

MASON COUNTY PUBLIC UTILITY DISTRICT No. 3

SHELTON, MASON COUNTY, WASHINGTON

**2006
COMPREHENSIVE ANNUAL
FINANCIAL REPORT**

COMPREHENSIVE ANNUAL FINANCIAL REPORT

Mason County Public Utility District No. 3
Shelton, Mason County, Washington

For the fiscal year ended December 31, 2006



Prepared by the Finance and Public Information Departments

Cover: With Washington State's Olympic Mountains rising in the background, Mason County PUD No. 3 Linemen Mike Willig and Mike Ladenburg conduct maintenance on PUD facilities on the Tahuya Peninsula. Photo Credit, Terri Oberg

**MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington**

2006 COMPREHENSIVE ANNUAL FINANCIAL REPORT

TABLE OF CONTENTS

Introductory Section

Manager's Message	Page 2
Commissioner's Message	Page 3
Fast Facts	Page 4
Certificate of Achievement for Excellence in Financial Reporting	Page 5
Letter of Transmittal	Page 6
Organizational Chart	Page 9
Commissioners and Management Staff	Page 10

Financial Section

Independent Auditor's Report	Page 13
Management's Discussion and Analysis	Page 14
Basic Financial Statements	
Statement of Net Assets	Page 17
Statement of Revenues, Expenses and Changes in Fund Net Assets	Page 20
Statement of Cash Flows	Page 21
Statement of Fiduciary Net Assets	Page 23
Statement of Changes in Fiduciary Net Assets	Page 24
Notes to Financial Statements	Page 25

Statistical Section

Financial Results	Page 41
Historical Customers, Energy Sales & Revenues	Page 43
Analysis of Uncollectible Accounts	Page 45
Comparative Tax Costs	Page 47
Demographic Statistics	Page 49

INTRODUCTORY SECTION

Message from the Manager

The Mason County PUD No. 3 board of commissioners and employees are happy to report that 2006, while a challenging year, was weathered well by the utility. We are on a sound financial footing and continue to improve our system reliability.



Following are some of the highlights of the year:

- The construction of the long-planned Johns Prairie substation was completed. This substation improves reliability in the Johns Prairie industrial area and backs up other substations, allowing load to be shifted when necessary. In addition, it provides an alternate feed for the Simpson waterfront operation.
- PUD 3 entered into an agreement with other participants to purchase an additional one megawatt from the Nine Canyon Wind Project near the Tri Cities. This makes our total current wind purchase three megawatts of nameplate capacity.
- A rate case with the Bonneville Power Administration (BPA) was concluded which sets our power rates for three years.
- In response to increasing costs in a number of areas and the fact that the BPA did not decrease wholesale rates in the new rate period as forecast during the energy crisis, two three percent retail rate increases were adopted by the board of commissioners to occur in 2006. The first three percent increase was effective on April 1 and the second on October 1.
- The worst storm we have seen in 10 years hit Mason County on December 14. The PUD 3 team pulled together in an amazing effort to restore power to utility customers as soon as possible. The understanding and support of our customers was greatly appreciated during this challenging time.

As always, the commission and staff of Mason County PUD No. 3 are committed to quality service that is responsive to customer needs in a fiscally planned and responsible way.

A handwritten signature in black ink that reads "Wyla J. Wood". The signature is written in a cursive, flowing style.

Wyla J. Wood, Manager
Mason County PUD No. 3

Message from the Board President



On behalf of the Board of Commissioners and staff of Mason County PUD No. 3, I am pleased to present our owner/ratepayers with the 2006 annual report. As a community-owned utility, PUD 3 is committed to ensuring that we serve you with safe, reliable and affordable service every day.

Mason County PUD No. 3 is a community-owned and governed utility, created to provide safe, reliable and cost-based electric and wholesale telecommunication services. PUD 3 strives to meet the community's expectations through responsive customer service; an educated, well-trained staff; a strong commitment to protect and improve the public's investment in the utility; and the wise and efficient use of the community's resources.

Because Mason County PUD No. 3 is a public power utility, each citizen who receives services from the PUD owns a part of it.

- PUD 3 is owned and controlled by the citizens who live in the community.
- PUD 3 benefits the local economy by keeping revenues in the community rather than paying profits to stockholders.
- PUD 3 works hard to keep electricity rates low and help its owner/ratepayers use energy efficiently and safely.

Mason County PUD No. 3 encourages all owner/ratepayers to communicate with us about our services through mail, telephone, or our web site www.masonpud3.org. Citizens are also invited to attend our regular board meetings that are held each Tuesday at the administrative office building in Shelton at 307 West Cota Street.

A handwritten signature in black ink, appearing to read "Bruce Jorgenson". The signature is fluid and cursive.

Bruce Jorgenson, President
Board of Commissioners
Mason County PUD No. 3

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington

FAST FACTS

Unaudited
FOR THE YEAR ENDING DECEMBER 31, 2006

Electric

Number of customers:	31,528
Number of employees:	114
Electricity sales in kWh:	646,985,720
Average annual residential use in kWh:	13,413
Average kWh cost for residential use:	\$0.0672
Number of substations:	11
Overhead line miles:	657
Underground line miles:	1,010
Average load in kW:	78,722
Maximum system load in kW:	162,315
2006 net budget:	\$47,200,000

Fiber

Number of end users:	386
Fiber miles within system:	354

Commissioners

Linda R. Gott, District 1
Bruce E. Jorgenson, District 3
John H. Whalen, District 2

Manager

Wyla J. Wood



Certificate of Achievement for Excellence in Financial Reporting

Presented to

Mason County

Public Utility District No. 3

Washington

For its Comprehensive Annual

Financial Report

for the Fiscal Year Ended

December 31, 2005

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



A handwritten signature in black ink, appearing to read "Ronald J. Klein".

President

A handwritten signature in black ink, appearing to read "Jeffrey R. Emer".

Executive Director

**COMMISSIONERS**

LINDA R. GOTT
BRUCE E. JORGENSON
JOHN H. WHALEN

MANAGER

WYLA J. WOOD

June 7, 2007

To the Board of Commissioners and Customers
Mason County Public Utility District No. 3
Shelton, Washington

The Comprehensive Annual Financial Report (CAFR) of the Mason County Public Utility District No. 3 for the year ended December 31, 2006, is hereby submitted. The report is designed to assess the district's financial condition, educate readers about district services, and examine current challenges facing the district.

Responsibility for Report

The management of the district is responsible for preparing the information in this annual report. The financial statements were prepared in accordance with generally accepted accounting principles (GAAP) applied on a consistent basis and include amounts that are based on management's best estimates and judgments. To provide a reasonable basis for making these representations, management has established and maintains a comprehensive internal control framework that includes organizational, administrative and accounting processes. The internal control system provides reasonable assurance as to the integrity and reliability of the financial statements, the safeguarding of assets from unauthorized use or disposition, and that business transactions are conducted in compliance with state laws and regulations. However, because the cost of internal controls should not outweigh their benefits, the district's system of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement. As management, we assert that to the best of our knowledge and belief, this financial report is complete and reliable in all material respects.

Independent Audit

The district's financial statements have been audited by the Washington State Auditor's Office. Management has made available to them all financial records and related data necessary to complete the audit. Management considers and takes appropriate action on audit recommendations concerning internal control procedures, financial matters and legal compliance.

The goal of the independent audit was to provide reasonable assurance that the financial statement of the district for the fiscal year ended December 31, 2006, is free of material misstatement. The audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The auditor concluded that there was a reasonable basis for rendering an unqualified opinion that the district's financial statement for the year ended December 31, 2006, is fairly presented in conformity with generally accepted accounting principles. The auditor's report is presented at the beginning of the financial section of this report.

