The District's net capital additions (after depreciation) including capital work in progress, were \$799,042 in 2016 and \$588,090 in 2015. These additions consisted of the acquisition of 4 small water systems, the installation of a backup generator on the District's largest system, the consolidation of a group A water system with 2 group B water systems, the complete rebuild of the distribution system for a small group A water system. Many smaller projects were completed during the year as the District implemented its asset management plan. See Note 4 of the accompanying notes to the financial statements for further detail related to capital asset activity.

Long-term Debt Activity

At year-end 2016 the District's long-term debt changed to \$5.60 million from \$5.4 million reported in 2015. Newly issued debt was used to acquire water systems, and fund capital projects completed in 2016. Funds for payment of long-term debt are provided for from the cash flow from water revenues. See Notes 8 and 9 of the accompanying notes to the financial statements for further detail related to long-term debt activity.

Debt Service Coverage

The debt service coverage ratio measures cash flow from operations in comparison to annual debt service for the District's parity bonds. The covenants governing the District's 2011 bond issue require the District to maintain a debt service coverage ratio of 1.25 or above. In 2016, the District's debt service coverage ratio is 2.99, compared to 3.43 in 2015.

Contacting the District's Financial Management

The financial report is designed to provide interested parties with a general overview of the District's finances and to demonstrate District accountability for the money it receives. If you have questions about this report, or require additional or clarifying financial information, contact the Public Utility District No. 1 of Thurston County, 921 Lakeridge Way SW, Suite 301, Olympia, WA 98502.

Julie Parker
Director of Finance and Administration

Public Utility District No. 1 of Thurston County, Washington

STATEMENT OF NET POSITION

December 31, 2016

ASSETS	<u>2016</u>
Current Assets	
General Reserve	296,237
Capital Improvement Reserve	297,135
Water Revenue Reserve	1,132,716
Customer Deposits	68,185
Customer Accounts Receivable (net)	245,278
Property Tax Receivable	6,582
Other Receivables	18,753
Prepaid Expenses	<u>30,623</u>
Total Current Assets	<u>\$ 2,095,509</u>
Non-Current Assets	
Restricted - Bond Reserve	509,410
Capital Assets Not Being Depreciated:	
Land and Land Rights	153,532
Construction in Progress	130,731
Capital Assets Being Depreciated:	
Water Plant	11,448,821
Office Furniture & Equipment	223,643
Vehicles & Equipment	294,965
Other Utility Plant	704,785
Less: Accumulated Depreciation	<u>(3,838,456)</u>
Total Capital Assets (Net)	9,118,021
Total Non-Current Assets	<u>\$ 9,627,431</u>
Total Assets	<u>\$ 11,722,940</u>
 DEFERRED OUTFLOWS of RESOURCES	
<u>Deferred Outflows Related to Pensions</u>	<u>\$ 177,205</u>

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

Public Utility District No. 1 of Thurston County, Washington

STATEMENT OF NET POSITION

December 31, 2016

LIABILITIES AND EQUITY**Current Liabilities:**

Accounts payable	208,566
Current Accrued Compensated Absences	71,084
Accrued Payroll Liabilities	48,187
Refundable Deposits	71,582
Current Portion of Bonds, Notes and Loans Payable	468,715

Total Current Liabilities	<u>\$ 868,134</u>
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Noncurrent Liabilities:

Bonds Payable	1,705,000
Bond Anticipation Note	863,000
PWTF Note - Preconstruction 05	368,421
DWSRF Loan - Tanglewilde Source	587,899
DWSRF Loan - Tanglewilde Reservoir	1,129,893
DWSRF Loan - Sward/Platt Consolidation	30,324
DWSRF Loan - Consolidate Lew's 81st	158,485
DWSRF Loan - Hawk Acres Main	59,193
DWSRF Loan - Hawk Acres Source	56,190
DWSRF Loan - Horsfall Improvements	90,674
DWSRF Loan - Ridgewood Improvements	54,270
DWSRF Loan - Webster Hill Improvements	27,418
Long Term Compensated Absences	7,671
Net Pension Liability	887,520

Total Noncurrent Liabilities	<u>\$ 6,025,958</u>
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Total Liabilities	<u>\$ 6,894,092</u>
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DEFERRED INFLOWS of RESOURCES

Deferred Inflows Related to Pensions	15,989
Total Deferred Inflows of Resources	<u>\$ 15,989</u>

NET POSITION

Net Investment in Capital Assets	3,518,538
Restricted for Capital Projects	297,135
Restricted for Debt Service	509,410
Restricted Net Position	<u>\$ 806,545</u>
Unrestricted Net Position	<u>664,981</u>
Total Net Position	<u>\$ 4,990,064</u>

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

Public Utility District No. 1 of Thurston County, Washington
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
 For the Year Ended December 31, 2016

