



Report of Independent Auditors and
Financial Statements

Public Utility District No. 1 of
Klickitat County

December 31, 2010 and 2009

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

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REPORT OF INDEPENDENT AUDITORS

Board of Commissioners
Public Utility District No. 1 of Klickitat County
Goldendale, Washington

We have audited the accompanying combined balance sheet of Public Utility District No. 1 of Klickitat County (the District) as of December 31, 2010 and 2009 and the related combined statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These combined financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Public Utility District No. 1 of Klickitat County as of December 31, 2010 and 2009 and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying Management's Discussion and Analysis 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.

Moss Adams LLP

Portland, Oregon
August 29, 2011

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
DIRECTORY OF OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>	<u>Term Expiration</u>
Board of Commissioners			
President	Ray A. Mosbrucker	6 years	December 2010
Vice President	Randy L. Knowles	6 years	December 2012
Secretary	Dan G. Gunkel	6 years	December 2014
Appointed Officials			
General Manager	James R. Smith	1313 S. Columbus	
Chief Financial Officer/Auditor	Shannon N. Crocker	Goldendale, WA 98620	
Public Utility District No. 1 of Klickitat County - Attorney	Ronald J. English	15624 111th Avenue N.E. Bothell, WA 98011	

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785 MANAGEMENT’S DISCUSSION AND ANALYSIS

This section provides an overview and analysis of key data presented in the basic financial statements for the years ended December 31, 2010 and 2009. Information within this section should be read in conjunction with the basic financial statements and accompanying notes.

OVERVIEW OF THE FINANCIAL STATEMENTS

Public Utility District No. 1 of Klickitat County (the District) consists of the electric system, eight water systems and five wastewater systems. The District’s service area covers approximately 1,680 square miles in Klickitat County. The District also serves small areas in the surrounding counties of Yakima, Skamania and Benton. As of December 31, 2010 the District had 12,157 electric, 1,141 water and 1,158 wastewater customers. The District’s wholesale activity is a significant part of the electric system business lines. Wholesale revenues are generated from the sale of the output from the Landfill Gas Project, a 10.5 MW facility, and from the White Creek Wind I power purchase contract, which the District owns 13% of the generated output from the 205 MW project.

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

The Balance Sheet presents information on the District’s assets and liabilities, with the difference between the two reported as net assets, and provides information regarding the nature and amount of resource investment (assets) and obligations incurred in the pursuit of such resources. This statement also provides a vehicle for evaluating the capital structure of the District and assessing liquidity and financial flexibility of the District.

The Statement of Revenues, Expenses and Changes in Net Assets reports revenues and expenses as well as change in net assets (net income) for this period. This statement provides a measurement of the District’s operations, helps to evaluate the level of cost recovery from charges for products and services, and can be used as a partial determinant of creditworthiness.

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

The Notes to Financial Statements provide additional information that is essential to a full understanding of the financial statements, as described above, including significant accounting policies, commitments, obligations, risks, contingencies and other financial matters of the District.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
MANAGEMENT’S DISCUSSION AND ANALYSIS

Financial Highlights - 2010 to 2009

- The year ended December 31, 2010 financial results showed the continued financial strength of the District. The District was in compliance with its debt service coverage covenant at year-end with a change in net assets of \$22,267,750. A large portion of this change is from contributions of Transmission Plant for three different Wind projects, while \$3,850,574 is from Operations.
- In 2010 the District expended \$36.8 million on construction of the Land Fill Gas II (LFG II) project and \$7.5 million on Electric Distribution capital construction. LFG II is a 26.5 MW gas-fired combustion turbine and steam recovery generating facility located at the Roosevelt landfill expected to be online in 2011.
- In October 2010 the District took a first draw of \$232,248 on the Drinking Water State Revolving Fund Loan of \$1,175,566 for Glenwood’s Water System. The project will replace distribution lines and develop an additional water source for the Glenwood Water System, lifting moratoriums on new connections due to undersized distribution lines.
- The District receives transmission revenues for providing transmission services for the White Creek Wind I project, Harvest Wind, Tuolumne, Windy Flats, Linden Farms, Windy Point and from the Goldendale Energy Center, a 248 MW natural gas-fired combined cycle combustion turbine electric generating facility owned and operated by Puget Sound Energy. The revenue received from this business-line was approximately \$5,145,000.
- Customer growth was near 1% in 2010, which is consistent over the last 4 years. Energy consumption was 1% lower than in 2009.
- Staff worked with each local community in which we serve either water or wastewater or both to review operations, rates and projected future projects. Rate increases were adopted for those systems where revenues did not cover estimated expenses and debt service.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
MANAGEMENT’S DISCUSSION AND ANALYSIS

Financial Highlights – 2009 to 2008

- The year ended December 31, 2009 financial results showed the continued financial strength of the District. The District was in compliance with its debt service coverage covenant at year-end with a change in net assets of \$18,244,717. A large portion of this change is from contributions of Transmission Plant for three different Wind projects, while \$7,340,408 is from operations.
- In 2009 the District completed a \$42.35 million bond sale to fund the remaining construction on the Land Fill Gas II (LFG II) project and provide three years of funding for Electric Distribution capital construction.
- In June 2008 the District completed the transaction with Lewis PUD to sell 10% of our 26% share of the White Creek Wind I project power output. In December 2008, the District also sold 3% of our remaining 16% share of the White Creek Wind I project Power output to Benton PUD. The proceeds of \$36,846,000 and \$11,053,800 from Lewis PUD and Benton PUD, respectively, were used to pay down the bond anticipation note of \$47,000,000 to \$5,000,000. The gain on the sale of White Creek power rights was \$23,678,404.
- In April 2008 the District approved a loan payoff on the Klickitat Water and Wastewater System in the amount of \$214,200 plus interest of \$5,535.
- The District receives transmission revenues for providing transmission services for various utilities in the White Creek Wind I project and from the Goldendale Energy Center, a 248 MW natural gas-fired combined cycle combustion turbine electric generating facility owned and operated by Puget Sound Energy. The revenue received from this business-line was approximately \$3,782,000.
- Customer growth was near 1% in 2009, which is consistent over the last 3 years. Energy consumption was 5% lower than in 2008.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
MANAGEMENT'S DISCUSSION AND ANALYSIS

Condensed Comparative Financial Information

Combined Balance Sheet

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Capital assets	\$ 222,592,618	\$ 167,546,723	\$ 115,858,833
Current, restricted and other assets	<u>65,613,629</u>	<u>103,677,107</u>	<u>89,691,828</u>
Total assets	<u>\$ 288,206,247</u>	<u>\$ 271,223,830</u>	<u>\$ 205,550,661</u>
Long-term liabilities	\$ 130,292,057	\$ 133,779,264	\$ 94,694,565
Current liabilities	<u>18,654,715</u>	<u>20,452,841</u>	<u>12,109,088</u>
Total liabilities	<u>148,946,772</u>	<u>154,232,105</u>	<u>106,803,653</u>
Invested in capital assets, net of related debt	91,370,913	72,287,796	55,474,073
Restricted	13,728,023	13,403,331	8,989,531
Unrestricted	<u>34,160,539</u>	<u>31,300,598</u>	<u>34,283,404</u>
Total net assets	<u>139,259,475</u>	<u>116,991,725</u>	<u>98,747,008</u>
Total liabilities and net assets	<u>\$ 288,206,247</u>	<u>\$ 271,223,830</u>	<u>\$ 205,550,661</u>

Capital Activity

2010 to 2009

Net utility plant for the District increased \$55 million during 2010. Some of the large projects completed to plant in 2010 were Linden Farm Wind, Biogas II Substation, Windy Flats, Harvest Wind, and Spearfish Substation Addition. These five projects contributed \$26 million to plant assets. Currently the District is in the process of constructing our LFG II facility expending \$36.8 million on this project in 2010.