Report Format

GAAP require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The district's MD&A can be found immediately following the report of the independent auditors.

The CAFR is presented in three sections: Introductory, Financial and Statistical. The Introductory Section includes the letter of transmittal and other material that may be useful in understanding the district. The Financial Section contains the MD&A, the auditor's report, and financial statements with accompanying notes. The Statistical Section provides unaudited ten year trend data for selected financial and operational information about the district's service territory that is intended to be helpful in assessing the district's financial condition.

About Mason County PUD No. 3

Mason County PUD No. 3 ("district") was established by vote in 1934 and began operations in 1939 under the direction of three elected commissioners. A schedule detailing the names of the board of commissioners, the length of their tenure, the names of key district personnel, and the name and address of the district attorney will be found on page 10 of this report. The district's headquarters are in Shelton, Washington, approximately 22 miles northwest of Olympia, the capital of Washington State.

The district's service area encompasses 567 square miles, most of which is in Mason County. Electric service is provided to 5 square miles in southern Kitsap County, 18 square miles in eastern Grays Harbor County, and 0.00156 square miles in southwestern Pierce County.

The district owns and operates 29.66 miles of 115 KV transmission lines. During 2002 a project to provide 5.6 MW of generating capacity was completed with the Olympic View Generating Station being put on-line. The district is now a full requirements customer of the Bonneville Power Administration (BPA), taking delivery of power at eleven substations. It has 1,667 miles of primary lines. As of December 31, 2006, the value of the district's net plant totaled \$108 million. At that time it served 31,528 customers. Load data for the year included kilowatt-hour sales to retail customers of 646,985,720.

The district provides wholesale fiber optic services to eight retail internet service providers in the county who in turn provide connections to 386 locations over 354 miles of fiber optic line.

The new John's Prairie Substation was nearing completion in December 2006. Once energized, the new substation will help meet the demands for electricity from increased residential constructions and the expansion of commercial and industrial uses in Mason County. The substation will allow for redundant power supply to the district's largest industrial customer and will back up other substations for reliability purposes. The district's system is designed to allow for redundant feeds between substations in order to restore electricity more quickly during outages or to allow for substation maintenance.

Annual Budget

The district records financial transactions within a proprietary fund, other than those in one fiduciary fund comprised of a Voluntary Employee Benefit Association (VEBA) trust established in May of 2004. The district is not required to legally adopt a budget that carries the force of law. Accordingly, the district's budget is not contained within this report.

The district adopts an annual budget for purposes of planning and management control. The budget process involves preparation of a proposed operating and capital budget by district staff for the ensuing year that is presented to the Board of Commissioners. During workshop sessions that are open to the public, the staff and board review and revise the proposed budget. A public hearing is conducted to obtain ratepayer comments. The budget is approved by the board and becomes the basis for operations for the ensuing calendar year.

Local Economy

In the past, Mason County's economy has been traditionally based on the forest products industry. However, at this time the government sector employs the most people in the county; over 3,139 employees at last count, spread among 13 of the county's top 50 employers, according to the Mason County Economic Development Council. The EDC's analysis shows Little Creek Casino Resort holds the top spot for most employees at 696. Five of the other top ten employers are in the government sector, including Washington Corrections Center, Shelton School District, Mason General Hospital, Mason County, and North Mason School District.

The forest products industry has eight of the top 50 spots for number of employees in Mason County with 1,328 employees. Simpson is the largest at 400 employees, while Hiawatha Corporation, with 40 employees, is the world's largest manufacturer of Christmas wreaths. Mason County Public Utility District No. 3 ranks 17 with 114 employees.

According to information from the Economic Development Council of Mason County, the unemployment rate for Mason County in 2006 was 5.9 percent, somewhat higher than the state average. The population of Mason County in 2006 is estimated at 53,100, which is a 7 percent increase since 2000.

Long-Term Financial Planning

The district adopted a five-prong approach to deal with the 2001 energy crisis that included a serious threat of increased Bonneville Power Administration wholesale rates. A 15 percent retail rate went into effect in May 2001; \$28 million was borrowed during 2001 and 2002 to help fund needed capital projects; the operating budget was cut; the level of reserves was reduced; and customers were asked to make all possible efforts to conserve energy locally. While the concern about continued BPA rate increases has not subsided, this plan of dealing with the continuing energy situation seems to have worked well for the district. Many neighboring utilities have adopted much higher rate increases than Mason County PUD No. 3.

After much analysis and study in early 2005, three rate increases of 3 percent on average were adopted by the Board of Commissioners for June 2005, April 2006 and October 2006. The district's rates still compare favorably with other utilities of similar size in the state.

Cash Management and Investments

The district invests its available funds in a manner that minimizes the district's risk of financial loss and maintains necessary liquidity. State law and the district policy permit investing in direct obligations of the U.S. government and its agencies, the State Treasurer's Local Government Investment Pool, certificates of deposit with banks that are qualified public depositories, and other investments allowed by state law.

Risk Management

The district maintains a comprehensive insurance program that includes liability and standard insurance coverage for personal property, automobile, public officials and equipment. The district has elected to become self-insured for all coverages except unemployment insurance. The district is a member of the Public Utility Risk Management Services Self-Insurance Fund, which is currently composed of 19 members. Additional information on the district's risk management program is included in Note 14 of the Notes to the Financial Statements.

Acknowledgements

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to Mason County Public Utility District No. 3 for its comprehensive annual financial report for the fiscal year ending December 31, 2004 and fiscal year ending December 31, 2005. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

Preparation of the Comprehensive Annual Financial Report was made possible by the dedicated service of the entire staff of the Finance and Public Information Departments of the district. We wish to express our appreciation to these staff members for their contributions to the development of this report. Further appreciation is extended to the Board of Commissioners for its leadership and support in planning and conducting the financial operations of the district in a responsible and enterprising manner.