	2016
Operating Revenues	
Metered & Unmetered Water Revenue	2,415,080
Sales to Irrigation	92,183
Miscellaneous Service Revenue	57,000
Other Water Revenue	351,316
Total Operating Revenue	\$ 2,915,579
Operating Expenses	
Salaries & Benefits Employees	\$ 1,346,637
Salaries Commissioners	76,646
Purchased Water	22,541
Purchased Power	112,124
Chemicals	37,517
System Repairs & Maintenance	120,253
Contract Engineering	17,200
Contract Legal	31,025
Contract Testing	53,498
Contract State Auditor	12,726
Contract Other	4,200
Rent and Janitorial	52,200
Transportation	43,289
Insurance	27,810
Advertising	3,960
Office Expense	58,223
Meeting Costs Commissioners	6,810
Meeting Costs Staff	5,354
Dues & Subscriptions	15,641
Telephone	10,469
Staff Training	3,096
Postage	23,325
Printing	13,153
Miscellaneous	58,873
Taxes	149,564
Depreciation/Amortization	491,629
Total Operating Expenses	\$ 2,797,763
Net Operating Income	\$ 117,816
Non-Operating Revenues (Expenses)	
Interest Income	\$ 17,109
Property Tax Revenue	\$ 277,161
Interest on Long Term Debt	\$ (105,428)
Election costs	\$ (29,041)
Grant Revenues	\$ 192,209
Total Non-Operating Revenues (Expenses)	\$ 352,010
Capital Contributions	\$ 737,174
Change in Net Position	\$ 1,207,000
Net Position	
Total Net Position, January 1	\$ 3,783,064
Total Net Position, December 31	\$ 4,990,064

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

Public Utility District No. 1 of Thurston County, Washington

STATEMENT OF CASH FLOWS

For the Year Ended December 31, 2016

	2016
Cash Flows from Operating Activities	
Cash received from customers	\$ 2,845,546
Cash payments to supplies and employees	\$ (2,023,821)
Taxes paid	\$ (149,564)
Net Cash Provided by Operating Activities	<u>\$ 672,161</u>
Cash Flows from Non-Capital Financing Activities	
Property Tax Income	\$ 277,418
Other Non Operating Income	\$ -
Election Expenses	\$ (29,041)
Net Cash Provided by Non-Capital Financing Activities	\$ 248,377
Cash Flows from Capital Financing Activities	
Payments to 2011 Revenue Bond	\$ (225,000)
Payments to Public Works Trust Fund Loan	\$ (52,632)
Payments to DWSRF Loans	\$ (176,146)
Net Proceeds from Issuance of Water Revenue Bond Anticipation Note	\$ 460,000
Proceeds from DWSRF Loans	\$ 164,717
Proceeds from Grants & Capital Contributions	\$ 652,360
Acquisition and construction of capital assets	\$ (1,290,672)
Interest paid on long term debt	\$ (105,428)
Net cash from Capital Financing Activities	\$ (572,801)
Cash Flows from Investing Activities	
Interest received on cash on deposit	\$ 17,108
Net Cash Provided by Investing Activities	\$ 17,108
Net Increase (Decrease) in Cash	\$ 364,845
Beginning of Year	<u>\$ 1,938,838</u>
End of Year	<u><u>\$ 2,303,683</u></u>

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

Public Utility District No. 1 of Thurston County, Washington

STATEMENT OF CASH FLOWS

For the Year Ended December 31, 2016

	2016
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities	
Operating Income (Loss)	\$ 117,816
Adjustments to reconcile operating Income to net cash provided (used) by operating activities:	
Depreciation Expense	\$ 491,629
Customer Accounts Receivable	\$ (68,114)
Other Accounts Receivable	\$ (5,771)
Prepaid Expenses	\$ 563
Accounts Payable	\$ 82,870
Refundable Deposit Payable	\$ 3,852
Payroll Liabilities	\$ 20,364
Accrued Compensated Absences	\$ (673)
Net Pension Deferred Inflow/Outflows	\$ 29,625
Total Adjustments	\$ 554,345
Net Cash Provided by Operating Activities	\$ 672,161
NonCash Investing, Capital and Financing Activities	
Capital Assets Acquired by Contribution	\$ 721,184
Total Noncash Activities	\$ 721,184

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

Public Utility District No. 1 of Thurston County, Washington
STATEMENT OF FIDUCIARY NET POSITION - AGENCY FUNDS
December 31, 2016

	<u>Agency Funds Total</u>	
Assets:		
Cash with County	\$	354,937
Liabilities:		
Custodial Accounts	\$	354,937

PUBLIC UTILITY DISTRICT NO. 1 OF THURSTON COUNTY
NOTES TO FINANCIAL STATEMENTS
January 1, 2016 through December 31, 2016

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

NOTE 1 – NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

Public Utility District No. 1 of Thurston County, Washington (Thurston PUD or the District) is a municipal corporation governed by an elected three-person Commission, authorized under Title 54 RCW. As required by generally accepted accounting principles, management has considered all potential component units in defining the reporting entity. Thurston PUD has no component units.

Nature of Activities

Thurston PUD owns and operates 161 water systems serving approximately 4082 active connections in 5 counties (Thurston, Lewis, Pierce, Grays Harbor and Mason Counties). Thurston PUD also manages 17 systems under contract as a Satellite Management Agency (SMA). The District employs 13 full time employees.

Basis of Accounting

The accounting policies of Thurston PUD conform to generally accepted accounting principles (GAAP) as applicable to proprietary funds of governments. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The accounting records of the District are maintained in accordance with methods prescribed by the Washington State Auditor under the authority of Chapter 43.09 RCW. The full accrual basis of accounting is used, where revenues are recognized when earned and expenses are recognized when incurred. Capital asset purchases are capitalized and long-term liabilities are accounted for in the appropriate funds. The Uniform System of Accounts for Class A Water Utilities, 1996, published by the National Association of Regulatory Utility Commissioners, is the foundation for the accounting policies of the District, and includes instructions regarding the capitalization of capital assets and the methods of accounting for and reporting contributions in aid of construction.

