Report of Independent Auditors
and Financial Statements for

# McMinnville Water and Light Department

(A Component Unit of the City of McMinnville, Oregon)

June 30, 2012 and 2011

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

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## Commissioners as of June 30, 2012

| Name | Term Expires |
|---|---|
| Thomas Tankersley, Chairperson | December 31, 2013 |
| Rick Olson, Mayor | December 31, 2012 |
| Edward Gormley | December 31, 2012 |
| Patrick Fuchs | December 31, 2014 |
| Mike Keyes | December 31, 2015 |

### Administrative Staff

Kem M. Carr, General Manager
Mark R. Carlton, CPA, CGMA, Director of Finance
Mary Ann Nolan, Clerk

### Department Address

McMinnville Water and Light Department
855 NE Marsh Lane
McMinnville, Oregon 97128

MOSS-ADAMS LLP
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# REPORT OF INDEPENDENT AUDITORS

To the Board of Commissioners
McMinnville Water and Light Department

We have audited the accompanying combined balance sheets of McMinnville Water and Light Department (the Department), a component unit of the City of McMinnville, Oregon, as of June 30, 2012 and 2011 and the related combined statements of revenues, expenses, and changes in net assets and combined statements of cash flows for the years then ended. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 Department'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 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 the Department as of June 30, 2012 and 2011 and the changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 8 and 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.

Julie DeSimone

Julie Desimone, Partner for Moss Adams LLP
November 15, 2012

McMinnville Water and Light Department (the Department or MWL) was established in 1889 as a municipal utility responsible for providing water and electricity for the City of McMinnville. The Department is governed by the City Charter and has a five-member Commission. Commissioners are appointed by the Mayor and approved by the City Council. The Mayor serves in an ex-officio capacity.

**Financial highlights**

- Took delivery of two additional power transformers for East McMinnville and Walnut City substations
- Water rates increased commencing May 1, 2011
- Electric rates increased for industrial customers on October 1, 2011. All other electric customer rates increased on September 1, 2011
- Completed Water Master Plan update
- Replaced Windishar circuit switchers and relays
- Replaced Booth Bend power transformer, circuit switcher, relays, and getaway cables
- Continued work on water main replacements
- Rebuilt and relocated overhead power lines at 99W & McDonald Lane, undergrounding some of the overhead facilities

**Overview of financial statements**

The Department obtains 96% of its power supply from the Bonneville Power Administration (BPA) and purchases 4% from other suppliers. Fiscal year 2012 saw the continuance of BPA's Energy Conservation Agreement program. The conservation efforts for the last fiscal year recorded over 150 residential and 12 commercial energy conservation projects. This effort netted the utility over 0.1 average megawatt of conservation.

FY 2011 included water rate increases commencing May 1, 2011, in order to rebuild cash reserves and amortize interdepartmental loans. A planned water rate increase on May 1, 2012, was postponed in order for the Commission to further assess the impacts of possible outside water sales and system development charges (SDCs).

**Analysis of the statements of revenues, expenses, and changes in fund net assets**

The Statements of Revenues, Expenses, and Changes in Net Assets show the financial results of activities for any given fiscal year. These statements measure the success of the Department's operations during the last three years and can be used to determine whether all of its costs have been successfully recovered.

**Condensed statements of revenues, expenses and changes in fund net assets ($000s)**

| | FY 2012 | FY 2011 | Increase (Decrease) | Percent Change | FY 2010 | Increase (Decrease) | Percent Change |
|---|---|---|---|---|---|---|---|
| Operating revenues | $ 41,123 | $ 36,534 | $ 4,589 | 13% | $ 35,302 | $ 1,232 | 3% |
| Operating expenses | 40,072 | 37,107 | 2,965 | 8% | 36,012 | 1,095 | 3% |
| Net operating revenue (loss) | 1,051 | (573) | 1,624 | 283% | (710) | 137 | -19% |
| Other revenues | 3,688 | 3,568 | 120 | 3% | 1,800 | 1,768 | 98% |
| Other expenses | (555) | (695) | 140 | -20% | (50) | (645) | 1290% |
| Contributions | 643 | 522 | 121 | 23% | 766 | (244) | -32% |
| Total other | 3,776 | 3,395 | 381 | 11% | 2,516 | 879 | 35% |
| Changes in fund net assets | $ 4,827 | $ 2,822 | $ 2,005 | 71% | $ 1,806 | $ 1,016 | 56% |

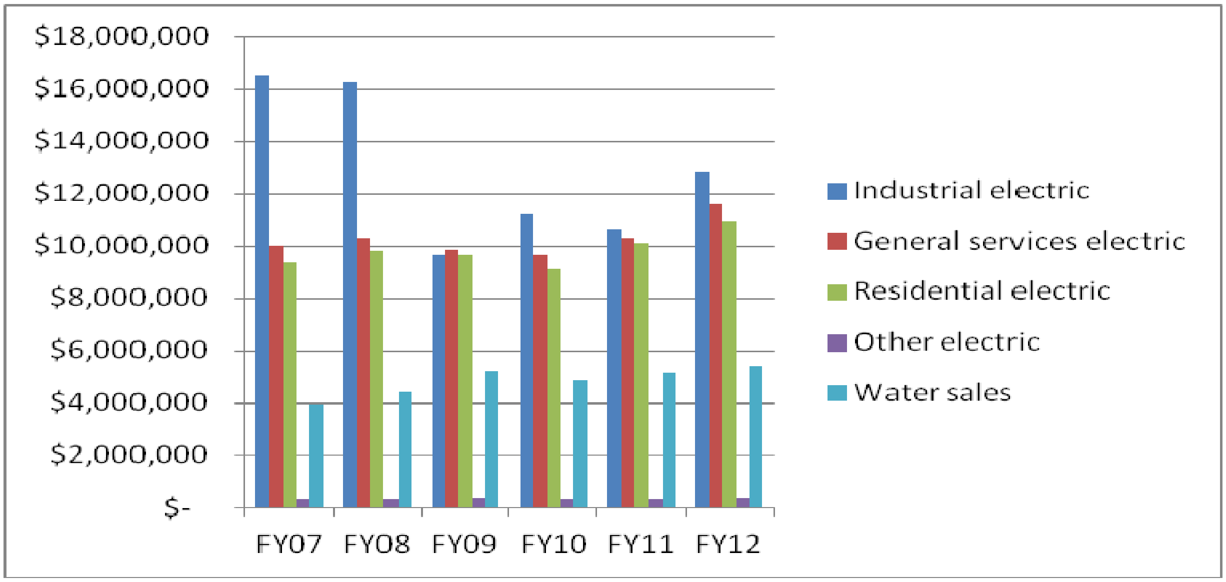
Fiscal Year 2012

Net operating revenues increased overall by 283%. This was largely due to increased revenue from electricity by 14% and increased revenue from the water department by 4.2%, both largely due to rate increases. Consumption of electricity (kWh) and water (Cu. Ft.) increased / (decreased) by 0.7% and (2%), respectively, with operating expenses coming in 8% higher than the prior year for both water and electricity. Economic and mild weather conditions, along with conservation continue to be factors with flat or decreasing consumption. Total other net revenue increased by 11% for the fiscal year largely due to increased net timber revenue, decreased net conservation expenses, and higher contributions in aid of construction.