Respectfully submitted,



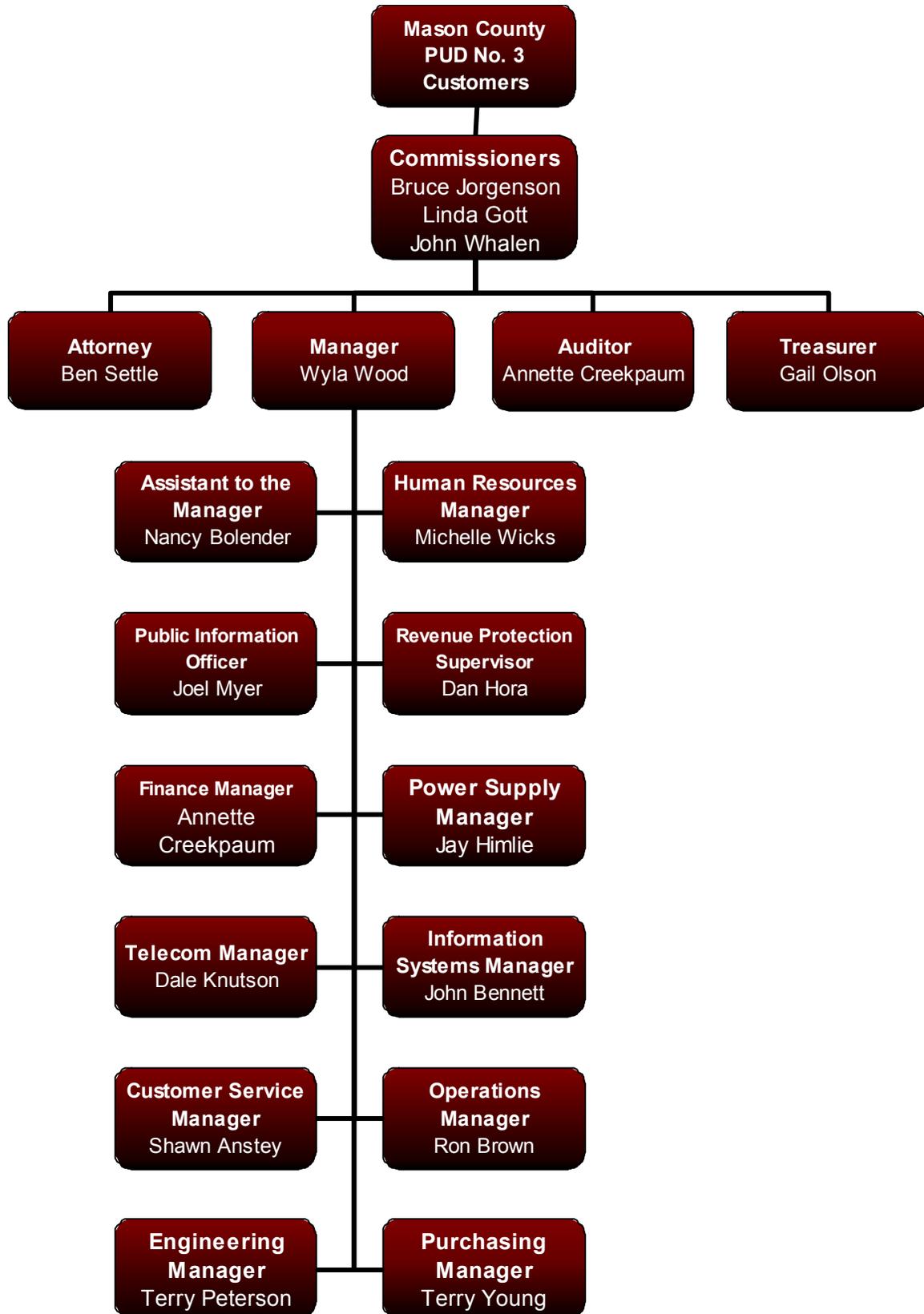
Wyla Wood
Manager



Annette Creekpaum
Finance Manager/Auditor

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington

ORGANIZATIONAL CHART FOR MASON COUNTY PUD No. 3



**MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington**

P. O. Box 2148
307 West Cota Street
Shelton, Washington 98584
360-426-8255
www.masonpud3.org

Board of Commissioners:

Bruce E. Jorgenson, President, took office 1995
Linda R. Gott, Vice President, took office 1999
John H. Whalen, Secretary, took office 1983

Attorney:

Settle & Johnson
P. O. Box 1400
Shelton, WA 98584
360-426-9728

Key District Management:

Wyla Wood, Manager
Annette Creekpaum, Finance Manager/Auditor
Michelle Wicks, Human Resources Manager
Ron Brown, Operations Manager
Terry Peterson, Engineering Manager
Gail A. Olson, Treasurer
Shawn Anstey, Customer Services Manager
Jay Himlie, Power Supply Manager
Terry C. Young, Purchasing Manager
Nancy Bolender, Assistant to the Manager
John Bennett, Information Services Manager
Joel Myer, Public Information Officer
Dale Knutson, Telecommunications Manager



Mason County PUD No. 3 Commissioners, 2006

Bruce Jorgenson, President • Linda Gott, Vice President • John Whalen, Secretary

PUD 3

FINANCIAL SECTION



Legislative Building
P.O. Box 40021
Olympia, Washington 98504-0021

(360) 902-0370
FAX (360) 753-0646
TDD Relay 1-800-833-
6388
<http://www.sao.wa.gov>

INDEPENDENT AUDITOR'S REPORT

June 7, 2007

Board of Commissioners
Public Utility District No. 3 of Mason County
Shelton, Washington

We have audited the accompanying financial statements of the business-type activities and aggregate remaining fund information of the Public Utility District No. 3 of Mason County, Mason County, Washington, as of and for the year ended December 31, 2006, as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and aggregate remaining fund information of the Public Utility District No. 3 of Mason County, Mason County, Washington, as of December 31, 2006, and the respective changes in financial position and, where applicable, cash flows thereof, for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 14 through 16 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.

The information identified in the table of contents as the Introductory and Statistical Sections is presented for purposes of additional analysis and is not a required part of the basic financial statements of the District. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

Sincerely,

A handwritten signature in black ink, appearing to read "Brian Sonntag".

BRIAN SONNTAG, CGFM
STATE AUDITOR

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3

Shelton, Mason County, Washington

Management's Discussion and Analysis

The following discussion and analysis of the financial results of Mason County Public Utility District No. 3 (the district) provide an overview of the utility's financial activities for the year ended December 31, 2006. This discussion is designed to be used in conjunction with the financial statements and notes, which follow this section.

Financial Highlights

The Bonneville Power Administration (BPA), a federal power marketing agency, supplied most of the district's power resources in 2006. BPA continues to be the lowest cost source of wholesale power in the region. The district has a contract for power through September 30, 2011. The District entered a new BPA rate period on October 1, 2006. All previous Cost Recovery Adjustment Clauses (CRAC's), Load Based, Financial Based and Safety Net, were eliminated under the new rate schedule; however, the new base rate without surcharges is approximately equal to the previous rate with all surcharges in place.

The new rate only contains one CRAC, triggered by a shortfall in the Accumulated Modified Net Revenues (AMNR). There are also two potential surcharges which may be added to the CRAC: the National Marine Fisheries Service, Federal Columbia River Power System, Biological Opinion Adjustment (NFB Adjustment), triggered by Endangered Species Act (ESA) related cost increases; and an Emergency NFB surcharge, triggered under the same conditions as the normal NFB Adjustment, but requiring collection of the funds sooner than the NFB Adjustment notification requirements will allow. BPA does not anticipate that the AMNR-CRAC or either of the surcharges will be applied in 2007.

In 2006, the district entered into an agreement with the BPA to provide a financial tool that addresses the issue of guaranteeing BPA's annual payments to the U.S. Treasury on market rate loans for capital projects such as construction of transmission lines and improvements to generating facilities. If implemented, this financial tool would require the district to prepay up to three months of its wholesale electricity bills. This agreement is not a loan as BPA must, within 120 days after prepayment of the bills, credit succeeding power bills until the prepayment and discount amounts are fully repaid. By participating in the agreement, the chance of surcharges (such as the Safety Net Cost Recovery Adjustment Clause) being implemented by BPA due to cash flow issues are eliminated. In addition to stabilizing wholesale power rates through surcharge avoidance, the district also benefits by: 1) receiving a rate of return of .5 percent higher than U.S. Treasury rate on the amount prepaid on the wholesale power bills; and 2) receiving a Priority Firm (PF) rate reduction of approximately 33 cents per megawatt hour whether or not the prepayment agreement is implemented. BPA reimburses the district the cost of the financing vehicle for advancing the funds, up to one percent of its face value per year. The agreement is in effect through 2009.

The district buys a small amount (two megawatts) of power from Energy Northwest as renewable energy, or green power, produced by the Nine Canyon Wind Farm Project (Phase I and Phase II) near Kennewick, Washington. The District signed a Power Purchase Agreement (PPA) for one megawatt of capacity from Phase III of the Nine Canyon Wind Project. Another potential 50 MW wind farm in Reardan, Washington, is also being investigated by Energy Northwest. The district has also expressed preliminary interest in this project.