Proprietary Fund Financial Statements

The District's financial statements include the financial position and results of operations of its two reporting units, general and water operations, which have been combined for this report. In accordance with governmental accounting principles, all Thurston PUD funds are considered proprietary.

Fiduciary Fund Financial Statements

The District uses agency funds to report assets that are held in a custodial relationship. Agency funds are not used to support the District's own programs so these funds are excluded from the government-wide financial statements. Agency funds do not have a measurement focus and report only assets and liabilities. The District's seven agency funds represent amounts held on behalf of various homeowner's associations.

PUBLIC UTILITY DISTRICT NO. 1 OF THURSTON COUNTY
NOTES TO FINANCIAL STATEMENTS
January 1, 2016 through December 31, 2016

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

New Accounting Standards

With this report, the District has implemented GASB Statement 77, Tax Abatement Disclosures; and GASB Statement 72, Fair Value Measurement and Application.

Operating and NonOperating Revenue and Expenses

The District distinguishes between operating revenues and expenses from those that are nonoperating. Operating revenues and expenses result from providing services and producing and delivering goods in connection with the district's principal ongoing operations. The principal operating revenues of the District are charges to customers relating to the provision of retail water utility services, as well as special charges relating to the administration of customer accounts. Operating expenses for the District include the cost of providing water utility services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues & expenses.

Gains and losses from the disposal of utility plant and other non-core activities are excluded from operating income.

Accounting Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. Estimates may be included in the disclosure of contingent assets and liabilities at the date of the financial statements, and in the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Revenue Recognition

Revenue is recognized as billed based on rates established by Thurston PUD's Board of Commissioners. Customer meters are read monthly during the second and third weeks of the month, and billed at month end. Unbilled utility service receivables are considered to be the revenue of the following month and are not accrued, which is a departure from GAAP.

Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, the District considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents. All investments are held in trust with the Thurston County Treasurer's Office who acts as the Treasurer of the District.

Utility Plant and Depreciation

See Note 4 – Capital Assets

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Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of all state sponsored pension plans and additions to/deductions from those plans' fiduciary net position have been determined on the same basis as they are reported by the Washington State Department of Retirement Systems. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Restricted Net Position

In accordance with bond resolutions and other agreements, separate reserve accounts have been established for restricted or limited-use resources. The assets held in these funds are limited as to their use, including debt service, dedicated capital project funds, and other reserve requirements. At year-end there are restricted funds of Thurston PUD in the amount of \$509,410 in the Bond Reserve.

Receivables

All utility customers are billed monthly in arrears for water service. Customer accounts receivable consist of amounts owed from private individuals or organizations for water services rendered. Management has reviewed customer accounts receivable at year-end to determine if any receivables will potentially be uncollectible, and to establish the provision for uncollectible customer accounts. For the current year, an estimate based on a percentage of water revenue billed during the year was used to establish this provision. Actual losses are then charged against the provision as they are identified. Management believes that the provision for uncollectible accounts as of year-end was adequate. The financial statements reflect customer accounts receivable net of the provision for uncollectible accounts.

Taxes receivable consists of property taxes and related interest and penalties (see Note 2 – Property Taxes).

Compensated Absences

Employees accrue vacation leave in accordance with years of service. The balance of vacation may be carried forward from year-to-year to a maximum accumulation of 240 hours. Upon termination or resignation any accrued vacation through the last date of employment is cashed-out at the current equivalent salary or hourly wage of the employee. Thurston PUD records the cost of vacation leave as earned with a liability representing leave balances earned but not taken.

Sick leave is accrued by employees on a monthly basis at the rate of one day of sick leave per month. There is no cap to the amount of sick leave that can be accumulated. Any accrued sick leave at the time of separation of service may be converted to cash at the rate of 25% of the value of the sick leave determined based on the employee's last rate of pay. Thurston PUD records the cost of sick leave as earned with a liability representing 25% of the value earned but not taken.

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Income Tax Status

Thurston PUD is a municipal corporation and is exempt from federal income taxes.

Statement of Cash Flows

For purposes of the Statement of Cash Flows, all highly liquid debt instruments purchased with a maturity of three months or less are considered to be cash equivalents.

Changes in Accounting

There are no changes to the accounting presentation in the 2016 financial statements.

NOTE 2 – PROPERTY TAXES

The Thurston County Treasurer (County Treasurer) acts as an agent to collect property taxes levied in the county for all taxing authorities.

Property Tax Calendar	
January 1	Taxes are levied and become an enforceable lien against properties.
February 14	Tax bills are mailed.
April 30	First of two equal installment payments are due.
May 31	Assessed value of property established for next year's levy at 100 percent of market value.
October 31	Second installment is due

Property taxes are recorded as receivable and revenue when levied. Property taxes collected in advance of the fiscal year to which they apply are recorded as deferred inflow and recognized as revenue of the period to which they apply. No allowance for uncollectible taxes is established because delinquent taxes are considered fully collectible. Prior year tax levies were recorded using the same principal, and delinquent taxes are evaluated annually. A revaluation of all property is required every four years.

The District's regular levy for 2016 was \$0.009616688132 per \$1,000 on an assessed valuation of \$27.898 billion for a total regular levy of \$268,287. In 2015 the regular levy was \$261,352. Washington State Constitution and Washington State law, RCW 84.55.010, limit the rate.

NOTE 3 – DEPOSITS AND INVESTMENTS

The District utilizes the services of the County Treasurer to invest and disburse all District cash.