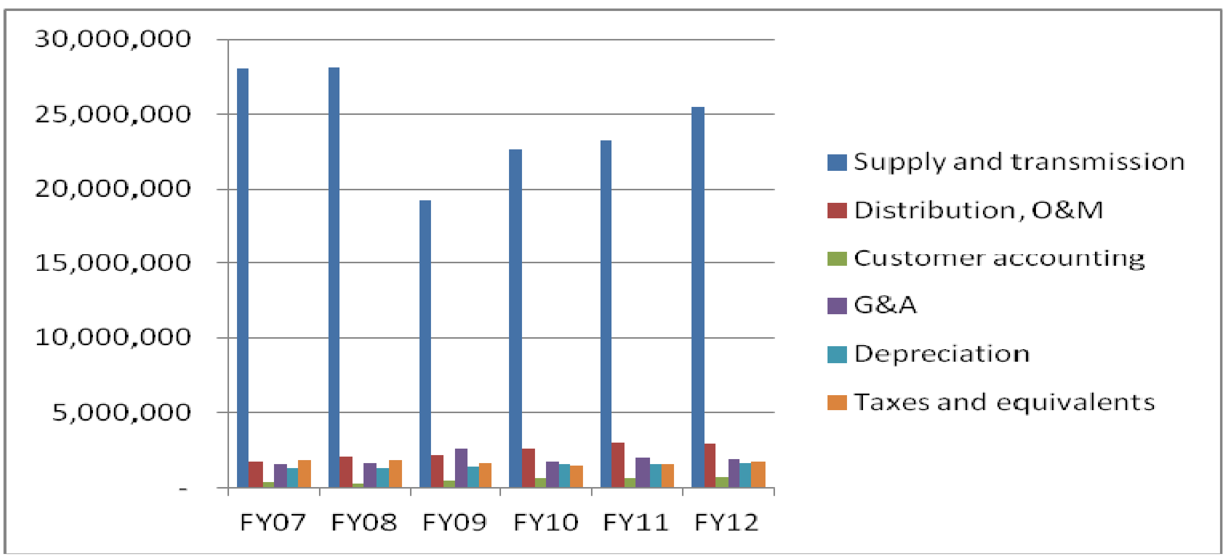
Fiscal Year 2011

Net operating revenues increased overall by 19%. This was largely due to increased revenue from electricity by 3.2% and increased revenue from the water department by 5%. Actual consumption of electricity (kWh) and water (Cu. Ft.) decreased by (1.7%) and (3.5%), from the prior year, with operating expenses 3% higher than 2010. Despite the fact that revenue has not met expectations, due to the economy and weather conditions, the net operating loss from 2010 to 2011 was trimmed by $137,000. Other revenues increased by 98% largely due to increased timber revenues and BPA conservation reimbursements. Other expenses increased due to losses from retirements/abandonments of fixed assets.

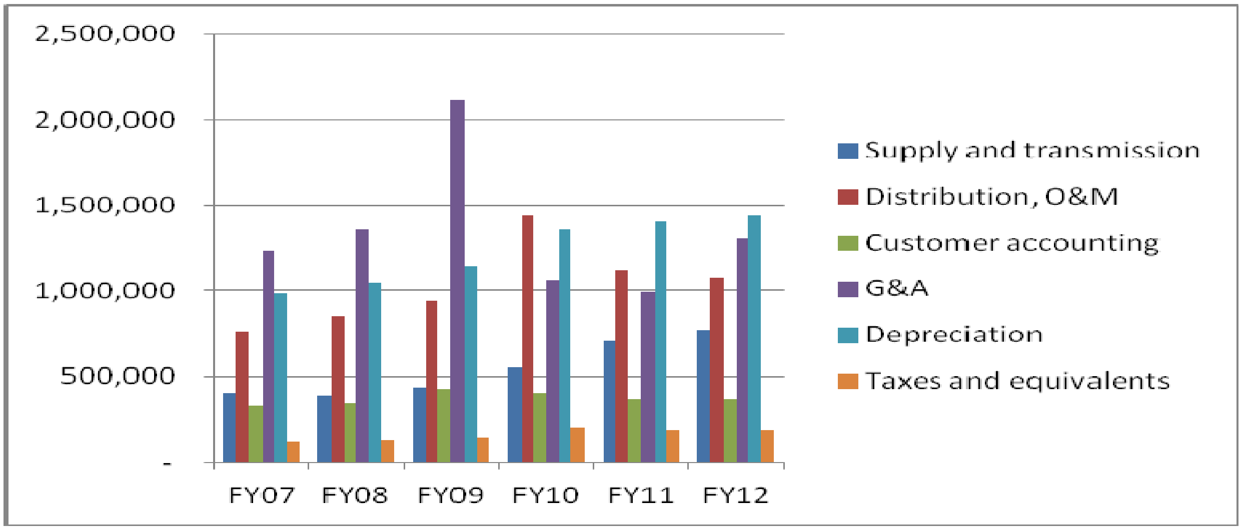
**Operating revenues**




**Operating expenses - Electric**



**Operating expenses - Water**




The Balance Sheets include all of the Department's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations of the Department (liabilities). They also provide the basis for assessing the Department's capital structure, liquidity, and financial flexibility.

**Condensed balance sheets ($000s)**

| | FY 2012 | FY 2011 | Increase (Decrease) | Percent Change | FY 2010 | Increase (Decrease) | Percent Change |
|---|---|---|---|---|---|---|---|
| Assets | | | | | | | |
| Net utility plant | $ 116,015 | $ 114,665 | $ 1,350 | 1% | $ 113,931 | $ 734 | 1% |
| Current assets | 26,129 | 22,226 | 3,903 | 18% | 22,058 | 168 | 1% |
| Other assets | 3,970 | 3,786 | 184 | 5% | 3,598 | 188 | 5% |
| Total assets | $ 146,114 | $ 140,677 | $ 5,437 | 4% | $ 139,587 | $ 1,090 | 1% |
| Liabilities | | | | | | | |
| Current liabilities | 4,387 | 3,933 | 454 | 12% | 5,642 | (1,709) | -30% |
| Long-term liabilities | 1,372 | 1,216 | 156 | 13% | 1,239 | (23) | -2% |
| Total liabilities | 5,759 | 5,149 | 610 | 12% | 6,881 | (1,732) | -25% |
| Net assets | | | | | | | |
| Investment in capital assets, net of related debt | 106,683 | 103,522 | 3,161 | 3% | 103,852 | (330) | 0% |
| Unrestricted | 33,672 | 32,006 | 1,666 | 5% | 28,853 | 3,153 | 11% |
| Total net assets | $ 140,355 | $ 135,528 | $ 4,827 | 4% | $ 132,706 | $ 2,822 | 2% |

Fiscal Year 2012

The Department's total assets increased by 4% during FY 2012. This can be traced largely to an increase in net utility plant and cash from operations (see table on page 7).

Fiscal Year 2011

The Department's total assets increased by 1% during FY 2011. Current assets and utility plant also increased by 1%. This is the result of completing several large construction projects. Liabilities decreased by 25%, largely due to a reduction of accounts payable from the winding down of several large construction projects, as already mentioned.

**Condensed statement of cash flows ($000s)**

| | FY 2012 | FY 2011 | Increase (Decrease) | Percent Change | FY 2010 | Increase (Decrease) | Percent Change |
|---|---|---|---|---|---|---|---|
| Beginning cash and cash equivalents | $ 17,267 | $ 17,257 | $ 10 | 0% | $ 33,339 | $ (16,082) | -48% |
| From | | | | | | | |
| Operating activities | 8,250 | 3,632 | 4,618 | 127% | 2,405 | 1,227 | 51% |
| Capital and related financing activities | (4,545) | (3,931) | (614) | 16% | (21,032) | 17,101 | -81% |
| Investing activities | 269 | 309 | (40) | -13% | 2,545 | (2,236) | -88% |
| Ending cash and cash equivalents | $ 21,241 | $ 17,267 | $ 3,974 | 23% | $ 17,257 | $ 10 | 0% |

Fiscal Year 2012

As with FY 2011, cash from operating activities increased overall largely due to increases in net timber revenue, receipts from customers, and other receipts. The receipts from customers increased due to rate increases for both electric and water customers. Cash flows used in capital financing activities arose primarily from construction projects and renewable energy certificate additions.

Fiscal Year 2011

Cash from operating activities increased overall largely due to increases in net timber revenue, receipts from customers, and other receipts. Cash flows used in capital financing activities arose primarily from the winding down of several significant construction projects and a reduction of deferred conservation expenditures. Cash from investing decreased primarily from the maturity of a certificate of deposit in the prior year.

**Budget highlights**

| | In $000s | | | |
|---|---|---|---|---|
| | Budget FY 2012 | Actual FY 2012 | Dollar Change | Percent Change |
| Operating revenues | $ 43,530 | $ 41,123 | $ (2,407) | -6% |
| Operating expenses | 41,887 | 40,072 | (1,815) | -4% |
| Net operating revenue | 1,643 | 1,051 | (592) | -36% |
| Other revenues (expenses) | 1,804 | 3,133 | 1,329 | 74% |
| Contributions | 609 | 643 | 34 | 6% |
| Changes in fund net assets | $ 4,056 | $ 4,827 | $ 771 | 19% |

The FY 2012 budget included a water rate increase during the last two months of the year, while electric rates rose also, including increases for industrial customers, effective October 1st. Water and electricity sales came in over and under budget by 1% and (6%), respectively. These were largely attributable to the economic and weather conditions, as well as reduced consumption due to conservation measures. Expenses were lower than budgeted, thus lessening the impact of lower revenues. Even with the continued slow economy, contributions in aid were 6% higher than expected.