During 2005, Energy Northwest announced another potential project in which the district may be interested. In April 2006, it announced investigation of a 600 MW integrated gasification combined cycle (IGCC) facility near Kalama, Washington. This project has since been named the Pacific Mountain Energy Center (PMEC).

Mason County PUD No. 3's retail kilowatt hour sales increased by 5 percent in 2006, up from the 3 percent increase in 2005.

The district grew in customers at a lower rate than the previous year by adding 821 new service connections compared to 895 in 2005. Slightly more than 19 miles of primary electric lines were added in 2006, bringing the total to 1,667 miles. Wholesale telecommunications efforts include eight retail internet service providers in the county providing services to 386 connections over 354 miles of fiber optic cable.

Financial Analysis

Overall, the district's financial position has improved, as evidenced by a \$1,391,000 increase in net assets. The following information provides analysis of the 2006 and 2005 comparative financial information provided in the following table:

Condensed Financial Information for December 31, 2006 and 2005 (In Thousands)

	<u>2006</u>	<u>2005</u>	<u>Change</u>	<u>Change</u>
<u>Statement of Net Assets</u>				
Current Assets and Special Funds	\$ 18,570	\$ 19,796	\$ (1,226)	(6.19%)
Net Capital Assets	107,102	105,753	1,349	1.28%
Other Noncurrent Assets	418	451	(33)	(7.32%)
Total Assets	<u>126,090</u>	<u>126,000</u>	<u>90</u>	<u>0.07%</u>
Current Liabilities	11,265	10,659	606	5.69%
Noncurrent Liabilities	28,758	30,665	(1,907)	(6.22%)
Total Liabilities	<u>40,023</u>	<u>41,324</u>	<u>(1,301)</u>	<u>(3.15%)</u>
Invested in Capital Assets, Net of Debt	78,156	74,406	3,750	5.04%
Unrestricted	7,911	10,270	(2,359)	(22.97%)
Total Net Assets	<u>86,067</u>	<u>84,676</u>	<u>1,391</u>	<u>1.64%</u>
Total Liabilities and Net Assets	<u>\$ 126,090</u>	<u>\$ 126,000</u>	<u>\$ 90</u>	<u>0.07%</u>
<u>Statement of Revenue, Expenses and Changes in Net Assets</u>				
<u>Operating Revenues</u>				
Utility Sales and Service Fees	\$ 41,036	\$ 38,034	\$ 3,002	7.89%
Other	2,372	2,185	187	8.56%
<u>Nonoperating Revenues</u>				
Interest Income	594	457	137	29.98%
Other Income	841	145	696	480.00%
Total Revenue	<u>44,843</u>	<u>40,821</u>	<u>4,022</u>	<u>9.85%</u>
<u>Operating Expenses</u>				
Power Supply	22,161	21,096	1,065	5.05%
Operation and Maintenance	13,837	12,059	1,778	14.74%
Taxes/Depreciation Expense	5,880	5,608	272	4.85%
<u>Nonoperating Expenses</u>				
Other Expense	16	15	1	6.67%
Interest Expense	1,558	1,645	(87)	(5.29%)
Total Expenses	<u>43,452</u>	<u>40,423</u>	<u>3,029</u>	<u>7.49%</u>
Change in Net Assets	1,391	398	993	249.50%
Net Assets -beginning of year	84,676	84,278	398	0.47%
Net Assets -end of year	<u>\$ 86,067</u>	<u>\$ 84,676</u>	<u>\$ 1,391</u>	<u>1.64%</u>

Assets

Current assets and special funds decreased by \$1.23 million during 2006 primarily due to the decision to pay for capital construction from reserves built up as a result of \$28 million new debt in 2001 and 2002.

At December 31, 2006, the district had \$107.1 million invested in utility capital assets, up \$1.35 million from the previous year. The Johns Prairie substation project was completed with the installation of approximately four miles of transmission lines from the Mountain View substation to the Johns Prairie site. This project improves reliability and will help accommodate growth in that area of the county. Several other large projects including the Terrace Heights rebuild, the Morgan Road rebuild, the Port of Shelton and the Ballow Road underground rebuild were completed in 2006.

Additional information on Mason County PUD 3's capital assets can be found in Note 2 on page 26 of this report.

Liabilities

Current liabilities increased \$606,000 in 2006 over the previous year. Long-term debt (shown as Revenue Bonds under Noncurrent Liabilities) was reduced by fiscal agent payments of \$1.91 million during 2006 from \$30.67 to \$28.76 million. \$1.9 million in fiscal agent payments will pay down the revenue bonds in 2007.

Additional information on Long Term Debt of the district can be found in Note 6 on page 29 of this report.

Operating Revenues

Utility Sales and Service Fees increased \$3.0 million over the prior year. The number of customers at year end grew to 31,528 in 2006, an increase of 698 over 2005. Retail sales to customers were up nearly 28 million kilowatt hours from the prior year. Other revenues increased \$187,000 over 2005 figures.

Operating Expenses

Purchased power increased in 2006 by \$1.1 million. This was a 5 percent increase over the previous year. Operating and maintenance expenses increased by \$1.78 million, or 15 percent, from the previous year. Taxes and depreciation increased \$272,000 for 2006.

Nonoperating Revenues and Expenses

The Other Nonoperating revenues increased by \$1,000 in 2006 and Interest Expense decreased by \$87,000. Total expenses increased by \$3.03 million over 2005.

Net Assets

Net Assets increased by \$1.39 million in 2006. Year end net assets totaled \$86.07 million.

Requests for Information

The basic financial statements, notes and management discussion and analysis are designed to provide a general overview of the district's finances. Questions concerning any of the information provided in this report should be directed to the Finance Manager of Mason County Public Utility District No. 3, P. O. Box 2148, Shelton, Washington 98584.

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington

STATEMENT OF NET ASSETS

FOR THE YEAR ENDING DECEMBER 31, 2006

ASSETS

Current Assets

Cash and Cash Equivalents (Note 3)	\$ 11,174,472
Investments	999,970
Accounts Receivable	3,910,067
Less: Uncollectibles	(10,989)
Plant Material & Oper. Supplies	2,460,844
Prepayments	23,803
Interest & Dividend Receivable	12,416
Total Current Assets	<u>18,570,583</u>

Noncurrent Assets

Deferred Charges (Note 8)	417,705
Capital Assets	
Land	2,085,382
Plant	120,471,116
Structures and Improvements	6,369,271
Machinery and Equipment	14,195,158
Construction Work in Progress (Note 4)	8,978,576
Less: Accumulated Depreciation	<u>(44,997,863)</u>
Total Capital Assets (Net) (Note 2)	107,101,640
Total Noncurrent Assets	107,519,345
TOTAL ASSETS	<u><u>\$ 126,089,928</u></u>

The accompanying notes are an integral part of the financial statement.

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington

STATEMENT OF NET ASSETS

FOR THE YEAR ENDING DECEMBER 31, 2006

LIABILITIES

Current Liabilities

Current Portion Long-Term Debt	\$ 1,903,946
Warrants Payable	190,726
Accounts Payable	4,284,564
Customer Deposits	361,712
Taxes Accrued	854,951
Interest Accrued - Long Term Debt	149,995
Other Current & Accrued Liabilities	<u>3,516,427</u>
Total Current & Accrued Liabilities	11,262,321

Noncurrent Liabilities

Revenue Bonds	30,664,569
Subtotal Noncurrent Liabilities	30,664,569
Less: Portion Maturing Within One Year	<u>(1,903,946)</u>
Total Noncurrent Liabilities	28,760,623

TOTAL LIABILITIES 40,022,944

Net Assets

Invested in Capital Assets, Net of Debt	78,156,415
Restricted	-
Unrestricted	<u>7,910,569</u>
Total Net Assets	86,066,984
TOTAL NET ASSETS AND LIABILITIES	<u><u>\$ 126,089,928</u></u>

The accompanying notes are an integral part of the financial statement.