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Deposits

All receipts received by the District are deposited into qualified bank depositories as directed by the County Treasurer and specified by the Washington Public Deposit Protection Commission (PDPC). All deposits, including money markets and certificates of deposits, are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington PDPC. The PDPC is a statutory authority established under Chapter 39.58 of the Revised Code of Washington. PDPC coverage is of the nature of insurance pursuant to the Governmental Accounting Standards Board Statement No. 3. All deposits held at December 31, 2016, and throughout the year, were classified as category 1, insured or collateralized with securities held by the County Treasurer or by their agent in the County Treasurer's name.

Investments

In 2016, Thurston PUD held no other investments than the deposits with the County Treasurer. Investments are governed by State statute and County investment policy. All investment instruments are those allowed by statute, which may include U.S. Treasury Notes, Federal Agencies, bankers' acceptances, short-term commercial paper, money market account and the State Treasurer's Local Government Investment Pool (LGIP). There is no statutory regulatory oversight of the LGIP other than annual audits through the Washington State Auditor's Office. The fair value of County shares in the LGIP is dollar for dollar equal to the value of pool shares. The Pool offers 100% liquidity, therefore, all of these short term investments are considered cash equivalents and not subject to risk categorization.

The investment policy of the County Treasurer dictates that all investment instruments be transacted on the delivery vs. payment basis. Wells Fargo acts as safekeeping agent for the Thurston County Treasurer.

Custodial credit risk – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Thurston County limits its credit risk through diversification of security types and issuers. Thurston County policy further limits risk to investments in securities that have one of the three highest ratings of a national rating agency at the time of investment.

FAIR MARKET VALUE. Fair value is the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. GASB 72 establishes a hierarchy of inputs to valuation techniques used to measure fair value. This hierarchy has three levels:

Level 1 - Pricing inputs are observable inputs such as quoted prices, available in active markets, for identical assets on the measurement date.

Level 2 - Pricing inputs are either directly or indirectly observable inputs available in active markets as of the measurement date.

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Level 3 - Pricing inputs are unobservable inputs used in cases where financial instruments are considered illiquid, with no significant market activity and little or no pricing information on the date of measurement.

All investment balances as of December 31, 2016 are based on level 1 inputs. At December 31, 2016 the District has the following investments measured at fair value:

Investments by Fair Value Level	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Deposits held with Thurston County Treasurer	\$2,303,683	\$0	\$0
Total Investments by Fair Value	\$2,303,683	\$0	\$0

NOTE 4 – CAPITAL ASSETS

Capital assets are defined by the District as assets with initial individual cost of more than \$500 and an estimated useful life in excess of three years. Major expenses for capital assets and major repairs, in excess of \$500, that increase useful lives are capitalized. Maintenance, repairs and minor renewals are accounted for as expenses when the cost is 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 the estimated cost to construct the plant, discounted to the year the plant was originally dedicated to public service. Contributions by developers and customers are recorded, at cost, as capital contributions. The District amortizes as depreciation those assets acquired by contributions.

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Utility plant activity for the year ended December 31, 2016 was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Utility plant not being depreciated:				
Land and Land Rights	113,532	40,000	-	153,532
Construction in Progress	753,103	812,530	(1,434,902)	130,731
Total utility plant not being depreciated	\$ 866,635	\$ 852,530	\$ (1,434,902)	\$ 284,263
Utility plant being depreciated				
Structures & Improvements	460,289	253,131		713,420
Wells and Springs	1,005,743	99,580		1,105,323
Supply Mains	390,180			390,180
Power Generation Equipment	6,443	242,846		249,289
Pumping Equipment	1,370,951	267,990		1,638,941
Water Treatment Equipment	1,057,692	52,422		1,110,114
Distribution Reservoir & Standpipe	1,883,262	184,767		2,068,029
Transmission & Distribution Mains	2,946,034	644,456		3,590,490
Services	226,511	50,864		277,375
Meters & Meter Installations	262,065	12,473		274,538
Hydrants	11,227			11,227
Other Plant & Miscellaneous Equipment	19,895			19,895
Office Furniture & Equipment	223,643			223,643
Transportation Equipment	192,767	31,934		224,701
Tools, Shop, & Garage Equipment	8,230	4,265		12,495
Communication Equipment	9,740	28,316		38,056
Miscellaneous Equipment	19,713			19,713
Other Tangible Plant	704,785			704,785
Total utility plant being depreciated	\$ 10,799,170	\$ 1,873,044	\$ -	\$ 12,672,214
Accumulated Depreciation	3,346,827	491,630		3,838,457
Total Utility Plant, Net	\$ 8,318,978	\$ 2,233,944	\$ (1,434,902)	\$ 9,118,020

Depreciation is computed using the straight line method over their estimated useful lives of 3 to 80 years. Initial depreciation on utility plant is recorded on a pro-rata basis in the year it is placed in service. When operating property is retired, or otherwise disposed of, the original cost is removed from the utility plant accounts and from accumulated depreciation.

NOTE 5 – CONSTRUCTION IN PROGRESS

The District has active construction projects as of December 31, 2016. The projects include: the consolidation of the Platt and Sward water systems into a group A water system, mainline replacement on the Crowder water system, and development of a prototype for emergency generators on small water systems.