**Capital assets and debt administration**

The Department continues to develop its infrastructure to meet the water and power needs of its customers. The FY 2012 saw a net increase in capital assets, after depreciation, of $1,349,859. A net increase of $733,500 was reported for the FY 2011. For additional information on capital assets, refer to Note 4 of the Notes to combined financial statements.

The Department had interdepartmental loans during the fiscal years ended June 30, 2012 and 2011 amounting to $9,331,455 and $11,118,974, respectively, for the financing of the Norm Scott Water Treatment Plant. These loans were eliminated in the total combined balance column for financial statement purposes.

**Economic factors and outlook for next year**

The cash position of the Water and Light Departments should improve during the 2013 fiscal year with planned rate increases taking hold. The economy and weather will continue to be important factors for sales of water and electricity that will ultimately impact cash reserves.

**Requests for information**

This financial report is designed to provide a general overview of the Department's finances for all those with an interest therein. Questions concerning any of the information provided in this report, or requests for additional financial information, should be addressed to the Director of Finance, McMinnville Water and Light Department, 855 NE Marsh Lane, McMinnville, OR 97128.

| | Water | | Light | | Total | |
|---|---|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 |
| **ASSETS** | | | | | | |
| Utility plant, net | $ 80,586,946 | $ 81,262,682 | $ 35,427,614 | $ 33,402,019 | $ 116,014,560 | $ 114,664,701 |
| Current assets | | | | | | |
| Cash and cash equivalents | 5,998,613 | 4,578,158 | 14,966,397 | 12,599,595 | 20,965,010 | 17,177,753 |
| Designated cash | - | - | 276,431 | 89,398 | 276,431 | 89,398 |
| Accounts receivable, net of allowance | 518,876 | 487,072 | 3,213,286 | 2,643,265 | 3,732,162 | 3,130,337 |
| Due from the City of McMinnville | - | - | - | 387 | - | 387 |
| Current portion of note receivable and other | - | - | 2,064,043 | 2,838,397 | 240,064 | 1,050,878 |
| Inventories | 127,440 | 127,816 | 620,840 | 555,473 | 748,280 | 683,289 |
| Other current assets | 156,456 | 81,336 | 11,041 | 13,157 | 167,497 | 94,493 |
| Total current assets | 6,801,385 | 5,274,382 | 21,152,038 | 18,739,672 | 26,129,444 | 22,226,535 |
| Other assets | | | | | | |
| Note receivable, less current portion | - | - | 7,889,327 | 9,820,617 | 381,851 | 489,162 |
| Renewable energy certificates | - | - | 887,436 | 471,116 | 887,436 | 471,116 |
| Deferred conservation charges | - | - | 2,700,637 | 2,825,282 | 2,700,637 | 2,825,282 |
| Total other assets | - | - | 11,477,400 | 13,117,015 | 3,969,924 | 3,785,560 |
| TOTAL ASSETS | $ 87,388,331 | $ 86,537,064 | $ 68,057,052 | $ 65,258,706 | $ 146,113,928 | $ 140,676,796 |
| **LIABILITIES AND NET ASSETS** | | | | | | |
| Net assets | | | | | | |
| Investment in capital assets, net of related debt | $ 71,255,491 | $ 70,119,612 | $ 35,427,614 | $ 33,402,019 | $ 106,683,105 | $ 103,521,631 |
| Unrestricted | 5,246,999 | 3,674,506 | 28,424,842 | 28,331,795 | 33,671,841 | 32,006,301 |
| Total net assets | 76,502,490 | 73,794,118 | 63,852,456 | 61,733,814 | 140,354,946 | 135,527,932 |
| Current liabilities | | | | | | |
| Accounts payable | 25,112 | 124,946 | 2,123,848 | 1,687,545 | 2,148,960 | 1,812,491 |
| Accrued payroll | 112,008 | 118,467 | 133,277 | 146,266 | 245,285 | 264,733 |
| Other liabilities | - | 2,703 | 260,403 | 84,606 | 260,403 | 87,309 |
| Compensated absences | 184,936 | 194,016 | 239,883 | 233,036 | 424,819 | 427,052 |
| Due to City of McMinnville | 603,352 | 596,844 | 97,924 | 91,339 | 701,276 | 688,183 |
| Advances and deposits | 50,000 | 50,000 | 555,851 | 579,240 | 605,851 | 629,240 |
| Current portion of long-term notes payable | 1,823,979 | 1,811,615 | - | - | - | 24,096 |
| Total current liabilities | 2,799,387 | 2,898,591 | 3,411,186 | 2,822,032 | 4,386,594 | 3,933,104 |
| Long-term liabilities | | | | | | |
| Notes payable, less current portion | 7,507,476 | 9,331,455 | - | - | - | - |
| Other post-employment benefits liability | 578,978 | 512,900 | 793,410 | 702,860 | 1,372,388 | 1,215,760 |
| Total long-term liabilities | 8,086,454 | 9,844,355 | 793,410 | 702,860 | 1,372,388 | 1,215,760 |
| TOTAL NET ASSETS AND LIABILITIES | $ 87,388,331 | $ 86,537,064 | $ 68,057,052 | $ 65,258,706 | $ 146,113,928 | $ 140,676,796 |

*Intercompany notes receivable and payable are eliminated in the total column.*

# McMINNVILLE WATER AND LIGHT DEPARTMENT
## COMBINED STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

| | Water | | Light | | Total | |
|---|---|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 |
| OPERATING REVENUES | | | | | | |
| Sales of electricity | | | | | | |
| Residential | $ - | $ - | $ 10,950,341 | $ 10,101,585 | $ 10,950,341 | $ 10,101,585 |
| General service | - | - | 11,587,317 | 10,323,274 | 11,587,317 | 10,323,274 |
| Industrial | - | - | 12,844,081 | 10,637,530 | 12,844,081 | 10,637,530 |
| Rental light | - | - | 145,891 | 170,809 | 145,891 | 170,809 |
| Street light | - | - | 185,416 | 110,005 | 185,416 | 110,005 |
| Cable TV | - | - | 34,715 | 35,089 | 34,715 | 35,089 |
| Sales of water | 5,374,759 | 5,156,093 | - | - | 5,374,759 | 5,156,093 |
| Total operating revenues | 5,374,759 | 5,156,093 | 35,747,761 | 31,378,292 | 41,122,520 | 36,534,385 |
| OPERATING EXPENSES | | | | | | |
| Supply and transmission | 771,589 | 703,914 | 25,517,295 | 23,286,213 | 26,288,884 | 23,990,127 |
| Distribution, operation, and maintenance | 1,075,517 | 1,120,098 | 2,950,824 | 3,012,857 | 4,026,341 | 4,132,955 |
| Customer accounting and meter reading | 367,172 | 363,217 | 690,305 | 605,911 | 1,057,477 | 969,128 |
| General and administrative | 1,307,290 | 988,724 | 1,909,752 | 1,969,736 | 3,217,042 | 2,958,460 |
| Depreciation | 1,442,641 | 1,407,783 | 1,680,321 | 1,541,077 | 3,122,962 | 2,948,860 |
| Conservation | - | 1,000 | 394,651 | 334,142 | 394,651 | 335,142 |
| Taxes and tax equivalents | 189,896 | 187,407 | 1,774,837 | 1,584,873 | 1,964,733 | 1,772,280 |
| Total operating expenses | 5,154,105 | 4,772,143 | 34,917,985 | 32,334,809 | 40,072,090 | 37,106,952 |
| Operating income (loss) | 220,654 | 383,950 | 829,776 | (956,517) | 1,050,430 | (572,567) |
| NON-OPERATING INCOME (EXPENSE) | | | | | | |
| Timber sales, net of related expenses | 2,605,898 | 1,355,475 | - | - | 2,605,898 | 1,355,475 |
| Interest | 49,087 | 37,669 | 373,380 | 387,781 | 422,467 | 425,450 |
| Other, net | (4,270) | 39,679 | 664,463 | 1,747,826 | 660,193 | 1,787,505 |
| Loss on asset dispositions | (24,763) | (184,868) | (325,527) | (354,618) | (350,290) | (539,486) |
| Interest expense | (204,255) | (155,508) | - | (195) | (204,255) | (155,703) |
| Total non-operating income | 2,421,697 | 1,092,447 | 712,316 | 1,780,794 | 3,134,013 | 2,873,241 |
| Income before contributed capital | 2,642,351 | 1,476,397 | 1,542,092 | 824,277 | 4,184,443 | 2,300,674 |
| Hookup fees and contributed utility systems | 66,021 | 126,048 | 576,550 | 395,598 | 642,571 | 521,646 |
| Change in net assets | 2,708,372 | 1,602,445 | 2,118,642 | 1,219,875 | 4,827,014 | 2,822,320 |
| NET ASSETS, beginning of year | 73,794,118 | 72,191,673 | 61,733,814 | 60,513,939 | 135,527,932 | 132,705,612 |
| NET ASSETS, end of year | $ 76,502,490 | $ 73,794,118 | $ 63,852,456 | $ 61,733,814 | $ 140,354,946 | $ 135,527,932 |