PUD 3

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington

**STATEMENT OF REVENUES, EXPENSES
AND CHANGES IN FUND NET ASSETS**

FOR THE YEAR ENDING DECEMBER 31, 2006

Operating Revenues

Utility Sales and Service Fees	\$ 41,036,115
Other Charges for Services	2,230,546
Miscellaneous Operating Revenues	141,803
Total Operating Revenue	43,408,464

Operating Expenses

Purchased Power	22,160,973
Operation	3,087,790
Maintenance	4,389,822
Customer Accounts	1,482,642
Customer Service, Info., Advertising	776,217
Administrative & General	3,561,293
Maintenance of General Plant	539,625
Depreciation	4,259,505
Taxes Other than Income	1,620,619
Total Operating Expenses	41,878,486

OPERATING INCOME	1,529,978
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Nonoperating Revenues (Expenses)

Revenue from Merchandising	16,749
Cost of Merchandising	(16,670)
Interest Income	594,197
Interest and Amortization on Long Term Debt	(1,558,056)
Other Nonoperating Revenues	824,662
Total Nonoperating Revenues (Expenses)	(139,118)

Change in Net Assets	1,390,860
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Total Net Assets, January 1	84,676,124
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Total Net Assets, December 31	\$ 86,066,984
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The accompanying notes are an integral part of the financial statement.

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDING DECEMBER 31, 2006

Cash Flows From Operating Activities:

Cash received from customers	\$ 44,535,285
Cash payments to suppliers	(26,065,317)
Cash payments to employees	(10,107,080)
Taxes Paid	(2,930,636)
Misc. other revenue	824,661
Net cash provided by operating activities	<u>6,256,913</u>

Cash Flows From Noncapital Financing Activities:

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Cash Flows From Capital Financing Activities:

Interest paid on revenue bonds	(1,533,350)
Deferred credits	515,216
Acquisition and construction of capital assets	(5,607,788)
Principal payments on long term debt	(1,817,997)
Net cash used for capital financing activities	<u>(8,443,919)</u>

Cash Flows From Investing Activities:

Sale of Investments	2,517,376
Interest received on investments	602,627
Net cash flow provided by investing activities	<u>3,120,003</u>

Net Increase (Decrease) in Cash 932,997

Cash and Cash Equivalents at Beginning of Year 10,241,475

*Cash and Cash Equivalents at End of Year
(including Cash and Cash Equivalents and
Bond Surety Reserve) \$ 11,174,472

*Cash and cash equivalents represent investments

The accompanying notes are an integral part of the financial statement.

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
Shelton, Mason County, Washington

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDING DECEMBER 31, 2006

Cash Flows From Operating Activities:

Net Operating Income	\$ 1,529,978
Adjustments to reconcile operating income to net cash provided by operating activities:	
Merchandising - Net	79
Customer Deposits	(623)
Depreciation	4,259,503
Customer Accounts Receivable	(299,221)
Miscellaneous	811,110
Other Accounts Receivable	59,226
Uncollectibles	(602)
Material Inventory	(113,965)
Prepayments	252
Outstanding Warrants	(1,398,912)
Accounts Payable	1,059,846
Taxes Accrued	57,322
FICA & FWT Taxes Payable	-
Misc. Accrued Liabilities	292,920
Total Adjustments	<u>4,726,935</u>
Net Cash Provided by Operating Activities	<u>\$ 6,256,913</u>

The accompanying notes are an integral part of the financial statement.

**VEBA FOR EMPLOYEES OF WASHINGTON
PUBLIC UTILITY DISTRICTS TRUST**

STATEMENT OF FIDUCIARY NET ASSETS

FOR THE YEAR ENDING DECEMBER 31, 2006

	<u>2006</u>
<u>ASSETS</u>	
Cash and Cash Equivalents	\$ -
Registered Investments in Vanguard Group Funds	<u>1,899,156</u>
	1,899,156
 <u>LIABILITIES</u>	 -
 NET ASSETS	 <u><u>\$ 1,899,156</u></u>

The accompanying notes are an integral part of the financial statement.

**VEBA FOR EMPLOYEES OF WASHINGTON
PUBLIC UTILITY DISTRICTS TRUST**

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

FOR THE YEAR ENDING DECEMBER 31, 2006

	<u>2006</u>
<u>ADDITIONS:</u>	
Contributions	\$ 495,126
Net Investment Income	<u>190,860</u>
Total Additions	685,986
 <u>DEDUCTIONS:</u>	
Benefits paid to or for participants	<u>307,054</u>
Total Deductions	307,054
 NET INCREASE IN PLAN ASSETS	 378,932
 NET ASSETS	
Beginning of year	1,520,224
End of Year	<u><u>\$ 1,899,156</u></u>

The accompanying notes are an integral part of the financial statement.

MASON COUNTY PUBLIC UTILITY DISTRICT NO. 3
NOTES TO FINANCIAL STATEMENT
January 1, 2006 through December 31, 2006

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

NOTE 1 - Summary of Significant Accounting Policies

The accounting policies of Mason County Public Utility District No. 3 conform to generally accepted accounting principles as applicable to proprietary funds of governmental utilities. The following is a summary of the more significant policies (including identification of those policies which result in material departures from generally accepted accounting principles).

- a. Reporting Entity - Mason County Public Utility District No. 3 is a customer-owned utility providing electrical and wholesale telecommunications service in Mason County, Washington.

Formed by a vote of the people in 1934, the utility is a municipal corporation organized under the laws of the state of Washington. It is legally and fiscally independent of other state or local governments. It began electrical service during 1939.

A board of three commissioners elected by the voters serves the PUD to establish policy, review operations and approve plans, budgets and expenses. The legal responsibilities and powers of the PUD, including the establishment of rates and charges for services rendered, are exercised through the commission.

Mason County PUD No. 3 provides electric service to 31,528 customers as of December 31, 2006.

- b. Basis of Accounting and Presentation - The accounting records of the district are maintained in accordance with methods prescribed by the State Auditor under the authority of Chapter 43.09 RCW. Accounts are maintained in accordance with the uniform system of accounts of the Federal Energy Regulatory Commission.

The district uses the full-accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Capital asset purchases are capitalized and long-term liabilities are accounted for in the appropriate funds.

The district, in accordance with Governmental Accounting Standards Board (GASB) Statement No. 20, Accounting and Financial Reporting Proprietary Fund Accounting, elected not to apply all statements of the Financial Accounting Standards Board issued subsequent to November 30, 1989. In 2002, the district implemented GASB 33 which requires revenue recognition when requirements and purpose are met on customer contributions. It has been determined that currently all contributions in aid of construction will be treated as exchange transactions. The district implemented GASB 34 in 2003, requiring the Balance Sheet to be restated in terms of Statement of Net Assets. Also a Management's Discussion and Analysis precedes the financial statements as required supplementary information under GASB 34.