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At year-end the District's commitments with contractors are as follows:

Project	Spent to Date	Remaining Commitment
Emergency Generator for Tanglewilde Thompson Place WS	\$ 36,676	\$ 12,895

NOTE 6 – PENSION PLANS

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

Aggregate Pension Amounts – All Plans	
Pension liabilities	\$887,521
Pension assets	\$0
Deferred outflows of resources	\$177,203
Deferred inflows of resources	(\$15,989)
Pension expense/expenditures	\$126,197

State Sponsored Pension Plans

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

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

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

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

Public Employees' Retirement System (PERS)

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

PERS Plan 1 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service. The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service. Members retiring from active status prior to the age of 65 may receive actuarially reduced benefits. Retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries. PERS 1 members were vested after the completion of five years of eligible service. The plan was closed to new entrants on September 30, 1977.

Contributions

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

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

PERS Plan 2/3 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service for Plan 2 and 1 percent of AFC for Plan 3. The AFC is the average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who

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have at least 20 years of service credit and are 55 years of age or older, are eligible for early retirement with a benefit that is reduced by a factor that varies according to age for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions:

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

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service credit. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit. Other PERS Plan 2/3 benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the CPI), capped at three percent annually and a one-time duty related death benefit, if found eligible by the Department of Labor and Industries. PERS 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service if 12 months of that service are earned after age 44.

PERS Plan 3 defined contribution benefits are totally dependent on employee contributions and investment earnings on those contributions. PERS Plan 3 members choose their contribution rate upon joining membership and have a chance to change rates upon changing employers. As established by statute, Plan 3 required defined contribution rates are set at a minimum of 5 percent and escalate to 15 percent with a choice of six options. Employers do not contribute to the defined contribution benefits. PERS Plan 3 members are immediately vested in the defined contribution portion of their plan.

Contributions

The **PERS Plan 2/3** employer and employee contribution rates are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. The Plan 2/3 employer rates include a component to address the PERS Plan 1 UAAL and an administrative expense that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and Plan 3 contribution rates. The PERS Plan 2/3 required contribution rates (expressed as a percentage of covered payroll) for 2016 were as follows:

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

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Total	11.18%	6.12%
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The District's actual PERS plan contributions were \$41,877 to PERS Plan 1 and \$54,694 to PERS Plan 2/3 for the year ended December 31, 2016.

Actuarial Assumptions

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

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

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

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

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

- For all systems, the assumed valuation interest rate was lowered from 7.8% to 7.7%. Assumed administrative factors were updated.

Discount Rate

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

To determine that rate, an asset sufficiency test included an assumed 7.7 percent long-term discount rate to determine funding liabilities for calculating future contribution rate requirements.

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

Long-Term Expected Rate of Return

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

Estimated Rates of Return by Asset Class

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

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

Sensitivity of the Net Pension Liability/(Asset)

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

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
PERS 1	\$486,172	\$403,161	\$331,725
PERS 2/3	\$891,793	\$484,359	(\$252,137)

Pension Plan Fiduciary Net Position

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

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

At June 30, 2016, the District reported a total pension liability of \$887,520 for its proportionate share of the net pension liabilities as follows:

	Liability
PERS 1	\$403,161
PERS 2/3	\$484,359

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

	Proportionate Share 6/30/15	Proportionate Share 6/30/16	Change in Proportion
PERS 1	0.006960%	0.007507%	0.000547%
PERS 2/3	0.008989%	0.009620%	0.000631%

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

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

Pension Expense

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

	Pension Expense
PERS 1	\$50,265
PERS 2/3	\$75,932

Deferred Outflows of Resources and Deferred Inflows of Resources

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

PERS 1	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$0	\$0
Net difference between projected and actual investment earnings on pension plan investments	\$10,151	\$0
Changes of assumptions	\$0	\$0
Changes in proportion and differences between contributions and proportionate share of contributions	\$0	\$0
Contributions subsequent to the measurement date	\$20,633	\$0
TOTAL	\$30,784	\$0

PERS 2/3	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$25,792	(\$15,989)
Net difference between projected and actual investment earnings on pension plan investments	\$59,272	\$0
Changes of assumptions	\$5,006	\$0

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Changes in proportion and differences between contributions and proportionate share of contributions	\$29,404	\$0
Contributions subsequent to the measurement date	\$26,947	\$0
TOTAL	\$146,421	(\$15,989)

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

Year ended December 31:	PERS 1
2017	(\$2,499)
2018	(\$2,499)
2019	\$9,323
2020	\$5,827
2021	\$0
Thereafter	\$0
Total	\$10,151

Year ended December 31:	PERS 2/3
2017	\$10,512
2018	\$10,512
2019	\$53,124
2020	\$29,336
2021	\$0
Thereafter	\$0
Total	\$103,484

NOTE 7 – INSURANCE / RISK MANAGEMENT

Thurston PUD, along with seventeen other public utility districts and one joint operating agency, is a member of the Public Utilities Risk Management Services (PURMS) self-insurance fund. The program provides members with various liability, property and health insurance coverage in three separate pools. Thurston PUD is a member of the PURMS health & welfare (H&W) pool. As a former member of the liability and property pools of PURMS Thurston PUD continues to receive coverage from the pool for occurrences that happened while they were a member (years through 2010). Withdrawn PURMS members continue to be responsible for their share of assessments for occurrences that happen to all members while they were a member.

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The PURMS H&W pool maintains funded reserves in an amount approximately equal to the sum of three (3) times the amount of each member's historical average monthly H&W claims experience for its respective employees and their dependents. The H&W pool's operations are financed through assessments of its participating members. Assessments for the H&W pool are based on a formula that takes into account the H&W claims cost of each member's employees, as well as an allocated portion of shared administrative expenses.