See accompanying notes.

| | Water | | Light | | Total | |
|---|---|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | | | | | |
| Receipts from customers | $ 5,342,955 | $ 5,114,091 | $ 35,177,740 | $ 31,072,709 | $ 40,520,695 | $ 36,186,800 |
| Receipts from timber sales | 2,605,898 | 1,355,475 | - | - | 2,605,898 | 1,355,475 |
| Other receipts | (78,885) | (41,281) | 664,463 | 1,747,826 | 585,578 | 1,706,545 |
| Power purchases | - | - | (25,517,295) | (23,286,213) | (25,517,295) | (23,286,213) |
| Payments to suppliers | (141,309) | (1,565,321) | 8,752 | (1,553,454) | (132,557) | (3,118,775) |
| Conservation measures | - | (1,000) | (394,651) | (334,142) | (394,651) | (335,142) |
| Payments to employees | (3,425,878) | (3,324,414) | (4,026,784) | (3,779,786) | (7,452,662) | (7,104,200) |
| Payments of taxes | (189,896) | (187,407) | (1,774,837) | (1,584,873) | (1,964,733) | (1,772,280) |
| Net cash from operating activities | 4,112,885 | 1,350,143 | 4,137,388 | 2,282,067 | 8,250,273 | 3,632,210 |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | | | | | |
| Additions to utility plant, net | (725,647) | (1,875,692) | (3,454,893) | (1,824,507) | (4,180,540) | (3,700,199) |
| Additions to renewable energy certificates | - | - | (416,320) | (177,390) | (416,320) | (177,390) |
| Additions to deferred conservation | - | - | 124,645 | (23,200) | 124,645 | (23,200) |
| Proceeds from (payment on) interfund loan | (1,787,519) | 1,094,409 | 1,787,519 | (1,094,409) | - | - |
| Proceeds from (payments on) note payable | (24,096) | (18,304) | - | (11,920) | (24,096) | (30,224) |
| Interest paid | (204,255) | (155,508) | - | (195) | (48,747) | (195) |
| Net cash from capital and related financing activities | (2,741,517) | (955,095) | (1,959,049) | (3,131,621) | (4,545,058) | (3,931,208) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | | | | |
| Interest received | 49,087 | 37,669 | 375,496 | 427,160 | 269,075 | 309,321 |
| Net change in cash and cash equivalents | 1,420,455 | 432,717 | 2,553,835 | (422,394) | 3,974,290 | 10,323 |
| CASH AND CASH EQUIVALENTS, beginning of year | 4,578,158 | 4,145,441 | 12,688,993 | 13,111,387 | 17,267,151 | 17,256,828 |
| CASH AND CASH EQUIVALENTS, end of year | $ 5,998,613 | $ 4,578,158 | $ 15,242,828 | $ 12,688,993 | $ 21,241,441 | $ 17,267,151 |

*Interest paid and received on intercompany note is eliminated in the total column*

# McMINNVILLE WATER AND LIGHT DEPARTMENT
## COMBINED STATEMENTS OF CASH FLOWS

| | Water | | Light | | Total | |
|---|---|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 | 2012 | 2011 |
| RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH FROM OPERATING ACTIVITIES | | | | | | |
| Operating income (loss) | $ 220,654 | $ 383,950 | $ 829,776 | $ (956,517) | $ 1,050,430 | $ (572,567) |
| Adjustments to reconcile operating income (loss) to net cash from operating activities | | | | | | |
| Collections received for the City of McMinnville | 7,648,342 | 7,582,482 | - | - | 7,648,342 | 7,582,482 |
| Remittances of collections to City of McMinnville | (7,642,339) | (7,633,604) | - | - | (7,642,339) | (7,633,604) |
| Depreciation | 1,442,641 | 1,407,783 | 1,680,321 | 1,541,077 | 3,122,962 | 2,948,860 |
| Other, net | (4,270) | 39,679 | 664,463 | 1,747,826 | 660,193 | 1,787,505 |
| Timber sales, net of related expenses | 2,605,898 | 1,355,475 | - | - | 2,605,898 | 1,355,475 |
| Other post-employment benefits liability | 66,078 | 480 | 90,550 | 655 | 156,628 | 1,135 |
| Changes in assess and liabilities: | | | | | | |
| Accounts receivable | (31,804) | (42,002) | (570,021) | (305,583) | (601,825) | (347,585) |
| BPA receivable | - | - | 819,814 | 327,885 | 819,814 | 327,885 |
| Due from the City of McMinnville | - | - | 387 | 716 | 387 | 716 |
| Inventories | 376 | 10,701 | (65,367) | (68,681) | (64,991) | (57,980) |
| Other current assets | (75,120) | (81,336) | 98,311 | (26,874) | 23,191 | (108,210) |
| Accounts payable | (99,834) | (1,696,232) | 436,303 | (8,104) | 336,469 | (1,704,336) |
| Accrued payroll | (6,459) | (439) | (12,989) | 19,581 | (19,448) | 19,142 |
| Other liabilities | (2,703) | (23,948) | 175,797 | 17,838 | 173,094 | (6,110) |
| Compensated absences | (9,080) | 31,778 | 6,847 | 27,042 | (2,233) | 58,820 |
| Due to the City of McMinnville | 505 | 376 | 6,585 | (350) | 7,090 | 26 |
| Advances and deposits | - | 15,000 | (23,389) | (34,444) | (23,389) | (19,444) |
| Net cash from operating activities | $ 4,112,885 | $ 1,350,143 | $ 4,137,388 | $ 2,282,067 | $ 8,250,273 | $ 3,632,210 |
| NONCASH CAPITAL ACTIVITIES | | | | | | |
| Contributions from others | $ 16,143 | $ 99,355 | $ 226,040 | $ 235,058 | $ 242,183 | $ 334,413 |

 See accompanying notes.

**Note 1 – Summary of Significant Accounting Policies**

**Reporting entity** – The McMinnville Water and Light Department (the Department or MWL), under the provisions of Chapter X of the McMinnville City Charter of 1978, is vested with authority to direct the water works and electrical plants of the City of McMinnville, Oregon (the City). The Department's governing board, the five-member Water and Light Commission, appoints a General Manager who is responsible for the day-to-day operations of the Department.

The Department provides electrical and water service to residential and commercial customers within the city limits of the City. The Department, under the criteria of the Governmental Accounting Standards Board (GASB), is considered a component unit of the City; therefore, it is an integral part of the City's reporting entity. The Department is accounted for as a discretely presented component unit in the financial statements of the City. Intercompany notes receivable and payable are eliminated in the combined total column.

**Measurement focus, basis of accounting, and basis of presentation** – For financial reporting purposes, the Department reports on an enterprise fund basis. Enterprise funds (a proprietary fund type) are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included in the balance sheets. The Department's net assets are segregated into two amounts: investment in capital assets, net of related debt and unrestricted.

The accrual basis of accounting is utilized by the Department for financial reporting, which is in accordance with accounting principles generally accepted in the United States of America for proprietary fund types. Under the accrual basis of accounting, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

The Department has implemented GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which specifically identifies and consolidates the accounting and financial reporting provisions that apply to state and local governments.

In preparing the Department's financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the 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.

**Cash and cash equivalents** – For financial reporting purposes, the Department's cash and cash equivalents are considered to be cash on hand, demand deposits, short-term investments with original maturities of three months or less from the date of acquisition, and the State of Oregon Local Government Investment Pool deposits.

**Note 1 – Summary of Significant Accounting Policies (continued)**

**Fair value of financial instruments** – The carrying amounts of current assets, including cash and cash equivalents and receivables, and current liabilities approximate fair value because of the short maturity of those instruments.