- c. Cash and Cash Equivalents - The district considers all highly liquid investments maturing within three months to be cash equivalents.
- d. Utility Plant and Depreciation - See Note 2 page 26.
- e. Restricted Assets - None.
- f. Receivables - Estimated electric sales write-offs are charged to bad-debt expense and credited to accumulated provision for uncollectibles. Accounts that are determined to be uncollectible by the utility are turned over to a collection agency but remain in accounts receivable until it is determined there is no possibility of collection. They are then charged against the provision for uncollectibles.
- g. Inventories - Inventories are valued at average cost which approximates the market value.
- h. Investments - See Note 3 page 27.
- i. Personal Time Off (PTO) - The district accrues accumulated unpaid personal time off benefits as amounts earned. PTO includes vacation, sick leave and other leave. PTO, which may be accumulated up to 120 days, is payable upon resignation, retirement, or death. The liability increased \$109,483 from 2005 to 2006 leaving a balance of \$1,598,922 as of December 31, 2006 compared to \$1,489,439 at year end 2005. The amount of PTO due within one year is equal to the 2006 end balance of \$1,598,922. The liability for unpaid personal time off appears on the Statement of Net Assets under Other Current & Accrued Liabilities.

- j. Unamortized Debt Expense - Costs relating to the sale of bonds are deferred and amortized over the lives of the various bond issues. See Note 8 page 31.
- k. Separate fund financial statements are provided for the proprietary fund and the fiduciary fund.
- l. Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the district's enterprise fund, the electric enterprise fund, are charges to customers for sales and services. The district also recognizes as operating revenue the portion of connection fees intended to recover the cost of connecting new customers to the system. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation of capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.
- m. The fiduciary fund represents a trust held for employees in a Voluntary Employees' Beneficiary Association (VEBA) as described in Note 18 on page 39.

NOTE 2 - Utility Plant and Depreciation

Major expenses for capital assets and major repairs, in excess of \$500, that increase useful lives are capitalized. Maintenance, repairs and minor renewals are accounted for as expenses when incurred.

Utility plant in service and other capital assets are recorded at cost. When operating property is retired or otherwise disposed of, the original cost is removed from the utility plant accounts and from accumulated depreciation. Accumulated depreciation is charged or credited with a gain or loss on disposition. This policy is not in accordance with generally accepted accounting principles.

The district's Continuing Property Records System reflects the recording of property units added and retired. Depreciation is computed on the straight-line method with useful lives of 4 to 50 years. Initial depreciation on utility plant is recorded in the year it is classified.

Utility Plant Activity For Year Ending December 31, 2006

Plant Assets	Beginning Balance	Increase	Decrease	Ending Balance
Capital Assets Not Being Depreciated:				
Land	\$ 2,085,382	\$ -	\$ -	\$ 2,085,382
Construction Work in Progress	8,788,219	190,357	-	8,978,576
Total Not Being Depreciated	10,873,601	190,357	-	11,063,958
Capital Assets Being Depreciated:				
Olympic View Generating Plant	6,197,934	33,487	-	6,231,421
Transmission Plant	4,795,169	125,794	58,496	4,862,467
Distribution Plant	119,155,442	4,916,139	497,224	123,574,357
General Plant	6,317,285	498,037	448,022	6,367,300
Total Utility Plant Being Depreciated	136,465,830	5,573,457	1,003,742	141,035,545
Less Accumulated Depreciation for:				
Olympic View Generating Plant	888,204	214,355	-	1,102,559
Transmission Plant	1,302,737	152,302	(74,433)	1,380,607
Distribution Plant	33,233,892	3,498,329	(625,523)	36,106,698
General Plant	6,161,238	618,888	(372,127)	6,407,999
Total Accumulated Depreciation	41,586,071	4,483,875	(1,072,083)	44,997,863
Total Utility Plant Being Depreciation (net)	94,879,759	1,089,582	(68,341)	96,037,682
Total Utility Plant (net)	\$105,753,360	\$ 1,279,939	\$ (68,341)	\$107,101,640

NOTE 3 - Deposits and Investments

As required by state law, all deposits and investments of the district's funds are obligations of the U.S. Government and its Agencies, certificates of deposit, general obligations of Washington State municipalities (the State Treasurer's Investment Pool), passbook accounts and deposits with Washington State banks and savings and loan associations, or other investments allowed by Chapter 39.59 RCW.

The district's deposits and certificates of deposit are entirely covered by federal depository insurance (FDIC and FSLIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

All temporary investments are stated at cost plus accrued interest which approximates fair value. Fair value of these investments as of December 31, 2006, was \$12,161,627. Management intends to hold the time deposits and securities until maturity.

Cash and Temporary Investments For Year Ending December 31, 2006

Investment Type	Carrying Amount	Fair Value
Time Deposits	\$ 394,829	\$ 395,311
Cash & Cash Equivalents	6,100,404	6,100,946
Investment in State Treasurer's Investment Pool	4,679,239	4,679,239
U.S. Government Agency Securities	999,970	986,131
Total Investments	\$ 12,174,442	\$ 12,161,627

It is the district's policy to invest all temporary cash surpluses. At December 31, 2006, the treasurer was holding \$394,829 in time deposits for fiscal agent payments and \$6,100,404 in short-term residual investments and surplus cash. The amount is classified on the balance sheet as cash and cash equivalents in various funds. The district also had investments of \$4,679,239 in the Washington State Treasurer's Local Government Investment Pool and \$999,970 in U.S. Government Agency Securities.

The amounts reported as cash and cash equivalents also include compensating balances maintained with certain banks in lieu of payments for services rendered.

Interest rate risk. In accordance with its investment policy, the district manages its exposure to declines in fair values by matching investment maturities to meet anticipated cash flow requirements.

Credit risk. The district's investment policy conforms with state law which restricts investments of public funds to debt securities and obligations of the U.S. Treasury, U.S. Government agencies, and certain other U.S. Government sponsored corporations, certificates of deposit and other evidences of deposit at financial institutions qualified by the Washington Public Deposit Protection Commission (PDPC), bankers' acceptances, investment-grade general obligation debt of state and local governments and public authorities, and Washington State Treasurer's Local Government Invest Pool (LGIP). The LGIP is an unrated 2a7-like pool and investments in the LGIP are reported based on the pool's share price. The reported value of the pool is the same as the fair value of the pool shares. The LGIP is governed by the State Finance Committee and is administered by the State Treasurer. The district's investment in the Federal Home Loan Mortgage Corporation is rated AAA by Moody's Investor Services and AAA by Standard & Poor's.

Custodial credit risk – Deposits. For a deposit, this is the risk that in the event of a bank failure, the district's deposits may not be returned to it. The district's deposits and certificates of deposit are entirely covered by the Federal Depository Insurance Corporation (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the PDPC. Under Washington State law, public depositories under the PDPC may be assessed on a prorated basis if the pool's collateral is insufficient to cover a loss. As a result, deposits covered by collateral held in the multiple financial institution collateral pool are considered to be insured. State law requires that deposits may only be made with institutions that are approved by the PDPC.

NOTE 4 - Construction in Progress

Construction in progress represents expenses to date on projects totaling \$8,978,576 at year end. Some of these projects were started prior to the beginning of 2006 and are still in progress.

2006 Construction in Progress For Year Ending December 31, 2006

Description	Work Order	Expended
Johns Prairie New Substation	WF0059664	\$ 1,661,609
Johns Prairie Getaways	WF0111428	160,224
Morgan Road Rebuild	WF0074819	196,782
Shelton Matlock Road Rebuild	WF0078612	152,135
Grapeview Loop Rebuild	WF0092568	102,465
Subtotal		2,273,215
Various Projects Under \$100,000		6,705,361
Work in Progress Balance		\$ 8,978,576

NOTE 5 - Lease Commitments

Capital Leases: The district had no capital leases during 2006.