Thurston PUD is a member of the Washington Cities Insurance Authority (WCIA). Utilizing Chapter 48.62 RCW (self-insurance regulation) and Chapter 39.34 RCW (Interlocal Cooperation Act), nine cities originally formed WCIA on January 1, 1981. WCIA was created for the purpose of providing a pooling mechanism for jointly purchasing insurance, jointly self-insuring, and / or jointly contracting for risk management services. WCIA has a total of 168 members.

New members initially contract for a three-year term, and thereafter automatically renew on an annual basis. A one-year withdrawal notice is required before membership can be terminated. Termination does not relieve a former member from its unresolved loss history incurred during membership.

Liability coverage is written on an occurrence basis, without deductibles. Coverage includes general, automobile, police, public officials' errors or omissions, stop gap, and employee benefits liability. Limits are \$4 million per occurrence in the self-insured layer, and \$16 million per occurrence in the re-insured excess layer. The excess layer is insured by the purchase of reinsurance and insurance and is subject to aggregate limits. Total limits are \$20 million per occurrence subject to aggregate sublimits in the excess layers. The Board of Directors determines the limits and terms of coverage annually.

Insurance for property, automobile physical damage, fidelity, inland marine, and boiler and machinery coverage are purchased on a group basis. Various deductibles apply by type of coverage. Property coverage is self-funded from the members' deductible to \$750,000, for all perils other than flood and earthquake, and insured above that to \$300 million per occurrence subject to aggregates and sublimits. Automobile physical damage coverage is self-funded from the members' deductible to \$250,000 and insured above that to \$100 million per occurrence subject to aggregates and sublimits.

In-house services include risk management consultation, loss control field services, and claims and litigation administration. WCIA contracts for certain claims investigations, consultants for personnel and land use issues, insurance brokerage, actuarial, and lobbyist services.

WCIA is fully funded by its members, who make annual assessments on a prospectively rated basis, as determined by an outside, independent actuary. The assessment covers loss, loss adjustment, and administrative expenses. As outlined in the governing interlocal agreement, WCIA retains the right to additionally assess the membership for any funding shortfall.

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An investment committee, using investment brokers, produces additional revenue by investment of WCIA's assets in financial instruments which comply with all State guidelines.

A Board of Directors governs WCIA, which is comprised of one designated representative from each member. The Board elects an Executive Committee and appoints a Treasurer to provide general policy direction for the organization. The WCIA Executive Director reports to the Executive Committee and is responsible for conducting the day to day operations of WCIA.

The District has no settlements in the last 3 years exceeding coverage.

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NOTE 8– LONG-TERM DEBT

Thurston PUD issues revenue bonds to finance the purchase of capital assets and the acquisition or construction of water systems. Bonded indebtedness has also been entered into in prior years to advance refund the District's previous revenue bond issues. Revenue bonds are repaid using the water revenue of the District. The District is also liable for other loans obtained through state and federal programs to improve the condition of existing water infrastructure.

The District has pledged future water revenue, net of operating expenses to repay \$2,990,000 in water revenue bonds issued in 2011. Proceeds from the bonds provide financing for water system improvements and replacements as well as new water system construction and acquisition. The bonds are payable solely from water revenue and are payable through 2031. Annual principal and interest payments on the bonds are expected to require less than 50 percent of net revenues. The total principal and interest remaining to be paid on the bonds is \$2,442,088. Principal and interest paid for the current year and total water revenue, net of operating expenses were \$301,756 and \$609,446 respectively.

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The Long-Term Debt currently outstanding are as follows:

Purpose	Maturity Range	Stated Interest Rate	Original Amount	Amount of 2016 Installment
Public Works Loan PW04-691-PRE126	2024	0.5%	\$ 1,000,000	\$ 52,632
Water Revenue Bond 2011	2011 - 2031	3.0% - 4.45%	\$ 2,990,000	\$ 225,000
Water System Revenue Bond Anticipation Note 2014	2028	3.0%	\$ 1,000,000	\$ -
Drinking Water State Revolving Fund Loan DM09-952-026	2029	0.5%	\$ 1,028,180	\$ 48,992
Drinking Water State Revolving Fund Loan DM09-952-027	2029	0.5%	\$ 2,109,661	\$ 94,158
Drinking Water State Revolving Fund Loan DM12-952-103	2036	1.0%	\$ 165,400	\$ -
Drinking Water State Revolving Fund Loan DM12-952-113	2036	1.0%	\$ 370,725	\$ -
Drinking Water State Revolving Fund Loan DM15-952-035	3038	1.0%	\$ 194,350	\$ -
Drinking Water State Revolving Fund Loan 03-65103-029	2024	0.5%	\$ 93,017	\$ 8,456
Drinking Water State Revolving Fund Loan 03-65103-030	2024	0.5%	\$ 88,298	\$ 8,027
Drinking Water State Revolving Fund Loan 03-65103-031	2034	0.0%	\$ 112,009	\$ 5,334
Drinking Water State Revolving Fund Loan 03-65103-032	2024	1.5%	\$ 85,281	\$ 7,752
Drinking Water State Revolving Fund Loan 01-65101-039	2025	1.5%	\$ 41,127	\$ 3,427
Total Authorized Debt			\$ 9,278,048	\$ 453,778

In 2013, the District obtained loan financing for two capital projects through the Drinking Water State Revolving Fund loan program. The cost of these capital projects is expected to total \$536,125. One was completed in 2016 and the other is expected to be completed in 2017. Principal and interest on these obligations has been deferred until 2017, each of these loans has a term of 20 years and interest rate of 1.0%.