**Accounts receivable** – The Department recognizes revenue from electric and water services when the service is rendered. Accounts receivable also include estimated revenues, that are accrued for power and water deliveries not yet billed to customers from meter reading dates prior to month end (unbilled revenue) and are reversed in the following year when the billings occur.

The majority of the Department's receivables are due from companies, businesses, and individuals in areas served by the Department. Credit is extended to all customers who have requested service, who have identified themselves personally, and who do not have outstanding amounts owing to the Department. The Department may require deposits from customers depending on their specific payment performance, previous loss history, and history with the Department. Accounts receivable are due within 21 days and are stated at amounts due from customers as consumption is registered and billed monthly. Past due balances must be paid immediately to avoid additional fees and possible denial of services.

Management determines the allowance for doubtful accounts by considering a number of factors, including the length of time trade accounts receivable are past due, the customer's previous loss history, the customer's current ability to pay its obligation to the Department, the condition of the general economy and the industry as a whole. Management writes off accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts. Interest accrues as an account becomes past due with a subsequent monthly billing. Interest accruals are discontinued once an account becomes uncollectible.

**Inventories** – Inventories of materials and supplies are stated at the lower of average cost or market and are charged to expense or capitalized as construction in progress as they are used.

**Utility plant** – Utility plant is stated at cost, and includes property, plant, and equipment with an initial cost of $5,000 or more and an estimated useful life of more than one year. Cost generally includes materials, labor and an allocation of overhead costs. The costs of additions, renewals and betterments which improve or extend the lives of assets are capitalized. Maintenance and repairs are expensed as incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets as follows:

| | |
|---|---|
| Electric and water plant | 20 to 100 years |
| Office and other equipment | 10 to 14 years |
| Transportation equipment | 5 to 10 years |

**Note 1 – Summary of Significant Accounting Policies (continued)**

**Renewable energy certificates** – "Renewable Energy Certificate" (REC or Certificate) means a unique representation of the environmental, economic, and social benefits associated with the generation of electricity from renewable energy sources that produce qualifying electricity. One Certificate is created in association with the generation of one megawatt-hour (MWh) of qualifying electricity. While a Certificate is always directly associated with the generation of one MWh of electricity, transactions for Certificates may be conducted independently of transactions for the associated electricity.

The Department receives RECs as part of the purchase agreement with Bonneville Power Administration (BPA) for buying "Green Energy Premium Wind." The RECs are available for sale at market price. The Department also receives RECs as part of the renewable energy purchased from Waste Management Renewable Energy (WMRE). These RECs are also available for sale at market prices or are banked to satisfy future Oregon Renewable Portfolio Standard obligations. Markets for the sale of REC's are very limited at the present time. Future sales will be transaction specific and subject to Commission approval.

**Deferred conservation charges** – In November 2008, the Department entered into a long-term power purchase agreement with the BPA. The Commission also authorized conservation funding in order to secure a more favorable rate structure over the delivery period of 17 years. The Department will amortize these expenditures over the 17-year period which commenced October 1, 2011.

**Compensated absences** – It is the Department's policy to permit employees to accumulate earned but unused vacation benefits. Vacation pay is accrued when incurred and reported as a liability. Management considers all compensated absences as current liabilities.

**Due to/from City of McMinnville** – The Department bills and collects for sewer services rendered by the City. The Department also pays a tax on revenues from sales of electricity to the City in lieu of property tax. The balance due to the City represents this tax and sewer billings collected but not remitted to the City, and other miscellaneous amounts. The amount due from the City is for costs incurred by the Department.

**Operating revenues and expenses** – Management distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services in connection with the Department's principal ongoing operations. The principal operating revenues of the Department are sales of water and electricity. Operating expenses include the cost of sales, administrative expenses, and depreciation on capital assets. Revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**Note 2 – Cash and Deposits**

Oregon Revised Statutes authorize the Department to invest in general obligations of the U.S. Government and its agencies; certain bonded obligations of Oregon municipalities; bank repurchase agreements; certificates of deposit; bankers' acceptances; the State of Oregon Local Government Investment Pool; and certain corporate indebtedness.

The State of Oregon Local Government Investment Pool (Pool) is not registered with the U.S. Securities and Exchange Commission as an investment company. The Oregon Revised Statutes and the Oregon Investment Council govern the Pool's investment policies. The Oregon State Treasurer (OST) is the investment officer for the Pool and is responsible for all funds in the Pool. These funds must be invested, and the investments managed as a prudent investor would, exercising reasonable care, skill, and caution. Investments in the Pool are further governed by portfolio guidelines issued by the Oregon Short-Term Fund (OSTF) Board which establish diversification percentages and specify the types and maturities of investments. The Oregon Audits Division audits the Pool annually. The LGIP is commingled with other state funds in the OSTF. The OSTF is not managed as a stable net asset value fund. As such, preservation of principal is not assured by OST management or the OSTF Board. The OSTF is not currently rated by an independent rating agency, and may be sensitive to changing market conditions and investment risk.

The combined total bank balance at June 30, 2012, is $702,502. Of these deposits, $500,000 was covered by federal depository insurance. As required by Oregon Revised Statues, deposits in excess of federal depository insurance were held at a qualified depository for public funds. All qualified depositories for public funds are included in the multiple financial institution collateral pool that is maintained by and in the name of the Office of the State Treasurer.

The Commission authorized the funding for conversion of overhead power lines to underground. Cash is designated for this purpose in the amount of $276,431.

The Department had the following cash and cash equivalents, including designated cash, at June 30, 2012:

| | Water | Light | Total |
|---|---|---|---|
| Cash on hand | $ - | $ 1,400 | $ 1,400 |
| Cash on deposit with a bank | 128,650 | 484,065 | 612,715 |
| Local Government Investment Pool | 5,869,963 | 14,757,363 | 20,627,326 |
| | $ 5,998,613 | $ 15,242,828 | $ 21,241,441 |

**Note 2 – Cash and Deposits (continued)**

The Department had the following cash and cash equivalents at June 30, 2011:

| | Water | Light | Total |
|---|---|---|---|
| Cash on hand | $ - | $ 1,400 | $ 1,400 |
| Cash on deposit with a bank | 513,513 | 9,908 | 523,421 |
| Local Government Investment Pool | 4,064,645 | 12,677,685 | 16,742,330 |
| | $ 4,578,158 | $ 12,688,993 | $ 17,267,151 |

**Note 3 – Accounts Receivable**

Accounts receivable balances primarily from utility customers at June 30 are as follows:

| | 2012 | | |
|---|---|---|---|
| | Water | Light | Total |
| Accounts receivable | $ 524,831 | $ 3,239,562 | $ 3,764,393 |
| Allowance for doubtful accounts | (5,955) | (26,276) | (32,231) |
| | $ 518,876 | $ 3,213,286 | $ 3,732,162 |

| | 2011 | | |
|---|---|---|---|
| | Water | Light | Total |
| Accounts receivable | $ 492,753 | $ 2,669,934 | $ 3,162,687 |
| Allowance for doubtful accounts | (5,681) | (26,669) | (32,350) |
| | $ 487,072 | $ 2,643,265 | $ 3,130,337 |

**Note 4 – Utility Plant**

Utility plant is comprised of the following:

| | June 30, 2012 | June 30, 2011 |
|---|---|---|
| WATER | | |
| Structures and improvements | $ 6,440,828 | $ 6,429,305 |
| Water treatment plant | 34,700,586 | 34,649,602 |
| Supply and distribution systems | 52,946,983 | 52,379,133 |
| Furniture and equipment | 842,510 | 826,755 |
| Transportation equipment | 684,239 | 674,815 |
| | 95,615,146 | 94,959,610 |
| Less accumulated depreciation | (19,216,069) | (17,922,072) |
| | 76,399,077 | 77,037,538 |
| Land and land rights | 2,312,634 | 2,290,424 |
| Construction in progress | 1,875,235 | 1,934,720 |
| Total water | 80,586,946 | 81,262,682 |
| LIGHT | | |
| Structures and improvements | 2,195,659 | 2,178,375 |
| Supply and distribution systems | 49,034,608 | 45,388,638 |
| Furniture and equipment | 1,255,046 | 1,236,011 |
| Transportation equipment | 1,467,986 | 1,394,459 |
| | 53,953,299 | 50,197,483 |
| Less accumulated depreciation | (19,903,795) | (18,452,416) |
| | 34,049,504 | 31,745,067 |
| Land and land rights | 493,277 | 493,277 |
| Construction in progress | 884,833 | 1,163,675 |
| Total light | 35,427,614 | 33,402,019 |
| Total water and light | $ 116,014,560 | $ 114,664,701 |