Operating Leases: The district is committed under operating leases for personal computers. These leases are considered operating leases for accounting purposes. Lease expenses for the year ended December 31, 2006 amounted to \$55,665. New leases were entered into in April 2006 and December 2006 for personal computers; these new leases replaced expired leases. Future minimum rental commitments for all operating leases are as follows for the years indicated:

Year	Amount
2007	\$ 48,638
2008	12,443
2009	4,650
Total	\$ 65,731

NOTE 6 - Long Term Debt

The following is a list of the revenue bond debt activity and year end summary as of December 31, 2006. The original amounts of the remaining five revenue bonds totaled \$37,935,000 and the funds were used for the acquisition and construction of major capital facilities:

Revenue Bond Debt Activity For Year Ending December 31, 2006

Issue	Beginning Balance	Added	Redeemed	Ending Balance	Amounts Due Within One Year
1997 Electric Revenue Bonds, due in annual installments of \$25,000 - \$265,000 through July 1, 2011; interest at 4.05% - 5.2%	\$ 1,405,000	-	\$ 205,000	\$ 1,200,000	\$ 215,000
1998 Electric Revenue Bonds, due in annual installments of \$115,000 - \$800,000 through December 1, 2012; interest at 3.75% - 4.75%	4,925,000	-	615,000	4,310,000	640,000
2001 Electric Revenue Bonds, due in annual installments of \$400,000 - \$845,000 through December 1, 2021; interest at 4.375% - 5.10%	9,600,000	-	420,000	9,180,000	440,000
2001A Electric Revenue Bonds, due in annual installments of \$469,196 - \$750,279 through December 1, 2011; interest at 3.75%	3,967,565	-	577,997	3,389,568	608,946
2002 Electric Revenue Bonds, due in annual installments of \$210,000 - \$4,070,000 through December 1, 2021; interest at 4.45% - 5.10%	12,585,000	-	-	12,585,000	-
Total Long Term Debt	\$ 32,482,565	-	\$ 1,817,997	\$ 30,664,568	\$ 1,903,946

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

Annual Requirements to Amortize all Debts Outstanding For Years Ending December 31, 2006

Year	Principal	Interest	Total
2007	\$ 1,903,946	\$ 1,439,134	\$ 3,343,081
2008	1,996,945	1,357,324	3,354,269
2009	2,090,913	1,270,880	3,361,793
2010	2,407,104	1,180,478	3,587,582
2011	3,160,761	1,074,851	4,235,612
2012-2016	8,810,000	3,916,953	12,726,953
2017-2021	10,295,000	11,864,842	11,920,222
Total	\$ 30,664,669	\$ 11,864,842	\$ 42,529,511

Debt service in subsequent years decreases to an annual total of \$3,214,770 in 2012. Debt service fully matures in the year 2021. The total amount of principal scheduled for repayment on the revenue bonds for 2007 is \$1,906,946.

There is \$394,829 in assets of the district representing sinking fund requirements as contained in various indentures.

There are a number of other limitations and requirements contained in the various bond indentures. The district is in compliance with all significant limitations and restrictions.

Pursuant to bond resolutions, the district elected to purchase a surety bond in lieu of maintaining bond reserve funds to guarantee the principal and interest payments to the bondholders. Accordingly, cash and securities previously held in reserve accounts are now available to meet other obligations of the electric system.

A ten year variable rate term loan for \$6,000,000 from Bank of America was secured to build the Olympic View Generating Station in November 2001. The original interest rate was calculated at 75% of the prime rate and changed with adjustments in the prime rate. From January through February 28 of 2005 the rate was 3.93%. On March 1, it was increased to 4.12% until March 21. It then rose to 4.31% through May 2. From May 3 through June 22 it stayed at 4.50%. Because interest rates continued to increase, on June 23, 2005, a new fixed rate bond was secured from Bank of America with the rate set at 3.75%.

NOTE 7 - Pension Plans

All full-time and qualifying part-time district employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer defined benefit and defined contribution public employee 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, P. O. 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 governments. PERS participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977 and by 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 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 3. PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PERS retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement at any age after 30 years of service, or at age 60 with five years of service, or at age 55 with 25 years of service. The annual 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. If qualified, after reaching age 66 a cost-of-living allowance is granted based on years of service credit and is capped at three percent annually.

Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at age 65 with five years of service, or at age 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 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. There is no cap on years of service credit and a cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index), capped at three percent annually.

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

There are 1,181 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of September 30, 2005:

Retirees and Beneficiaries Receiving Benefits	68,509
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	22,567
Active Plan Members Vested	104,574
Active Plan Members Nonvested	51,004
Total	246,754

Funding Policy - Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at six percent for local government unit employees and do not vary from year to year. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the State Legislature. Under PERS Plan 3, employer contributions finance the defined benefit portion of the plans, 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 rates 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, 2006, were as follows:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
Employer*	3.69%*	3.69%*	3.69%**
Employee	6.00%	3.50%	***

* The employer rates include the employer administrative expense fee currently set at 0.18%.

** Plan 3 defined benefit portion only.

*** Variable from 5% minimum to 15% maximum based on rate selected by the PERS 3 member.

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

	PERS Plan 1	PERS Plan 2	PERS Plan 3
2006	\$15,128	\$169,175	\$49,635
2005	\$11,962	\$94,969	\$27,886
2004	\$10,192	\$67,699	\$19,940

NOTE 8 - Deferred Charges

In accordance with generally accepted accounting principles for regulated businesses, the district has deferred the following costs, some of which will be amortized on the straight line method over 19 years.

These costs resulted from discounts related to the various bond issues and costs deferred on possible future projects.

Deferred Charges	2006
Unamortized Debt Expense - 1997 Bond	\$ 10,092
Unamortized Debt Expense - 1998 Bond	33,192
Unamortized Debt Expense - 2001 Bond	127,376
Unamortized Debt Expense - 2002 Bond	189,054
Preliminary Surveys	57,991
Total	\$ 417,705

NOTE 9 - Association with Energy Northwest

Overview - Energy Northwest (previously Washington Public Power Supply System or WPPSS), a municipal corporation and joint operating agency of the state of Washington, was organized in 1957. It is empowered to finance, acquire, construct and operate facilities for the generation and transmission of electric power. On June 30, 1995, its membership consisted of 11 public utility districts and the cities of Richland, Seattle, and Tacoma. Mason County PUD 3 (hereafter the district) withdrew its membership on September 11, 1984. All members own and operate electric systems within the state of Washington. Energy Northwest has no taxing authority. In July 2001 the district once again became a member of Energy Northwest. Financial statements for Energy Northwest may be obtained by writing to: Energy Northwest, P.O. Box 968, Richland, Washington 99352-0969. A website is available at www.energy-northwest.com.

Nuclear Projects 1, 2, and 3 - The district continues to fulfill its obligation consistent with the terms and conditions of the Net Billing Agreements with Energy Northwest and the Bonneville Power Administration (BPA).

The district purchased 1.262 percent of WPPSS Nuclear Project (WNP) No. 1, 1.446 percent of WNP No. 2, and 1.265 percent of the capability of the Energy Northwest 70 percent ownership share of WNP No. 3. The district in turn sold this capacity to BPA. Under the "Net Billing Agreements," BPA is unconditionally obligated to pay the district, and the district is unconditionally obligated to pay Energy Northwest the pro rata share of the total annual costs of each project, including debt service on revenue bonds issued to finance the projects, whether or not the projects are completed, operable or operating and notwithstanding the suspension, reduction or curtailment of the projects' output.