In June 2014, the District authorized a Registered Revenue Bond Anticipation Note in the form of a non-revolving line of credit with Cashmere Valley Bank in the amount of \$1,000,000 to provide available funds for water system acquisitions and/or improvements. On December 31, 2016 the District issued a total of \$863,000 against this note. The initial draw of \$403,000 will have a fixed rate of 2.5731% for the initial four years, subsequent draws bear interest at the

PUBLIC UTILITY DISTRICT NO. 1 OF THURSTON COUNTY
 NOTES TO FINANCIAL STATEMENTS
 January 1, 2016 through December 31, 2016

variable rate of 65.01% of the prime rate. Semi-annual interest payments are due December 1 and June 1 beginning December 1, 2014 to and including June 1, 2018. Whatever principal amount remains outstanding as of that date will then be converted to an amortizing ten year term loan.

In 2015, the District was awarded a Drinking Water State Revolving Fund loan to finance the installation of disinfection treatment on a small water system in Thurston County. The cost of the treatment system is expected be \$194,350 and is expected to be complete in 2017. Principal and interest on this obligation has been deferred until 2019, the loan has a term of 20 years and interest rate of 1.0%, with forgiveness of loan principal at completion of 50%.

The annual requirements to amortize all debts outstanding as of December 31, 2016, including interest, are as follows:

Year Ending December 31	Principal	Interest	Total
2017	\$ 468,715	\$ 97,409	\$ 566,124
2018	\$ 511,056	\$ 90,126	\$ 601,182
2019	\$ 521,614	\$ 81,190	\$ 602,804
2020	\$ 522,181	\$ 71,945	\$ 594,126
2021	\$ 347,756	\$ 62,691	\$ 410,447
2022-2026	\$ 1,650,545	\$ 239,052	\$ 1,889,597
2027-2031	\$ 1,225,653	\$ 106,705	\$ 1,332,358
2032-2036	\$ 302,464	\$ 15,911	\$ 318,375
2037-2041	\$ 49,500	\$ 740	\$ 50,240
Total	\$ 5,599,484	\$ 765,769	\$ 6,365,253

There is \$509,410 in restricted assets of the district. These represent sinking funds and reserve requirements contained in the various indentures. There are a number of other limitations and restrictions contained in the various bond indentures. The District is in compliance with all significant limitations and restrictions.

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 January 1, 2016 through December 31, 2016

NOTE 9 – CHANGES IN LONG-TERM LIABILITIES

During the year ended December 31, 2016, the following changes occurred in long-term liabilities:

	Beginning Balance 01/01/2016	Additions	Reductions	Ending Balance 12/31/2016	Due Within One Year
Revenue Bonds	\$ 2,160,000	\$ -	\$ 225,000	\$ 1,935,000	\$ 230,000
Revenue Bond Anticipation Notes	\$ 403,000	\$ 460,000	\$ -	\$ 863,000	\$ -
Total Bonds Payable	\$ 2,563,000	\$ 460,000	\$ 225,000	\$ 2,798,000	\$ 230,000
Public Works Trust Fund Loans	\$ 473,684	\$ -	\$ 52,632	\$ 421,052	\$ 52,632
Drinking Water State Revolving Fund Loans	\$ 2,391,858	\$ 164,717	\$ 176,146	\$ 2,380,428	\$ 186,083
Pension Liability	\$ 685,255	\$ 202,266	\$ -	\$ 887,521	\$ -
Compensated absences	\$ 79,428	\$ -	\$ 674	\$ 78,754	\$ 71,084
Total Long-Term Liabilities	\$ 6,193,225	\$ 826,983	\$ 454,453	\$ 6,565,755	\$ 539,799

NOTE 10 – LEASES

In September 2015, Thurston PUD entered into a new three-year lease for office space and parking stalls at 921 Lakeridge Way SW, Olympia WA 98502. In 2015, the cost for the lease was \$49,200.00 annually with no change since 2011 or throughout the next three year term. The terms of the lease allow the District to vacate the premises with 90 days' notice if needed, and also provides the District with the option to extend the lease for an additional three year terms at a re-negotiated rental rate.

In 2014 the District entered into a 5 year operating lease for a color copier/network printer, replacing a printer purchased in 2005. The total cost for this lease in 2015-2019 is \$3,673.20 annually.

NOTE 11 – COMMITMENTS

Purchase Water Agreement

The District has entered into a purchase water agreement with the city of Lacey to supply water to a small water system served by the District after the well serving that water system was found to contain arsenic above the maximum contaminant level. The water system affected serves 15 residences and represents a very small segment of customers served by the District.

NOTE 12 – GRANTS

In 2015 the District was awarded a loan with 50% loan forgiveness from the Drinking Water State Revolving Fund (DWSRF) to install 4 Log Disinfection Treatment system on the

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January 1, 2016 through December 31, 2016

Skookumchuck water system. The total project is expected to cost \$196,264 and will be completed in 2017. The District has initiated the required environmental and cultural review studies, no draws on this contract were taken in 2016.