**Note 4 – Utility Plant (continued)**

Utility Plant activity during the year ended June 30, 2012 was as follows:

| | Balance June 30, 2011 | Increases | Decreases | Balance June 30, 2012 |
|---|---|---|---|---|
| Land and land rights | $ 2,783,701 | $ 22,210 | $ - | $ 2,805,911 |
| Construction in progress | 3,098,395 | 2,696,910 | (3,035,237) | 2,760,068 |
| Total non-depreciable | 5,882,096 | 2,719,120 | (3,035,237) | 5,565,979 |
| Structures and improvements | 8,607,680 | 28,807 | - | 8,636,487 |
| Water treatment plant | 34,649,602 | 50,984 | - | 34,700,586 |
| Supply and distribution systems | 97,767,771 | 4,675,948 | (462,128) | 101,981,591 |
| Furniture and equipment | 2,062,766 | 34,790 | - | 2,097,556 |
| Transportation equipment | 2,069,274 | 136,197 | (53,246) | 2,152,225 |
| Total depreciable | 145,157,093 | 4,926,726 | (515,374) | 149,568,445 |
| Less accumulated depreciation: | | | | |
| Electric plant | (17,488,658) | (1,579,013) | 215,190 | (18,852,481) |
| Water plant | (17,564,823) | (1,363,530) | 104,954 | (18,823,399) |
| Transportation equipment | (1,321,007) | (180,419) | 57,442 | (1,443,984) |
| Total accumulated depreciation | (36,374,488) | (3,122,962) | 377,586 | (39,119,864) |
| Utility plant, net | $ 114,664,701 | $ 4,522,884 | $ (3,173,025) | $ 116,014,560 |

**Note 4 – Utility Plant (continued)**

Utility Plant activity during the year ended June 30, 2011 was as follows:

| | Balance June 30, 2010 | Increases | Decreases | Balance June 30, 2011 |
|---|---|---|---|---|
| Land and land rights | $ 2,716,736 | $ 67,188 | $ (223) | $ 2,783,701 |
| Construction in progress | 4,139,862 | 2,486,773 | (3,528,240) | 3,098,395 |
| Total non-depreciable | 6,856,598 | 2,553,961 | (3,528,463) | 5,882,096 |
| Structures and improvements | 8,535,465 | 72,215 | - | 8,607,680 |
| Water treatment plant | 33,439,121 | 1,210,481 | - | 34,649,602 |
| Supply and distribution systems | 94,921,534 | 3,606,442 | (760,205) | 97,767,771 |
| Furniture and equipment | 1,956,202 | 106,564 | - | 2,062,766 |
| Transportation equipment | 1,901,532 | 167,742 | - | 2,069,274 |
| Total depreciable | 140,753,854 | 5,163,444 | (760,205) | 145,157,093 |
| Less accumulated depreciation: | | | | |
| Electric plant | (16,358,296) | (1,443,833) | 313,471 | (17,488,658) |
| Water plant | (16,171,881) | (1,392,942) | - | (17,564,823) |
| Transportation equipment | (1,149,073) | (171,965) | 31 | (1,321,007) |
| Total accumulated depreciation | (33,679,250) | (3,008,740) | 313,502 | (36,374,488) |
| Utility plant, net | $ 113,931,202 | $ 4,708,665 | $ (3,975,166) | $ 114,664,701 |

**Note 5 – Renewable Energy Certificates**

The Department currently has 131,472 and 69,795 RECs banked in its Western Renewable Energy Generation Information System (WREGIS) account as of June 30, 2012 and 2011, respectively. These RECs are valued at $6.75 per REC for a total value of $887,436 and $471,116 as of June 30, 2012 and 2011, respectively. These REC's were obtained from the purchase of BPA Wind (environmentally preferred power). The value of these REC's is based on management's estimate of fair market value.

The Department also holds 64,803 in its WREGIS account for RECs received from Waste Management Renewable Energy. These RECs can either be sold or used to satisfy the Department's Oregon Renewable Energy Standard (see Note 1).

**Note 6 – Long–Term Notes Payable**

Transactions on long-term notes payables for the land acquisition at June 30, 2012 were as follows:

| | Balance June 30, 2011 | Increases | Decreases | Balance June 30, 2012 |
|---|---|---|---|---|
| Water | $ 24,096 | $ - | $ (24,096) | $ - |

Transactions on two long-term notes payables for land acquisition at June 30, 2011 were as follows:

| | Balance June 30, 2010 | Increases | Decreases | Balance June 30, 2011 |
|---|---|---|---|---|
| Water | $ 42,400 | $ - | $ (18,304) | $ 24,096 |
| Light | 11,920 | - | (11,920) | - |
| Total | $ 54,320 | $ - | $ (30,224) | $ 24,096 |

The remaining note payable had a stated interest rate of 4% and matured on October 23, 2011.

**Note 7 – Related–Party Note Payable/Note Receivable**

In September 2009, the Department entered into an interdepartmental loan resulting in a note payable from Water to Light at a stated interest rate of 1.991% and maturing November 15, 2017. Transactions on the note payable at June 30, 2012 and 2011 are as follows:

| | Balance June 30, 2011 | Increases | Decreases | Balance June 30, 2012 |
|---|---|---|---|---|
| Total | $ 11,118,974 | $ - | $ (1,787,519) | $ 9,331,455 |

| | Balance June 30, 2010 | Increases | Decreases | Balance June 30, 2011 |
|---|---|---|---|---|
| Total | $ 10,042,869 | $ 2,623,000 | $ (1,546,895) | $ 11,118,974 |

**Note 7 – Related–Party Note Payable/Note Receivable (continued)**

Maturities of the note payable are as follows:

| | | Principal | Interest | Total |
|---|---|---|---|---|
| Year Ending June 30, | 2013 | $ 1,823,979 | $ 169,607 | $ 1,993,586 |
| | 2014 | 1,860,622 | 132,964 | 1,993,586 |
| | 2015 | 1,898,001 | 95,585 | 1,993,586 |
| | 2016 | 1,935,991 | 57,595 | 1,993,586 |
| | 2017 | 1,812,862 | 21,001 | 1,833,863 |
| | | $ 9,331,455 | $ 476,752 | $ 9,808,207 |

**Note 8 – Fiber Optic Activity**

The Department operates and maintains a fiber optic network for the benefit of the three primary city government partners and offers dark lease agreements with our customers. The system consists of approximately 26 miles of 144 count fiber with the school district, city government, and the Department, each having exclusive rights of use for 12 strands. Each of these organizations utilize the system to communicate to their various offices and facilities. The Department utilizes the fiber for water and electric control, monitoring, and facility communication systems.

The Department currently has seven dark fiber leases held by Light Speed networks, McMinnville Access Company, and Oregon Mutual Insurance. MWL policies allow for the expansion of the network to meet the needs of new customers or for system improvements to meet the needs of the three government partners.

**Note 8 – Fiber Optic Activity (continued)**

Selected financial data is reported as follows as of June 30:

| | 2012 | 2011 |
|---|---|---|
| OPERATING REVENUES | | |
| Dark fiber leases | $ 22,300 | $ 37,183 |
| Total operating revenues | 22,300 | 37,183 |
| OPERATING EXPENSES | | |
| Operating expenses | 15,940 | 17,772 |
| Maintenance expense | 2,016 | 4,428 |
| Administrative and general | 4,324 | 819 |
| Depreciation expense | 7,652 | 4,660 |
| Total operating expenses | 29,932 | 27,679 |
| Operating income (loss) | (7,632) | 9,504 |
| NON-OPERATING INCOME (EXPENSE) | | |
| Interest income | 552 | 536 |
| Other income (expense) | 16 | (3,400) |
| Total non-operating income (expense) | 568 | (2,864) |
| Income (loss) before contributed capital | (7,064) | 6,640 |
| Hookup fees and contributed utility systems | 28,162 | 25,505 |
| Change in net assets | $ 21,098 | $ 32,145 |

**Note 9 – Major Customer and Supplier**

Sales of electricity were made to one major commercial customer during the years ended June 30, 2012 and 2011, in amounts exceeding 10% of total sales. This customer accounted for approximately $11,317,200 and $9,394,600 of revenues during the years ended June 30, 2012 and 2011, respectively. At June 30, 2012 and 2011, accounts receivable from this same customer amounted to approximately $993,000 and $578,000, respectively.