2009 to 2008

Net utility plant for the District increased \$52 million during 2009. Some of the large projects completed to plant in 2009 were Energizer Substation, Rock Creek to Willis Transmission, and Willis Substation. These three projects contributed \$11.9 million to plant assets. Currently the District is in the process of constructing our LFG II facility expending \$34.5 million on this project in 2009.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
MANAGEMENT’S DISCUSSION AND ANALYSIS

Debt Activity

2010 to 2009

The District took a first draw of \$232,248 on the Drinking Water State Revolving Fund Loan of \$1,175,566 for Glenwood’s Water System. The project will replace distribution lines and develop an additional water source for the Glenwood Water System with expected completion in 2011.

2009 to 2008

The District issued \$42,350,000 in electric system revenue bonds in December 2009. The proceeds are being used to fund LFG II, a methane gas fired combustion turbine and steam recovery plant to generate 26.5 MW of electricity. The plant is expected to come on line in 2011.

Current, Restricted and Other Activity

2010 to 2009

Current, restricted and other assets decrease by \$38 million, primarily due to the expenditure of \$36.8 million in funds for construction of Landfill Gas II project.

2009 to 2008

Current, Restricted and Other assets increased by \$13.9 million, primarily due to \$13.5 million designated for the next three years of capital construction from bond proceeds.

Overall Results of Operations

2010 to 2009

The District’s 2010 results are 25% better than expectations set during the planning and budget process. Net operating income of \$5,198,591 puts the District in a position of continued financial strength.

2009 to 2008

The District’s 2009 results met or exceeded expectations set during the planning and budget process. Net operating income of \$7,340,408 puts the District in a position for continued financial strength.

Electric System Operating Results

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Operating revenues	\$ 39,148,172	\$ 41,104,154	\$ 37,970,633
Operating expenses	<u>33,984,179</u>	<u>33,638,316</u>	<u>34,081,266</u>
Operating income	5,163,993	7,465,838	3,889,367
Net non-operating revenue (expense)	(3,513,666)	(2,679,412)	19,936,317
Capital contributions	<u>20,504,483</u>	<u>12,726,042</u>	<u>1,872,245</u>
Change in net assets (net income)	<u>\$ 22,154,810</u>	<u>\$ 17,512,468</u>	<u>\$ 25,697,929</u>

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
MANAGEMENT'S DISCUSSION AND ANALYSIS

Operating Revenues

2010 to 2009

The District had decreased retail sales of 3,493,486 KWH during 2010 leading to decreased electric revenues of \$1,955,982 over 2009 as follows: Residential sales down \$330,642, general service sales up \$115,961, industrial sales down \$133,660, irrigation sales down \$30,033 and street lighting up \$1,031. Other wholesale and transmission electric revenues decreased \$1,578,639 mainly due to decreased prices in wholesale markets for our Landfill Gas and wind generation projects that are located within Klickitat County. Overall revenues decreased by 5% during 2010.

2009 to 2008

The District had increased retail sales of 16,009,208 KWH during 2009 which led to increased electric revenues of \$3,133,521 over 2008 as follows: Residential sales up \$978,684, general service sales up \$704,528, industrial sales up \$425,755, irrigation sales down \$110,814 and street lighting up \$2,920. Other wholesale and transmission electric revenues increased \$1,132,447 mainly due to increased wheeling fees on transmission lines serving multiple wind generation projects that are located within Klickitat County. Overall Revenues increased by 8% during 2009.

Operating Expenses

2010 to 2009

Operating expense increased in 2010 by \$345,863. Power, Operations and Maintenance costs are down \$121,204 because of decreased power generation and purchases during 2010. Admin and General expense increased by \$659,340 mainly due to expensing consulting fees to The Energy Authority in preparation for upcoming Slice Contract with BPA during 2010. Taxes accrued for state and municipal governments decreased \$763,538 due a change in estimate in accrued taxes and a credit received on privilege tax during 2010. Finally depreciation expense increased on Distribution and Transmission Plant by \$522,669 due to the large amount of work orders closed in 2010 for these asset classes.

2009 to 2008

Operating expenses were down slightly in 2009 by \$442,950. Power, Operations and Maintenance costs up \$389,755 because of increased aerial distribution maintenance during 2009. Admin and General expense decreased by \$454,462 mainly due to general expense being higher in 2009. Taxes assessed by state and municipal governments increased \$193,534 as a result of the increase in generation power sales for the landfill gas project, wind project and the increase in transmission revenues now collected by the District for services on the various generation projects. Finally depreciation expense increased on Transmission Plant by \$298,146 due the large amount of work orders closed in 2009 for this asset class. Expenses decreased .1% from 2008.

Non-operating Revenue/(Expense)

2010 to 2009

Non-operating income overall decreased in 2010 by \$834,254 due to several factors. New interest expense incurred for the 2009 Bond Issue raised interest expense by \$385,521 after the refund of interest for Build America Bonds. Investment income decreased \$317,926 due to lower cash availability throughout the year because of funding of construction projects and continued lower interest rates in the state investment pool during 2010. Rent revenues decreased by \$108,640 during 2010.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
MANAGEMENT’S DISCUSSION AND ANALYSIS

Non-operating Revenue/(Expense) – (continued)

2009 to 2008

Non-operating income decreased in 2009 mainly due to the sale of 13% of the District’s 26% White Creek power rights resulting in a gain of \$23,678,404 in 2008. Other income items changes in 2009 are: Interest expense down \$1,463,879 due to during 2008 increased interest payments for bond anticipation notes. Investment income decreased \$1,073,970 due to lower cash availability throughout the year because of funding of construction projects and continued lower interest rates in the state investment pool during 2009. Other income increased by \$790,870 mainly due to a DOE renewable energy credit received for \$437,029 and scheduling services and fees increases for Wind Project for \$176,976.