In November 2014 Thurston PUD was awarded a grant from the Community Development Block Grant Program as a subrecipient of the Pierce County Community Connections in the amount of \$170,000 to rehabilitate the Webster Hill water system in Pierce County. Construction of the project began in the summer of 2015 and was completed in 2016. The District drew \$57,775 in 2016 against this grant to complete the project.

In 2016 Thurston PUD was awarded a grant from the Washington State Department of Health in the amount of \$30,000 to conduct a study of the feasibility of acquiring the Cedar Ridge Estates water system in Thurston County. The District did not draw against this grant in 2016, the work was completed in January 2017 and the District received \$17,406 against this grant.

In 2012, the District was awarded a loan with 50% loan forgiveness from the DWSRF to consolidate a Thurston County group A water system with 2 adjacent group B water systems. In 2016 the District completed the majority of the project with close out late in the year. The District has received \$134,434 in grant income from this project.

NOTE 13 – TRANSFER OF OPERATIONS

On November 1, 2016, Thurston PUD acquired the Frog Hollow, 1, 2 and 3 water systems and the Redtail Hawk water system, from the Violet Prairie Water Company. The acquisition includes all related property consisting of and associated with the water system, including all wells, pump houses, storage tanks, water rights, water mains, pipes, valves, pumps, reservoirs, boosters, water treatment facilities, service meters and other facilities to serve 66 customers. The acquisition value of the assets acquired in this transaction is approximately \$513,811. The net position impact of this acquisition increased \$443,162 as of the acquisition date.

NOTE 14 – SUBSEQUENT EVENTS

On May 5, 2017 the District issued \$1.5 million Bond Anticipation Note to Cashmere Valley Bank to provide moneys necessary to pay for the acquisition of commercial real estate in Lacey Washington to be the new primary office space for the District. The bond anticipation note bears interest at the rate of 2.6 percent and will be interest only until June 1, 2019. The District plans to issue Revenue Bonds in 2017 to pay off this 2017 Bond Anticipation Note, the 2014 Bond Anticipation Note and to secure additional financing for implementation of the Asset Management Plan.

On October 1, 2017 the District issued a \$7.7 million Bond Anticipation Note to Cashmere Valley Bank to provide funding to acquire the water systems and other assets of H&R

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Waterworks, Incorporated for an amount of \$7,522,500. This increased the water system owned and operated by the District to 303 and increased total connections to 8,212. The bond anticipation note bears interest at the rate of 2.88 percent and will be interest only until repaid by the 2017 Revenue Bonds expected to be issued by the end of the year.

Schedule of Proportionate Share of the Net Pension Liability

As of June 30 (measurement date)

Last 10 Fiscal Years*

Public Employees' Retirement System Plan 1	<u>2016</u>	<u>2015</u>
<u>Employer's proportion of the net pension liability</u>	0.007507%	0.006960%
<u>Employer's proportionate share of the net pension liability</u>	\$ 403,161	\$ 364,073
<u>Employer's covered employee payroll</u>	\$ 863,175	\$ 795,446
<u>Employer's proportionate share of the net pension liability as a percentage of covered employee payroll</u>	46.71%	45.77%
<u>Plan fiduciary net position as a percentage of the total pension liability</u>	57.03%	59.10%
Public Employees' Retirement System Plans 2 & 3	<u>2016</u>	<u>2015</u>
<u>Employer's proportion of the net pension liability</u>	0.009620%	0.008989%
<u>Employer's proportionate share of the net pension liability</u>	\$ 484,359	\$ 321,182
<u>Employer's covered employee payroll</u>	\$ 863,175	\$ 795,446
<u>Employer's proportionate share of the net pension liability as a percentage of covered employee payroll</u>	56.11%	40.38%
<u>Plan fiduciary net position as a percentage of the total pension liability</u>	85.82%	89.20%

Notes to Schedule:

*This schedule will be built prospectively until it contains 10 years of data

*There were no changes in benefit terms or assumptions

Schedule of Employer Contributions

As of December 31
Last 10 Fiscal Years*

Public Employees' Retirement System Plan 1	<u>2016</u>	<u>2015</u>
<u>Statutorily or contractually required contributions</u>	\$ 41,877	\$ 35,597
<u>Contributions in relation to the statutorily or contractually required contributions</u>	\$ (41,877)	\$ (35,597)
<u>Contribution deficiency (excess)</u>	<u>\$ -</u>	<u>\$ -</u>
<u>Covered employer payroll</u>	\$ 877,912	\$ 809,212
<u>Contributions as a percentage of covered employee payroll</u>	4.77%	4.40%

Public Employees' Retirement System Plans 2 & 3	<u>2016</u>	<u>2015</u>
<u>Statutorily or contractually required contributions</u>	\$ 54,694	\$ 62,787
<u>Contributions in relation to the statutorily or contractually required contributions</u>	\$ (54,694)	\$ (62,787)
<u>Contribution deficiency (excess)</u>	<u>\$ -</u>	<u>\$ -</u>
<u>Covered employer payroll</u>	\$ 877,912	\$ 809,212
<u>Contributions as a percentage of covered employee payroll</u>	6.23%	7.76%

Notes to Schedule:

*This schedule will be built prospectively until it contains 10 years of data

*There were no changes in benefit terms or assumptions

ABOUT THE STATE AUDITOR'S OFFICE

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

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

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

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

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

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

Contact information for the State Auditor's Office	
Public Records requests	PublicRecords@sao.wa.gov
Main telephone	(360) 902-0370
Toll-free Citizen Hotline	(866) 902-3900
Website	www.sao.wa.gov