**Note 9 – Major Customer and Supplier (continued)**

Purchases were made from one major supplier of power, including supply, transmission and distribution during the years ended June 30, 2012 and 2011, in amounts exceeding 10% of the total of such purchases. This supplier accounted for approximately $24,014,800 and $21,541,200 of purchases during the years ended June 30, 2012 and 2011, respectively. At June 30, 2012 and 2011, amounts due to this same supplier, and included in accounts payable, amounted to approximately $1,943,300 and $1,121,900, respectively.

**Note 10 – Deferred Compensation Plan**

The Department offers all employees access to a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plans permit the employees to defer a portion of their salary until future years. The deferred compensation is not available to participants until termination, retirement, death, or certain unforeseeable emergency. The assets and income of the plans are held in trust for the exclusive benefit of the participants and their beneficiaries, and accordingly are not included in the Department's financial statements.

**Note 11 – Other Post-Employment Benefits**

**Plan description** – The Department provides post-employment health benefits, as per a contractual obligation, for certain retirees who were hired prior to August 1, 2005, and who are at least sixty years old, and their dependents. The benefits vary depending on the years of service of the retiree. The Department pays 100 percent of all health insurance costs for those employees with over 20 years of service up until the retiree reaches Medicare age. For those employees with over 25 years of service, the Department also pays for all health insurance costs of the retiree's spouse until they reach Medicare age, and the children of the retiree until they reach the age of maturity. The plan is financed by the Department on a pay-as-you-go basis. Retired employees who do not have 20 years of service may continue to participate in the health insurance plan until they reach Medicare age provided the retired employees pay all insurance premiums. This "plan" is not a stand-alone plan and therefore does not issue its own financial statements. The MWL Commission is responsible for establishing and amending benefits and funding policies.

**Funding policy** – At June 30, 2012, 2011, and 2010, there were 15 retired employees and spouses, receiving health insurance coverage provided by the Department. For the years ended June 30, 2012, 2011, and 2010 the Department incurred $113,284, $105,352, and $114,292, respectively, of expenses for these health insurance premiums.

**Note 11 – Other Post-Employment Benefits (continued)**

**Annual OPEB cost and net OPEB obligation** – The Department's annual other post-employment benefit (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), and amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize the actuarial liability over one year. The following table shows the components of the Department's annual OPEB cost for the years, amounts actually contributed to the plan, and changes in the Department's net OPEB obligation:

| | June 30, 2012 | June 30, 2011 | June 30, 2010 |
|---|---|---|---|
| Annual required contribution | $ 221,324 | $ 51,829 | $ 54,332 |
| Interest on net OPEB obligation | 48,588 | 54,658 | 54,886 |
| Annual OPEB cost | 269,912 | 106,487 | 109,218 |
| Explicit benefit payments | 113,284 | 105,352 | 114,292 |
| Increase (decrease) in net OPEB obligation | 156,628 | 1,135 | (5,074) |
| Net OPEB obligation – beginning of year | 1,215,760 | 1,214,625 | 1,219,699 |
| Net OPEB obligation – end of year | $ 1,372,388 | $ 1,215,760 | $ 1,214,625 |

The Department's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2010, 2011, and 2012 were as follows:

| Fiscal Year Ended June 30, | Annual OPEB Cost | Contribution | Percent of Annual OPEB Cost Contributed | Net OPEB Obligation |
|---|---|---|---|---|
| 2010 | $ 109,218 | $ 114,292 | 105% | $ 1,214,625 |
| 2011 | 106,487 | 105,352 | 99% | 1,215,760 |
| 2012 | 269,912 | 113,284 | 42% | 1,372,388 |

**Funded status and funding progress**

| Actuarial Valuation Date | Actuarial Accrued Liability (a) | Actuarial Value of Assets (b) | Actuarial Accrued Unfunded Liability (a) - (b) | Funded Ratio (b) / (a) | Annual Covered Payroll (c ) | Unfunded Actuarial Accrued Liability as % of Payroll [(a) – (b)] / (c ) |
|---|---|---|---|---|---|---|
| 8/1/2006 | $ 1,146,124 | $ - | $ 1,146,124 | 0.00% | $ 2,854,677 | 40.15% |
| 8/1/2008 | 1,191,313 | - | 1,191,313 | 0.00% | 2,634,910 | 45.21% |
| 8/1/2010 | 1,338,305 | - | 1,338,305 | 0.00% | 2,558,493 | 52.31% |

**Note 11 – Other Post-Employment Benefits (continued)**

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

**Actuarial methods and assumptions** – Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the Department and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and the plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the actuarial valuation conducted as of August 1, 2010, the projected unit credit actuarial cost method was used. The unfunded actuarial accrued liability has been amortized over a one-year period. Actuarial assumptions included a discount rate of 4% and an annual healthcare cost trend rate of 8.5% in the first year, 7.5% in the second year, 6.5% in the third year, 6% for the 4th through 23rd year, 5.5% for the 24th through 47th year, and 5% thereafter.

**Note 12 – Public Employee Retirement Systems (PERS)**

**Plan description** – The Department contributes to two pension plans administered by the Oregon Public Employees Retirement System (OPERS). The Oregon Public Employees Retirement Fund (OPERF) applies to the Department's contribution for qualifying employees who were hired before August 29, 2003, and is a cost-sharing multiple-employer defined benefit pension plan. The Oregon Public Service Retirement Plan (OPSRP) is a hybrid successor plan to the OPERF and consists of two programs: the Pension Program and the Individual Account Program (lAP). The Pension Program, the defined benefit portion of the plan, applies to qualifying Department employees hired after August 29, 2003.

Both OPERS plans provide retirement and disability benefits, post employment healthcare benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefits are calculated by a formula for members who attain normal retirement age. The formula takes into account final average salary and years of service. OPERF members are allowed to retire at age 58 with unreduced benefits, but retirement is generally available after age 55 with reduced benefits. Compulsory retirement age is 70. Retirement benefits are payable in lump sum or monthly amounts using several payment options. The 1995 Oregon Legislature established a second tier of OPERF benefits for employees who established membership on or after January 1, 1996 called Tier Two. The second tier does not have the Tier One assumed earnings rate guarantee and has a higher retirement age of 60 with unreduced benefits. OPSRP members are allowed to retire at age 65 with unreduced benefits.

**Note 12 – Public Employee Retirement Systems (PERS) (continued)**

OPERS is administered under *Oregon Revised Statute (ORS) Chapter* 238, which establishes the Public Employees Retirement Board as the governing body of OPERS. OPERS issues a publicly available *Comprehensive Annual Financial Report* that includes financial statements and required supplementary information. This report may be obtained by writing to Oregon Public Employees Retirement System, PO Box 23700, Tigard, Oregon 97281-3700 or by calling 503-598-7377.

**Funding policy** – The Department is required by ORS 238.225 to contribute at an actuarially determined rate for the qualifying employees under the OPERF plan, and a general service rate for the qualifying employees under the OPSRP plan. The Department's employer contributions are paid as a percentage of covered employees' salaries. The OPERF (Tier One and Tier Two) rate in effect for each of the years ended June 30, 2012, 2011, and 2010 was 18.12%, 13.93%, and 13.93%, respectively. The OPSRP rate in effect for the years ended June 30, 2012, 2011, and 2010 was 14.06%, 12.25%, and 12.25%, respectively.

Beginning January 1, 2004, all OPERS member contributions go into the Individual Account Program (IAP), the defined contribution portion of the plan. OPERS members retain their existing OPERS accounts, but any future member contributions are deposited into the member's IAP account, not the member's OPERS account. All employees who serve a six-month waiting period in a qualifying position are eligible to participate; benefits generally vest after five years of continuous service.

The employee contribution of 6% of covered compensation, referred to as the employee pickup, is paid by the Department. As of January 1, 2004, Tier One and Two employee contributions are also deposited into the IAP. Employer contribution requirements are established and may be amended by the OPERS Public Employees Retirement Board while the employee members' rate is set by statute, ORS 238.200.

**Annual pension cost** – The Department's contributions to OPERS for the years ended June 30, 2012, 2011, and 2010, were approximately $1,005,000, $845,000, and $846,000, respectively. The annual pension costs were equal to the required contributions for fiscal years ended June 30, 2012, 2011, and 2010.