Capital Contributions

2010 to 2009

Capital contributions increased \$7,778,441 in 2010 over 2009. The capital contributions in 2010 were above normal contributions for a given year due to an \$18.4 million contribution of plant assets from the District’s agreements with Harvest Wind, Windy Flats and Linden Farms to maintain and operate transmission and substation equipment.

2009 to 2008

Capital contributions increased \$10,853,797 from the previous year. The capital contributions in 2009 were above normal contributions for a given year due to an \$11.9 million contribution of plant assets from our agreements with Windy Point Partners to maintain transmission and substation equipment which the District operates and maintains.

Legal Settlement

There were no legal issues during 2010 or 2009 where the District received or disbursed a settlement.

Water and Wastewater Systems Operating Results

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Operating revenues	\$ 1,351,946	\$ 1,414,787	\$ 1,411,738
Operating expenses	<u>1,317,348</u>	<u>1,540,216</u>	<u>838,897</u>
Operating income	34,598	(125,429)	572,841
Net non-operating revenue/(expense)	15,515	(14,226)	(14,445)
Capital contributions and grants	<u>62,827</u>	<u>871,905</u>	<u>17,904</u>
Change in net assets (net income)	<u>\$ 112,940</u>	<u>\$ 732,250</u>	<u>\$ 576,300</u>

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
MANAGEMENT'S DISCUSSION AND ANALYSIS

Operating Revenues

2010 to 2009

The District Water/Waste Water revenues are down in 4% in 2010 mainly due to large sewer connection fees being recorded in 2009 for one customer in the amount of \$62,183. All other revenues were essentially unchanged from 2009.

2009 to 2008

The District Water/Waste Water revenues were essentially unchanged from 2008.

Operating Expenses

2010 to 2009

The expenses to operate the Water/Waste Water systems were down 14% or \$222,868 compared to a year ago. This decrease in operating expenses can be attributed to a change in the methodology of allocating Administrative Costs to Water/Waste Water systems during 2009 and 2010. Also, initial cost of taking over operations for the Dallesport Wastewater and Industrial Park Water Systems only appears in 2009 not 2010.

2009 to 2008

The expenses to operate the Water/Waste Water systems were up 84% or \$701,319 compared to a year ago. This increase in operating expenses can be attributed to the takeover of operations for the Dallesport Wastewater and Industrial Park Water Systems having a full year of expenses in 2009 as opposed to only a half year expenses in 2008. These two systems represented \$345,036 of expenses in 2009. Depreciation expense is up by 158% or \$295,623 due to the booking of a large amount of depreciable plant at the end of 2007 for phase II and III of the Klickitat Water and Waste Water projects collection system and treatment plant.

Non-operating Revenue/(Expense)

2010 to 2009

Non-operating revenue increased primarily due to service connection charges in the amount of \$15,497 for Dallesport Sewer system during 2010.

2009 to 2008

Non-operating expenses were basically unchanged between 2009 and 2008.

Capital Contributions & Grants

2010 to 2009

Capital contributions were in line with expectations during 2010 as no significant LUD's were established.

2009 to 2008

The significant increase of \$854,001 was primarily due to establishment of Ponderosa Park LUD contributing \$828,200 during 2009.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
MANAGEMENT’S DISCUSSION AND ANALYSIS

The District Looking Forward 2011

The District issued bonds in 2009 to finance a portion of the additional capacity at the Landfill II Gas (LFG II) Generating Facility by approximately 26 MW’s. The anticipated capital cost is around \$65 million for the entire project. LFG II is expected to be on line in July 2011.

The District anticipates that additional transmission projects will surface during 2011 along with those undertaken during 2010 due to other entities locating wind projects within Klickitat County. These capital costs are paid for by project developers.

The District sees many challenges and opportunities in the coming years with additional projects in transmission, landfill gas and wind generation, and a new Bonneville Power Administration power sales contract which will set rates and limit supply for the period beginning on October 1, 2011. The District is positioned to meet these changes with a solid financial position.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
COMBINED BALANCE SHEET

ASSETS

	December 31,	
	2010	2009
CURRENT ASSETS		
Cash and cash equivalents	\$ 12,639,161	\$ 15,358,699
Notes receivable	162,938	146,876
Accounts receivable, net	1,128,610	1,015,381
Unbilled revenue	1,462,226	1,583,969
Other receivables	4,063,916	4,395,313
Materials and supplies	1,529,715	1,835,291
Prepayments	244,560	246,573
Current portion of prepaid power contract	1,180,359	1,180,359
	22,411,485	25,762,461
RESTRICTED ASSETS		
Special deposits	400	400
Construction funds	3,846,789	37,417,619
Special funds	14,307,309	13,792,107
	18,154,498	51,210,126
CAPITAL ASSETS		
Total plant in service	206,110,631	168,952,097
Construction work in progress	70,647,675	48,299,053
	276,758,306	217,251,150
Total utility plant	276,758,306	217,251,150
Accumulated provision for depreciation	(54,165,688)	(49,704,427)
	222,592,618	167,546,723
OTHER ASSETS		
Other investments and transmission deposits	2,451,853	2,694,841
Deferred debits	22,595,793	24,009,679
	25,047,646	26,704,520
TOTAL ASSETS	\$ 288,206,247	\$ 271,223,830

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
COMBINED BALANCE SHEET

LIABILITIES AND NET ASSETS

	December 31,	
	2010	2009
CURRENT LIABILITIES		
Accounts payable	\$ 6,791,209	\$ 8,725,335
Current portion of long-term debt	3,391,010	2,777,287
Bond anticipation note	5,000,000	5,000,000
Consumers deposits	281,594	297,374
Other current and accrued liabilities	3,190,902	3,652,845
Total current liabilities	<u>18,654,715</u>	<u>20,452,841</u>
NONCURRENT LIABILITIES		
Compensated absences	267,443	363,481
Long-term debt	130,021,403	133,390,602
Deferred credits	3,211	25,181
Total noncurrent liabilities	<u>130,292,057</u>	<u>133,779,264</u>
Total liabilities	<u>148,946,772</u>	<u>154,232,105</u>
NET ASSETS		
Invested in capital assets, net of related debt	91,370,913	72,287,796
Restricted	13,728,023	13,403,331
Unrestricted	34,160,539	31,300,598
Total net assets	<u>139,259,475</u>	<u>116,991,725</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 288,206,247</u>	<u>\$ 271,223,830</u>

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
COMBINED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	Years Ended December 31,	
	2010	2009
OPERATING REVENUES		
Electric system		
Sales to retail customers	\$ 20,987,714	\$ 21,365,057
Sales to wholesale and transmission customers	18,160,458	19,739,096
Water/wastewater systems	1,351,946	1,414,787
Total operating revenues	40,500,118	42,518,940
OPERATING EXPENSES		
Power expense	15,427,215	15,667,600
Operations expense	7,230,448	6,011,285
Maintenance expense	2,781,833	3,818,329
Administrative and general expense	4,573,880	4,011,409
Depreciation expense	4,456,412	4,072,044
Tax expense	831,739	1,597,865
Total operating expenses	35,301,527	35,178,532
OPERATING INCOME	5,198,591	7,340,408
NON-OPERATING REVENUES/(EXPENSES)		
Interest income	170,437	483,823
Other non-operating revenues	1,418,709	1,501,351
Interest expense	(4,928,234)	(4,546,492)
Amortization expense	(159,063)	(132,320)
Total nonoperating revenues/(expenses)	(3,498,151)	(2,693,638)
INCOME BEFORE CAPITAL CONTRIBUTIONS AND GRANTS	1,700,440	4,646,770
CAPITAL CONTRIBUTIONS AND GRANTS	20,567,310	13,597,947
CHANGE IN NET ASSETS	22,267,750	18,244,717
NET ASSETS, beginning of year	116,991,725	98,747,008
NET ASSETS, end of year	\$ 139,259,475	\$ 116,991,725

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
COMBINED STATEMENT OF CASH FLOWS

	Years Ended December 31,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	\$ 40,804,708	\$ 38,716,564
Payments to suppliers for goods and services	(24,196,798)	(16,945,716)
Payments to employees for services	(6,391,239)	(5,910,860)
Taxes paid	(1,473,717)	(1,131,083)
Net cash flows from operating activities	<u>8,742,954</u>	<u>14,728,905</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Proceeds from BPA transmission deposits	242,988	242,988
Other nonoperating income	1,418,709	1,501,351
Net cash flows from noncapital financing activities	<u>1,661,697</u>	<u>1,744,339</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Principal payments on long-term debt	(2,557,263)	(232,179)
Issuance of long-term debt	-	42,350,000
Bond issuance costs	-	(585,142)
Interest payments	(4,935,937)	(4,745,787)
Capital contributions, DOE funds and grants	2,150,120	1,657,905
Deferred debits/credits - preliminary engineering	74,466	25,465
Capital expenditures	(41,085,119)	(43,819,894)
Net cash flows from capital and related financing activities	<u>(46,353,733)</u>	<u>(5,349,632)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest received	173,916	546,261
Net change in LGIP	33,055,628	(11,117,585)
Net cash flows from investing activities	<u>33,229,544</u>	<u>(10,571,324)</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	(2,719,538)	552,288
CASH AND CASH EQUIVALENTS, beginning of year	<u>15,358,699</u>	<u>14,806,411</u>
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 12,639,161</u>	<u>\$ 15,358,699</u>

PUBLIC UTILITY DISTRICT NO. 1 OF KCLICKITAT COUNTY – MCAG No. 1785
COMBINED STATEMENT OF CASH FLOWS

	Years Ended December 31,	
	2010	2009
RECONCILIATION OF OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES		
OPERATING INCOME	\$ 5,198,591	\$ 7,340,408
ADJUSTMENTS TO RECONCILE OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES		
Depreciation expense	4,456,412	4,072,044
Amortization of prepaid power contract	1,180,359	1,180,359
Loss on White Creek Public LLC investment	-	115,365
CHANGES IN OPERATING ASSETS AND LIABILITIES		
Receivables and unbilled revenue	320,370	(3,825,278)
Materials and supplies	305,576	384,493
Prepayments	2,013	(48,412)
Accounts payable	(1,934,126)	4,752,058
Customer deposits	(15,780)	22,902
Other current and accrued liabilities	(652,453)	1,010,417
Compensated absences	(96,038)	(135,953)
Deferred credits	(21,970)	(139,498)
Total adjustments	3,544,363	7,388,497
Net cash from operating activities	\$ 8,742,954	\$ 14,728,905

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization and combined financial statements – Public Utility District No. 1 of Klickitat County, Washington (the District) is a municipal corporation governed by an elected three-person Board of Commissioners. The District’s reporting entity is comprised of the combined electric system, eight water systems and five wastewater systems. All significant intercompany balances and transactions have been eliminated from the combined amounts reported. The District has no component units. The District’s service area covers approximately 1,680 square miles in Klickitat County. The District also serves small areas in the surrounding counties of Yakima, Skamania and Benton. As of December 31, 2010 the District had 12,157 electric, 1,141 water and 1,158 wastewater customers. The District’s wholesale activity is a significant part of the electric system business lines. Wholesale revenues are generated from the sale of the output from the Landfill Gas project, 10.5 MW, and from the White Creek Wind I power purchase contract. The District owns 13% of the generated output from the 205 MW project.

Basis of accounting and presentation – The accounting policies of the District conform to generally accepted accounting principles (GAAP) as applicable to proprietary funds of governments using the full accrual basis of accounting. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. Accounting records are maintained in accordance with methods prescribed by the State Auditor under the authority of Chapter 43.09 RCW, the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission (FERC) for the Electric System and the Uniform System of Accounts for Class A & B Water Utilities prescribed by the National Association of Regulatory Utility Commissioners for the Water System.

GASB Statement No. 20 requires that the District apply all GASB pronouncements as well as the pronouncements issued on or before November 30, 1989 by the Financial Accounting Standard Board (FASB) and its predecessor organizations, unless those pronouncements conflict with or contradict GASB pronouncements. As provided for in GASB Statement No. 20, the District has elected not to implement FASB Statements and Interpretations issued after November 30, 1989.

Cash equivalents – The District considers all highly liquid investments (including restricted assets) with a maturity of three months or less to be cash equivalents. Assets in the Local Government Investment Pool (LGIP) that are for operating purposes are considered cash equivalents as they can be converted to cash within one day.

Investments – The District records investments at fair value based on quoted market rates, with changes in unrealized gains and losses reported as investment income (See Note 2). Restricted funds in the LGIP are considered investments.

Accounts receivable and allowance for uncollectible accounts – Accounts receivable are recorded when invoices are issued and are written off when they are determined to be uncollectible. The allowance for uncollectible accounts includes amounts estimated through an evaluation of specific accounts, based on the best available facts and circumstances, of customers that may be unable to meet their financial obligations, and a reserve based on historical experience. The allowance for uncollectible accounts at December 31, 2010 and 2009 was \$68,287 and \$77,259, respectively.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – (continued)

Other receivables – Other receivables consists of amounts due from customers for small material purchases, certain aid in construction billings, repairs to damaged plant and equipment from accidents caused by others, funding requests to granting or loaning agencies, customers who take primary electric service from the District or have a power sales contract, and other miscellaneous items that may require invoicing that would not normally be entered into the customer service billing system.

Materials and supplies – Materials and supplies provide for additions, maintenance and repairs to utility plant and are stated at average cost.

Restricted assets – In accordance with bond resolutions and certain related agreements, separate restricted funds are required to be established. Cash and investments held in these funds are restricted for specific uses, including construction, debt service and other special reserve requirements.