**Note 13 – Retirement Health Insurance Account (RHIA)**

**Plan description** – As a member of OPERS, the Department contributes to the Retirement Health Insurance Account (RHIA) for each of its eligible employees. RHIA is a cost-sharing multiple-employer defined benefit other post-employment benefit plan administered by OPERS. RHIA pays a monthly contribution toward the cost of Medicare companion health insurance premiums of eligible retirees. Oregon Revised Statute (ORS) 238.420 established this trust fund. Authority to establish and amend the benefit provisions of RHIA reside with the Oregon Legislature. The plan is closed to new entrants after January 1, 2004. OPERS issues a publicly available *Comprehensive Annual Financial Report* that includes financial statements and required supplemental information. The report may be obtained by writing to Oregon Public Employees Retirement System, PO Box 23700, Tigard, Oregon 97281-3700 or by calling 503-598-7377.

**Note 13 – Retirement Health Insurance Account (RHIA) (continued)**

**Funding policy** – Because RHIA was created by enabling legislation (ORS 238.420), contribution requirements of the plan members and the participating employers were established and may be amended only by the Oregon Legislature. ORS require that an amount equal to $60 or the total monthly cost of Medicare companion health insurance premiums coverage, whichever is less, shall be paid from the RHIA established by the employer, and any monthly cost in excess of $60 shall be paid by the eligible retired member in the manner provided in ORS 238.410. To be eligible to receive this monthly payment toward the premium cost, the member must: (1) have eight years or more of qualifying service in OPERS at the time of retirement or receive a disability allowance as if the member had eight years or more of creditable service in OPERS, (2) receive both Medicare Parts A and B coverage, and (3) enroll in a OPERS sponsored health plan. A surviving spouse or dependent of a deceased OPERS retiree who was eligible to receive the subsidy is eligible to receive the subsidy if he or she (1) is receiving a retirement benefit or allowance from OPERS, or (2) was insured at the time the member died and the member retired before May 1, 1991.

Participating entities are contractually required to contribute to RHIA at a rate assessed each year by OPERS. The rates applied to annual covered payroll for the fiscal years 2011 and 2012 were 0.29% and 0.59%, respectively for Tier 1 and 2 members and 0.19% and 0.50%, respectively for OPSRP members. The OPERS Board of Trustees sets the employer contribution rate based on the ARC of the employers, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45.

The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) of the plan over a period not to exceed 30 years. The Department's contributions to RHIA for the fiscal years 2012–11, 2011–10, and 2010–09 were $25,000, $11,000, and $11,000, respectively, which equaled the required contributions each year.

**Note 14 – Jointly Governed Organization**

The Department, in conjunction with six other Oregon municipal corporations that provide distribution of electric services, is a member of the Oregon Municipal Energy and Conservation Agency (OMECA). OMECA issued tax-exempt revenue bonds to fund conservation projects of the member organizations. The bonds are payable solely by BPA and do not represent obligations of OMECA or the Department. OMECA's Board of Directors is comprised of one member from each participating entity. No member has any obligation, entitlement or residual interest in OMECA.

**Note 15 – Risk Management**

The Department is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; natural disasters; and injuries to employees. The Department is covered for comprehensive liability, property, auto liability and physical damage, employer's liability, and workers' compensation insurance through City County Insurance Services, a public entity risk pool.

**Note 15 – Risk Management (continued)**

For property and liability insurance, settlements did not exceed insurance coverage in any of the past three fiscal years.

**Note 16 – Commitments and Contingency**

The Department previously entered into Net Billing Agreements (the Agreements) to purchase a portion of the power to be generated from Washington Public Power Supply System, now Energy Northwest Nuclear Projects No. 1, 2, and 3 (the Projects). Over the life of the Projects, the Agreements provide for the Department to make payments equal to its share of all operating and debt service costs of the Projects whether or not the plants are operable or operating. Project No. 1 and 3 have never been completed. Project No. 2 continues in operation.

Pursuant to the Agreements the Department assigned its share of the Projects to BPA. In return for these assignments, the Department's annual power purchase payment obligation to BPA is reduced by the amount of payments the Department would, but for the assignments, make directly to Energy Northwest in connection with the Projects' costs. If such costs exceed the Department's cost of power purchased from BPA on an annual basis, BPA will assign to other participants or pay to Energy Northwest any of the Department's portion of the projects' cost in excess of BPA's billings to the Department for the purchase of power.

While the Department remains liable to Energy Northwest pursuant to the Agreements, BPA accepted assignments of the Agreements and agreed to provide the Department with the payments, offsets and credits specified in the Agreements, whether or not the Projects were completed, operable or operating or if there was a default by Energy Northwest or any participant.

The Department's present commitments based on its participant's share and representing its share of construction costs based on aggregate outstanding debt as of June 30, 2012 and 2011, approximates $73,041,000 and $78,848,000, respectively, for Projects No. 1, 2 and 3. This aggregate amount, including interest and annual operating costs, is payable over the life of Project No. 2 as part of the cost of power purchased and, for Projects No. 1 and 3 until the bonded indebtedness for these Projects has been paid. The Department's obligations pursuant to the Agreements are projected to extend beyond the term of the Department's current BPA Power Sales Agreement which expires on Sept. 30, 2028.

The Department also purchases power from Priest Rapids Development and Wanapum Development, and is also required to pay a portion of the development costs under these contracts through April 1, 2052, which coincides with the expiration of the new FERC license (unless terminated earlier under terms of the contract.) Costs associated with these contracts for each of the years ended June 30, 2012 and 2011, were approximately $564,000 and $583,000, respectively.

**Note 17 – BPA Overpayment**

The Residential Exchange Program (REP) is used to distribute financial benefits of the Federal Columbia River Power System to the residential and small farm customers of the region's investor-owned utilities (IOUs). On May 3, 2007, the U.S. Ninth Circuit Court of Appeals ruled that BPA exceeded its settlement authority in 2000 when it executed the REP settlements with six IOUs, holding that BPA's decision to allocate costs of the settlements to publicly owned utilities was not in accordance with the law.

The Court remanded the issue back to BPA and as a result of the Court's decisions, BPA suspended monthly program benefits to the IOUs. This resulted in BPA's over-collection of funds from its publicly-owned utility customers. This left BPA with larger than anticipated financial reserves. Because of the over-collection from public utilities, BPA has refunded amounts directly to public utilities as well as issuing "look back adjustments" that show as credits against power costs on monthly BPA bills. The overpayment that was attributed to the Department was $3,700,000 and this is recorded as a reduction to supply and transmission expense within operating expenses. This was refunded to the Department in October 2008. The fiscal year 2012 and 2011 credits for 2002–2006 look back amounts were $1,120,000 and $1,265,000 respectively. For fiscal year 2013, the look back credit will be $1,079,000. Future look back credits have not yet been determined.

# INDEPENDENT AUDITOR'S COMMENTS

MOSS ADAMS LLP
Certified Public Accountants | Business Consultants

# INDEPENDENT AUDITOR'S COMMENTS

Board of Commissioners
McMinnville Water and Light Department
McMinnville, Oregon

We have audited the accompanying combined financial statements of the McMinnville Water and Light Department (the Department) as of and for the year ended June 30, 2012 and have issued our report thereon dated November 15, 2012. We conducted our audit 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.

**Compliance**

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, including provisions of Oregon Revised Statutes as specified in Oregon Administrative Rules (OAR) 162-010-000 to 162-010-330, as set forth below, noncompliance with which could have a direct and material effect on the determination of financial statement amounts:

- The accounting records and related internal control over financial reporting.
- The amount and adequacy of collateral pledged by depositories to secure the deposit of public funds.
- The requirements relating to debt.
- The requirements relating to insurance and fidelity bond coverage.
- The appropriate laws, rules, and regulations pertaining to programs funded wholly or partially by other governmental agencies.
- The statutory requirements pertaining to the investment of public funds.
- The requirements pertaining to the awarding of public contracts and the construction of public improvements.

The results of our tests disclosed no matters of noncompliance with those provisions that are required to be reported under Minimum Standards for Audits of Oregon Municipal Corporations, prescribed by the Secretary of State. 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.

## Internal Control over Financial Reporting

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

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affect the Department's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Department's financial statements that is more than inconsequential will not be prevented or detected by the Department's internal controls.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Department's internal control.

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

This report is intended solely for the information and use of the Department's management, the Board of Commissioners, and the Secretary of State, Division of Audits of the State of Oregon and is not intended to be and should not be used by anyone other than these specified parties.

Julie Desimone

Julie Desimone, Partner for Moss Adams LLP
November 15, 2012