Capital assets (utility plant) – Utility plant is stated at original cost or contract price or fair value if donated (See Note 3). Costs include labor, materials and related indirect costs, such as engineering, transportation and allowance for funds (i.e. interest) used during construction. Additions, renewals and betterments with a minimum cost of \$500 per item are capitalized. Repairs and minor replacements are charged to operating expenses. Unless a major retirement or a general plant asset, the cost of property and any removal cost less salvage are charged to accumulated depreciation when property is retired. Depreciation is computed using straight-line group rates; 3% for distribution plant, 2.75% for transmission plant and 1.67% to 2.5% for generating plant. Depreciation of water and wastewater plant has been computed over useful lives of 25 to 40 years. General plant composite rates range from 2.2% to 14.4%.

Unamortized debt expense and premium – Bond issue costs are amortized to amortization expense using the straight-line method over the term of the bonds. Bond premium is amortized to interest expense, using the weighted average method over the term of the bonds.

Other investments – Consists of investment in White Creek Public LLC carried on the equity basis of accounting.

Transmission deposits – Consists of deposits for certain transmission services paid to Bonneville Power Administration (BPA).

Unamortized prepaid power contract – Consists of prepaid power amortized using the straight-line method over the term of the contract (See Note 4).

Compensated absences – Compensated absences are absences for which employees will be paid, such as vacation and sick leave. The District records compensated absences as an expense and liability when earned. Vacation pay and sick leave pay policies were superseded by a Personal Time Off (PTO) Policy in 2008. District employees are entitled to time off based upon length of continuous service which is payable upon resignation, retirement or death. There is a 700-hour cap on PTO accrual, determined according to the employees' anniversary dates. After the annual transfer of PTO hours into Volunteer Employee Beneficiary Association (VEBA) or deferred comp, any hours over the 700-hour cap will be forfeited. At separation, if an employee is not eligible to retire, they may cash out their PTO bank at a schedule governed by years of service.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – (continued)

Fair value of financial instruments – The carrying amounts of current assets, including restricted cash and investments, and current liabilities approximate fair value due to the short-term maturity of those instruments. The fair value of the District’s investments and debt are estimated based on the quoted market prices for the same or similar issues.

Net assets – Net assets consist of:

- **Invested in capital assets, net of related debt** – This component of net assets consists of capital assets, net of accumulated depreciation, and unspent bond proceeds less outstanding balances of any bonds and other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- **Restricted** – This component consists of net assets on which constraints are placed as to their use. Constraints include those imposed by creditors (such as through debt covenants), contributors, or laws or regulation of other governments or constraints imposed by law through constitutional provisions or through enabling legislation.
- **Unrestricted** – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

Revenues and expenses – Operating revenues and expenses result from providing services and producing and delivering goods in connection with the District’s principal ongoing operations. Operating revenues are recognized when billed and expenses are recognized when incurred. In addition, the District recognizes unbilled revenue, revenues from services provided, but not yet billed. The principal operating revenues of the District are charges to customers for electric, water and wastewater service. Operating expenses for the District include the cost of sales and services, maintenance, administrative expenses, depreciation on capital assets and taxes. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The credit practices of the District require an evaluation of each new customer’s credit worthiness on a case-by-case basis. Based on policy, a deposit may be obtained from the customer. Concentrations of credit risk with respect to receivables for residential customers are limited due to the number of customers comprising the District’s customer base. Credit losses have been within management’s expectations. Similar to its evaluation of residential, commercial and industrial customers’ credit reviews, the District continually evaluates its wholesale power customers by reviewing credit ratings and financial credit worthiness of existing and new customers.

Capital contributions – Capital contributions are District-mandated customer connection charges used to fund construction of system properties necessary to extend service to a new customer.

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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES – (continued)

Significant risks and uncertainties – The District is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include, but are not limited to, weather and natural disaster related disruptions; collective bargaining labor disputes; fish and other Endangered Species Act issues; Environmental Protection Agency regulations; federal government regulations or orders; deregulation of the electric industry; and market risks inherent in buying and selling of power, a commodity with inelastic demand characteristics and minimal storage capability.

Reclassifications – Changes have been made to prior year account classifications as needed to conform to the current year presentation format. The primary change is in the classification of capital assets.

NOTE 2 – DEPOSITS AND INVESTMENTS

Cash and investments consist of the following at December 31:

	Investments	Cash and Cash Equivalents	Total 2010	Total 2009
Construction funds	\$ 3,846,789	\$ -	\$ 3,846,789	\$ 37,417,619
Special funds	14,307,309	-	14,307,309	13,792,107
Cash - general funds	-	12,639,161	12,639,161	15,358,699
Special deposits	-	400	400	400
Totals	<u>\$ 18,154,098</u>	<u>\$ 12,639,561</u>	<u>\$ 30,793,659</u>	<u>\$ 66,568,825</u>

Interest rate risk – The District’s investment policy limits investment maturities to less than five years from the date of purchase unless authorized by the General Manager and Finance Manager for a specific purpose. During 2010 and 2009 all investments were in the State Treasurer’s LGIP, which has a weighted average portfolio maturity of less than 90 days.

Credit risk – In accordance with the Revised Code of Washington, District bond resolutions and District internal investment policies, all investments are direct obligations of the U.S. Government, deposits in the LGIP, or deposits with financial institutions recognized as qualified public depositories of the State of Washington. The District’s cash deposits are covered by federal depository insurance or protected against loss by deposit with financial institutions recognized as qualified public depositories of the State of Washington. The District intends to hold deposits and securities until maturity.

Concentration of credit risk – District policies allow the entire portfolio to be invested in direct United States Government guaranteed obligations or in the LGIP. No other investment may exceed half of portfolio market value. The LGIP, a 2a7-like pool as defined by GASB Statement No. 31 and the Securities and Exchange Commission, invests in high quality, short term investments; all LGIP money market securities must be rated A-1 by Standard & Poor’s Corporation or P1 by Moody’s Investor Services, Inc. The LGIP weighted average maturity must not exceed 90 days and no single investment may exceed 762 days in maturity. Withdrawals in excess of \$10 million are available on a one day notice. The LGIP Annual Report is available on the Washington State Treasurer’s website.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 3 – CAPITAL ASSETS (UTILITY PLANT)

The following are changes in capital assets for the year ended December 31, 2010:

Description	Balance 1/1/2010	Additions	Retirements and Transfers	Balance 12/31/2010
Capital assets not being depreciated				
Organization	\$ 14,767	\$ -	\$ -	\$ 14,767
Franchises and consents	211,427	-	-	211,427
Land and land rights	1,302,615	107,301	-	1,409,916
Construction work in progress	48,299,053	60,313,793	37,965,171	70,647,675
	<u>49,827,862</u>	<u>60,421,094</u>	<u>37,965,171</u>	<u>72,283,785</u>
Capital assets being depreciated				
Electric plant				
Distribution plant	85,901,624	10,374,804	1,048,011	95,228,417
Transmission plant	30,537,952	26,400,888	112,229	56,826,611
Generating plant	24,309,457	1,814	-	24,311,271
Water and wastewater plant	17,484,642	1,059,366	-	18,544,008
General plant	9,189,613	380,261	5,660	9,564,214
	<u>167,423,288</u>	<u>38,217,133</u>	<u>1,165,900</u>	<u>204,474,521</u>
Total capital assets	217,251,150	98,638,227	39,131,071	276,758,306
Accumulated depreciation	<u>(49,704,427)</u>	<u>(5,622,372)</u>	<u>1,161,111</u>	<u>(54,165,688)</u>
Net capital assets	<u>\$ 167,546,723</u>	<u>\$ 93,015,855</u>	<u>\$ 37,969,960</u>	<u>\$ 222,592,618</u>

NOTE 4 – DEFERRED DEBITS

Deferred debits consist of the following:

	2010	2009
Prepaid power contract, net of current portion	\$ 18,885,756	\$ 20,066,112
Unamortized debt issuance expense	3,343,919	3,491,343
Preliminary investigation charges	366,118	452,224
	<u>\$ 22,595,793</u>	<u>\$ 24,009,679</u>

PUBLIC UTILITY DISTRICT NO. 1 OF KCLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 4 – DEFERRED DEBITS – (continued)

Prepaid power contract – The District entered into a 20-year Energy Purchase Agreement for the White Creek Wind I Facility, which became effective January 1, 2008. Under this Agreement, the District had rights to 26% of the output from the 205 MW facility and was obligated to pay the same percentage of the reimbursable operating expenses. In June 2008, the District completed a transaction with Lewis PUD to sell 10% of the 26% share of the White Creek Wind I project power output. In December 2008, the District also sold 3% of the remaining 16% share of the White Creek Wind I project power output to Benton PUD. The gain on the sale of White Creek power rights was \$23,678,404. The remaining portion of the project is amortized on a straight-line basis over the remaining term of the contract.

NOTE 5 – LONG-TERM DEBT

The following are changes in long-term debt for the year ended December 31, 2010:

	Balance 01/01/10	Additions	Payments/ Amortization	Balance 12/31/10	Due Within One Year
Electric revenue bonds	\$ 131,385,000	\$ -	\$ 2,580,000	\$ 128,805,000	\$ 3,180,000
Unamortized bond premium	2,800,208	-	198,214	2,601,994	-
W/WW revenue bonds	285,000	-	27,500	257,500	29,000
W/WW loans	<u>1,697,681</u>	<u>232,248</u>	<u>182,010</u>	<u>1,747,919</u>	<u>182,010</u>
Total Long-Term Debt	<u>\$ 136,167,889</u>	<u>\$ 232,248</u>	<u>\$ 2,987,724</u>	<u>\$ 133,412,413</u>	<u>\$ 3,391,010</u>

Substantially all electric revenues are pledged as security for the electric revenue bonds and substantially all water/wastewater revenues are pledged as security for the water/wastewater revenue bonds. Water/wastewater loans are secured by water/wastewater assets. Electric revenue bonds carry fixed interest rates of 1.470% to 7.038%. The water/wastewater revenue bonds have a 5.0% fixed rate. The loans from the Public Work Trust Fund (PWTF) carry fixed rates from 0.0% to 3.0% and the State Revolving Fund (SRF) loans have fixed rates of 0.0% to 1.0%. Electric revenue bonds mature through December 1, 2031, water and wastewater bonds mature through March 1, 2021 and the PWTF and SRF loans mature through October 1, 2028. There is \$14,307,309 in restricted assets of the District representing revenue bond reserve requirements for the various indentures. There are a number of other limitations and restrictions contained in the various bond indentures.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 5 – LONG-TERM DEBT – (continued)

Future maturities are as follows:

Electric Revenue Bonds			
Year(s)	Principal	Interest	Totals
2011	\$ 3,180,000	\$ 6,721,539	\$ 9,901,539
2012	3,240,000	6,656,985	9,896,985
2013	3,325,000	6,573,425	9,898,425
2014	3,430,000	6,467,724	9,897,724
2015	3,565,000	6,336,869	9,901,869
2016-20	28,235,000	28,472,554	56,707,554
2021-25	43,650,000	19,142,504	62,792,504
2026-30	33,600,000	7,905,088	41,505,088
2031	6,580,000	419,678	6,999,678
	<u>\$ 128,805,000</u>	<u>\$ 88,696,366</u>	<u>\$ 217,501,366</u>

Water/Wastewater Revenue Bonds			
Year(s)	Principal	Interest	Totals
2011	\$ 29,000	\$ 12,775	\$ 41,775
2012	31,000	11,325	42,325
2013	23,000	9,775	32,775
2014	23,000	8,625	31,625
2015	26,000	7,475	33,475
2016-20	121,500	16,375	137,875
2021	4,000	100	4,100
	<u>\$ 257,500</u>	<u>\$ 66,450</u>	<u>\$ 323,950</u>

Water/Wastewater P WTF & SRF Loans			
Year(s)	Principal	Interest	Totals
2011	\$ 182,010	\$ 4,110	\$ 186,120
2012	136,957	2,589	139,546
2013	136,957	2,421	139,378
2014	136,957	2,252	139,209
2015	136,957	2,083	139,040
2016-20	505,129	7,885	513,014
2021-25	416,322	3,807	420,129
2026-28	96,630	733	97,363
	<u>\$ 1,747,919</u>	<u>\$ 25,880</u>	<u>\$ 1,773,799</u>
Total	<u>\$ 130,810,419</u>	<u>\$ 88,788,696</u>	<u>\$ 219,599,115</u>

NOTE 5 – LONG-TERM DEBT – (continued)

The carrying amounts of the Bonds and PWTF and SRF loans approximate the fair value since such loans are exclusive and have no market.

At December 31, 2010, the District's 2001 Electric Revenue Bonds in the amount of \$24,955,000 were considered defeased. This refunded bond constitutes a contingent liability of the District only to the extent that cash and investments presently in the control of the refunding trustees are not sufficient to meet debt service requirements, and are therefore excluded from the financial statements because the likelihood of additional funding requirements is considered remote.

NOTE 6 – SHORT-TERM DEBT

The District issued a bond anticipation note on November 5, 2007 in the amount of \$47,000,000 to finance the District's 26% of the power output from the White Creek Wind I project for the term of 20 years per the agreement. This note was in two sections, a \$42,000,000 and a \$5,000,000 section. Proceeds from the sale of 13% of the District's 26% share of power output from White Creek Wind project was used to pay off the first \$42,000,000 section of the bond anticipation note, and the balance has remained \$5,000,000 at December 31, 2010 and 2009.

NOTE 7 – RETIREMENT BENEFITS

1. Pension plan

Substantially all of the District's full-time and qualifying part-time employees participate in one of the 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 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 – PO Box 48380 – Olympia WA 98504-8380. The following disclosures are made pursuant to GASB Statement 27, Accounting for Pensions by State and Local Government Employers.

Public Employees' Retirement System (PERS) Plans 1, 2 and 3

Plan description – 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 defined benefit plan with a defined contribution component.

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, community and technical colleges, college and university employees not participating in national higher education retirement programs; judges of district and municipal courts; and employees of local government.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 7 – RETIREMENT BENEFITS – (continued)

PERS participants who joined the system by September 30, 1977 are Plan 1 members. Those who joined on or after October 1, 1977 and 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 irrevocable 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 in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to PERS Plan 2.

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 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement at any age after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual benefit 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 24 eligible consecutive compensation months. 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 members are vested after the completion of five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of two 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. Plan 2 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 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, 2007, 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 age 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.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 7 – RETIREMENT BENEFITS – (continued)

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.

There are 2,326 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of December 31, 2010:

Retirees and beneficiaries receiving benefits	\$ 76,899
Terminated plan members entitled to but not yet receiving benefits	28,860
Active plan members vested	105,212
Active plan members non-vested	<u>56,456</u>
Total	<u>\$ 267,427</u>

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 PERS 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 benefits portion for 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, 2010, were as follows:

	<u>PERS Plan 1</u>	<u>PERS Plan 2</u>	<u>PERS Plan 3</u>
Employer*	5.31%**	5.31%**	5.31%**
Employee	6.00%***	3.9%***	****

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

** The employer rate for state elected officials is 12.39% for Plan 1, 8.31% for Plan 2 and Plan 3.

*** The employee rate for state elected officials is 7.50% for Plan 1, and 5.45% for Plan 2.

**** Variable from 5% to 15% maximum based on rate selected by the PERS3 member.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 7 – RETIREMENT BENEFITS – (continued)

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>PERS Plan 1</u>	<u>PERS Plan 2</u>	<u>PERS Plan 3</u>
2010	\$ 8,678	\$ 537,268	\$ 34,399
2009	\$ 20,312	\$ 589,365	\$ 33,197
2008	\$ 63,430	\$ 533,370	\$ 31,087

2. Post Employment Benefits Plan Other than Pensions

Plan description – In addition to pension benefits, the District provides post employment health care benefits. District members are eligible for retiree medical benefits after becoming eligible for service retirement pension benefits under Plan 2 of the PERS (age 65 with 5 years of service; age 55 with 20 years of service). Currently former members who are entitled to a deferred vested pension benefit are not eligible to receive medical benefits after pension benefit commencement. Survivors of members who die are not eligible for medical benefits.

Funding policy – The funding policy is based upon the pay-as-you-go financing requirements.

Annual OPEB cost and net OPEB obligation – The District’s annual other postemployment benefit (OPEB) cost is based upon the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities over a period of thirty years as of January 1, 2008.

The District’s annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2010 and 2009 were as follows:

<u>Fiscal Year</u> <u>Ended</u>	<u>Annual OPEB</u> <u>Cost</u>	<u>Percentage of</u> <u>OPEB Cost</u> <u>Contributed</u>	<u>Net OPEB</u> <u>Obligation</u>
12/31/2010	\$ 413,230	43.30%	\$ 723,886
12/31/2009	\$ 410,566	39.58%	\$ 489,595
12/31/2008	\$ 407,386	40.71%	\$ 241,532

Funding Status and Funding Progress – As of December 31, 2010, the most recent valuation date, the plan was 0% funded. The accrued liability for benefits was \$4.8 million, and the actuarial value of assets was \$0, resulting in a UAAL of \$4.8 million.

PUBLIC UTILITY DISTRICT NO. 1 OF KCLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 7 – RETIREMENT BENEFITS – (continued)

The following table presents a schedule of funding progress for the District’s OPEB Plan:

Valuation Date	Actuarial Value of Assets	Accrual Accrued Liability	Unfunded Actuarial Accrued Liabilities (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
1/1/2008	\$ -	\$ 4,784,699	\$ 4,784,699	0%	N/A	N/A

Actuarial valuations 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 required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

NOTE 8 – SEGMENT INFORMATION – ENTERPRISE FUNDS

The District operates an electric, eight water and five wastewater utilities which are primarily financed by user charges. The key financial data for the years ended December 31, 2010 and 2009 is as follows:

Condensed balance sheets:

	Electric System	Water- Wastewater Systems	Total 2010	Total 2009
Assets				
Current, restricted and other assets	\$ 62,006,905	\$ 3,606,724	\$ 65,613,629	\$ 103,677,107
Capital assets	206,215,051	16,377,567	222,592,618	167,546,723
Total assets	\$ 268,221,956	\$ 19,984,291	\$ 288,206,247	\$ 271,223,830
Liabilities				
Current liabilities	\$ 16,871,106	\$ 1,783,609	\$ 18,654,715	\$ 20,452,841
Noncurrent liabilities	128,430,917	1,861,140	130,292,057	133,779,264
Total liabilities	145,302,023	3,644,749	148,946,772	154,232,105
Net assets				
Invested in capital assets, net of related debt	77,062,744	14,308,169	91,370,913	72,287,796
Restricted	13,498,018	230,005	13,728,023	13,403,331
Unrestricted	32,359,171	1,801,368	34,160,539	31,300,598
Total net assets	122,919,933	16,339,542	139,259,475	116,991,725
Total liabilities and net assets	\$ 268,221,956	\$ 19,984,291	\$ 288,206,247	\$ 271,223,830

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 8 – SEGMENT INFORMATION – ENTERPRISE FUNDS – (continued)

Condensed statements of revenues, expenses and changes in net assets:

	Electric System	Water- Wastewater Systems	Total 2010	Total 2009
Operating revenues	\$ 39,148,172	\$ 1,351,946	\$ 40,500,118	\$ 42,518,940
Operating expenses	30,031,252	813,863	30,845,115	31,106,488
Depreciation	3,952,927	503,485	4,456,412	4,072,044
Operating income	5,163,993	34,598	5,198,591	7,340,408
Non-operating revenues (expenses)				
Interest income	153,860	16,577	170,437	483,823
Interest expense	(4,906,035)	(22,199)	(4,928,234)	(4,546,492)
Other non-operating revenue (expense), net	1,238,509	21,137	1,259,646	1,369,031
Capital contributions and grants	20,504,483	62,827	20,567,310	13,597,947
Change in net assets	22,154,810	112,940	22,267,750	18,244,717
Net assets, beginning of year	-	-	116,991,725	98,747,008
Net assets, end of year	\$ 22,154,810	\$ 112,940	\$ 139,259,475	\$ 116,991,725

NOTE 9 – RISK MANAGEMENT AND SELF INSURANCE

Unemployment insurance – The District maintains insurance against most normal hazards, except for unemployment insurance, where the District has elected to become self-insured for all losses. The District reimburses the State Employment Security Department for actual costs upon receipt of any claim. The District does not estimate any future liability as the amount is not significant.

Public Utility Risk Management Services – The District, along with seventeen other public utility districts and one joint operating agency, is a member of the Public Utility Risk Management Services self-insurance fund. The program provides members with various liability, property and health insurance coverage in three separate pools.

The District has not accrued a liability for any outstanding claims of the self-insured pools, including incurred-but-not-reported health and welfare claims, as the amount cannot be reasonably estimated. Management believes the claims, for those that are successful, will not have a significant impact on the financial position of the District.

The District is a participant in the liability pool, which maintains a base self-insured retention level of \$1,000,000, funded reserves ranging from \$1,500,000 to \$2,000,000, and individual member deductibles of \$250. The liability pool provides the District with shared excess coverage of \$60,000,000 general liability, \$10,000,000 professional liability, and \$10,000,000 per occurrence Directors and Officers liability.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 9 – RISK MANAGEMENT AND SELF INSURANCE – (continued)

The District is also a participant in the property pool, which maintains a self-insured retention level of \$250,000, funded reserves ranging from \$500,000 to \$750,000, and varying deductibles of \$250 on most property and \$75,000 on the H. W. Hill Landfill Gas project. The property pool provides the District with \$175,000,000 shared excess coverage, attaching at the self-insured retention level for all property risks excepting flood and earthquake, which attach at 2% of total insured value. Any gap between the self-insured level and excess insurance is funded half by the property pool and half by the affected member.

The District also participates in the health and welfare pool. Participating members are billed each month for shared costs (administration costs to operate the pool, mail order prescription plan costs, and stop loss carrier costs), claims by the members covered employees and dependents, and any shared claims for members who exceeded stop loss limits.

NOTE 10 – JOINT VENTURES

Conservation and Renewable Energy System (CARES) – The District, along with seven other public utility districts, is a member of CARES, a municipal corporation and joint operating agency of the State of Washington. CARES was formed pursuant to RCW Chapter 43.52. The purpose of CARES is to develop and acquire conservation, renewable and high efficiency resources consistent with the Northwest Conservation and Electric Power Plan. CARES issued Conservation Project Revenue Bonds which are tax-exempt and unconditionally guaranteed by the BPA. The District has not contributed any money to CARES for several years. The District has no equity interest or liability for CARES operations.

McNary North Fishway Hydroelectric Project – On August 14, 1995, the District and Northern Wasco County PUD entered into an Ownership Agreement to jointly construct and operate the McNary North Fishway Hydroelectric Project. The project was completed in September 1997 and is generating approximately ten megawatts (10 MW) of electricity. Both the District and Northern Wasco County PUD share equally in the output, as well as the construction and operation costs of the Project. In 2010 and 2009 the District contributed \$450,000.

Last Mile Electrical Cooperative (LMEC) – The District, along with seven other public utility districts and two other organizations, is a member of LMEC, a non-profit cooperative. LMEC was formed pursuant to RCW Chapter 24.06. The purpose of LMEC is to develop wind and other renewable energy projects. At this time, LMEC has not issued any debt and is solely funded by its members. The District has no equity interest or liability for the LMEC operations at this time.

PUBLIC UTILITY DISTRICT NO. 1 OF KLICKITAT COUNTY – MCAG No. 1785
NOTES TO COMBINED FINANCIAL STATEMENTS

NOTE 10 – JOINT VENTURES – (continued)

White Creek Public, LLC & White Creek Project, LLC – The District, along with Cowlitz PUD, formed White Creek Public, LLC to participate in White Creek Project, LLC which also includes as members Tanner Electric Co-op and Lakeview Light & Power. Early development of the project was done by the utilities involved, but prior to the end of 2007 the project was sold to Prudential and Lehman Brothers. Energy purchase agreements were signed by the utilities for 20 years of power that began commercial operation on November 21, 2007 (See Note 4). The percentage owned by each utility was determined based upon their contribution made during the original development stage. Phases 1 and 2 of White Creek Wind I have a total of 89 2.3 MW wind turbines for an anticipated output of 205 MW. Both phases were in production as of November 21, 2007. In 2010 and 2009, the District's investment in the project of \$(1,863) consisted of a share of the remaining assets. These amounts have been shown on the balance sheet as other investments and transmission deposits.

NOTE 11 – CONTINGENCIES

Lawsuits – The District is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, it is the opinion of District management that resolution of these matters will not have a material adverse effect on the financial condition of the District.

Construction financing – On April 17, 2001 the District entered into a thirty (30) year agreement with the Goldendale Energy, Inc. in order to provide for the transmission of the electric energy to be produced at Goldendale Energy Inc. generating facility from the E.E. Clouse Substation to Bonneville's Harvalum Substation. The generating facility was sold through bankruptcy auction in February 2007 to Puget Sound Energy. The District established a new letter of credit for the transmission line service, which the District built and operates for the generation facility. The letter of credit covers the net present value of the remaining contract amount including the debt outstanding.

The District established a new letter of credit on August 16, 2006 for the White Creek transmission line service, which the District built and operates at a cost of \$17.7 million, for the generation facility. The letter of credit covers the net present value of the remaining 20 year contract amount including the debt outstanding.

Grants – Grants received by the District are subject to audit by the granting agency and may result in certain costs being disallowed and required to be returned. Management believes it has complied with grant guidelines and the likelihood of disallowed costs is remote.

NOTE 12 – POWER CONTRACTS

The District purchases power from the BPA under contracts which expire on September 30, 2011. The District's contract is a partial requirements contract that provides the District the option to provide a portion of customer load with existing generation from the McNary Hydroelectric facility, approximately 5 MW. The balance of the District's load requirement is supplied by BPA at the public preference customer rate.

The White Creek Wind I facility energy purchase agreement for 13% of the 205 MW project is currently sold under contract to other utilities (See Note 4).

NOTE 13 – GENERATION ASSETS

H. W. Hill Landfill Gas project is rated a 10.5 MW plant that takes methane gas from the regional landfill and produces electricity from five 2.1 MW reciprocating combustion engines. 2.0 MW's of the output from this project is sold to a public utility and the balance sold on the spot market.

McNary Dam Hydroelectric project is a 10 MW plant that the District shares joint ownership with Northern Wasco Peoples Utility District in The Dalles, Oregon. The facility is located on the north shore fish bypass area of McNary Dam and received a 50-year license on September 30, 1991. Of the 5 MW's the District receives, 4.5 MW's are declared to load.

NOTE 14 – UNION CONTRACTS

The District has a contract with the International Brotherhood of Electrical Workers which covers the electrical line workers employed by the District. The District signed a new contract with the union in early April 2008. The contract is for three years starting April 1, 2008 and expiring on March 31, 2011. A new contract was executed beginning June 1, 2011.