WNP No. 2 commenced commercial operation in December 1984. In May 1994 the BPA and WPPSS terminated WNP No. 1 and WNP No. 3, subject to repayment of the debt service on the outstanding revenue bonds.

The district's obligations under the Net Billing Agreements are presently scheduled to be fulfilled on WNP No. 2 in 2012, on WNP No. 1 in 2017, and on WNP No. 3 in 2018.

Bonneville Power Administration worked with Energy Northwest to refinance some of the bond issues for the Net Billed Projects which may affect the fulfillment dates.

Packwood Hydroelectric Project - The Packwood Hydroelectric Project is located near Packwood in eastern Lewis County, Washington. The project is a 30 MW peaking resource. Commercial operation began in June 1964.

Under power sales agreements, the Energy Northwest member public utility districts have purchased the project at Packwood. The district has a 10 percent share in the project (participant owners are not equally invested in the project). The participant owners are obligated to pay annual costs of the project, including debt service, whether or not the project is operable, until outstanding bonds are paid, or provision is made for their retirement, in accordance with provisions of the bond resolution. Debt service on the Packwood Hydroelectric Project is scheduled to conclude in 2012.

The participant members commissioned a study of the Packwood Hydroelectric Project by D. Hittle & Associates, Inc. in early October of 1995. This study was initiated because of the proposed changes in BPA's power and transmission rates (1996 Rate Case Proceeding). These rates went into effect October 1, 1996, and had two significant impacts on the net revenues of the Packwood project. First, there was a significant increase in the transmission rate charged Energy Northwest. Second, the new rates dramatically reduce the value of capacity, changed the value of energy by season, and decreased the priority firm rate by approximately eight percent overall. These changes combined with the transmission expenses under the Lewis/Energy Northwest Packwood wheeling contract could result in costs exceeding revenues for years when plant generation is below average. The focus of the study was to evaluate alternatives that may enhance project net revenues over the next five years.

The alternative accepted by the participants was to negotiate a five-year agreement with BPA for the purchase of the plant's generation (output). This simplified the existing agreements, maintaining positive net revenue for average generation, and limited the cost impact on the participants that had previously purchased plant generation.

This agreement between Energy Northwest and BPA was negotiated and accepted by the participants in December 1996. The agreement was retroactive to October 1996 when the new BPA rates went into effect. The plant sold the generation to BPA and BPA was responsible for the transmission costs to the point of delivery (location). The rate for the power was fixed through the year 2001 with an option to continue the arrangement upon agreement of the parties on the payment provisions beyond 2001.

Due to anticipated relicensing costs for Packwood, the Participants Group (of which the district is a member) voted to leave excess revenues in the project operating fund rather than receive a refund payment.

In September of 2002, BPA notified Energy Northwest it was invoking the termination option and would no longer purchase the output from Packwood under terms of the 1996 contract as of October 2002. A contract was signed for two Packwood participants

(Benton and Franklin County PUDs) to purchase the output at cost for one year, and allow the participants time to investigate other options, in September 2003. This contract has been subsequently renewed each year.

Nine Canyon Wind Project – In early 2001 Energy Northwest approached public utilities about developing a wind generation project. In September of 2001, the district signed an agreement with Energy Northwest to purchase a 1 MW share (2.08%) of the Nine Canyon Wind Project.

Nine Canyon Phase I consists of 37 Bonus wind turbines with a peak generating capacity of 48 MW near Kennewick, Washington. The project began commercial operation in October of 2002. As with the Packwood Hydroelectric Project, participants of Nine Canyon are obligated to pay the annual costs of the project, including debt service, whether or not the project is operable, until the outstanding bonds are paid or provision is made for their retirement in accordance with the bond resolution. Bonds in the amount of \$71 million were sold to finance construction of the project and are scheduled to conclude in 2023.

On April 22, 2003, the district agreed to enter into Phase II of the Nine Canyon Wind Project with Energy Northwest and four other participants. Twelve more Bonus wind turbines were erected in the same area as Phase I. They have a peak generating capacity of an additional 15.6 MW. The district's share of Phase I and Phase II will be 2 MW or 3.14%. Bonds in the amount of \$32.9 million were sold to finance the construction of this second phase. Commercial operation of the second phase of this wind generation project began in September 2003.

In December of 2004, Energy Northwest refinanced the Phase I bonds, resulting in a savings of \$5.3 million.

On October 30, 2006, the district agreed to enter into Phase III of the Nine Canyon Wind Project with Energy Northwest and nine other participants. Phase III will consist of fourteen 2.3 MW Siemens (Siemens purchased the Bonus wind turbine company) wind turbines. The new turbines will be erected in the same general area as Phases I & II. They have a peak generating capacity of approximately 32 MW. The district's combined share of all three phases is 3 MW, or approximately 3.14% of the overall capacity of the project. Energy Northwest sold bonds in the amount of \$80 million to finance the construction of Phase III. Commercial operation is planned for March of 2008.

During 2005, Energy Northwest announced several potential new generation projects. The district has indicated preliminary interest in two of these projects. In April it announced investigation of interest in a 600 MW integrated gasification combined cycle (IGCC) facility near Kalama, WA. This project has since been named the Pacific Mountain Energy Center (PMEC).

In July it announced it was investigating a potential new 50 MW wind project near Reardan, Washington, just west of Spokane.

Hanford Generating Project - The Hanford Generating Project (HGP), an 860 MW plant completed in 1966, previously used by-product steam from the Department of Energy's (DOE) dual-purpose New Production Reactor (N-Reactor) and has not operated since the shutdown of the N-Reactor in 1987.

The Secretary of Energy's decision to place the N-Reactor in permanent shutdown eliminated the N-Reactor as an energy source for HGP. Energy Northwest has evaluated alternative energy uses for the plant to no avail. Current options include a transfer to DOE for removal and site restoration, or removal and site restoration by Energy Northwest. At this time the eventual disposition of HGP is unknown. Energy Northwest has reduced the assets of HGP to its net realizable value and has accrued for the estimated cost of removal and site restoration.

Energy Northwest redeemed the remaining HGP bonds in the principal amount of \$6.635 million on September 1, 1992.

NOTE 10 - Power Supply/Power Sales Contract

Bonneville Power Administration - BPA is a federal power marketing agency, established by the Bonneville Power Act of 1937. BPA is part of the U.S. Department of Energy, but is self financing and receives no tax revenues. Its costs are recovered through the revenue it generates. Additionally, the BPA makes annual payments to the U.S. Treasury for money appropriated to the Corps of Engineers and Bureau of Reclamation, or for money borrowed to construct dams, substations, and transmission facilities. About one half of all the power used in the Northwest is sold by the BPA. BPA also has funded fish costs associated with the system of rivers in the Northwest.

The BPA owns no generation resources or distribution facilities. Its function is to market the output of federal resources, and transmit non-federal power over its transmission grid. The U.S. Army Corps of Engineers and the U.S. Bureau of Reclamation operate and maintain 31 hydroelectric projects, which constitute the backbone of the federal base system. The BPA owns and operates approximately 75 percent of the region's transmission capacity.

The BPA sells electric power at wholesale rates to utilities, as well as industrial and governmental customers inside and outside of the Pacific Northwest region.

In May 2000, Bonneville issued a Record of Decision establishing fees and charges for services to be provided to its customers under the new contracts effective October 1, 2001. The Record of Decision included a Cost Recovery Adjustment Clause (“CRAC”), which authorizes Bonneville to impose a surcharge on its power rates (except rates applicable to the Slice product) in order to deal with a number of contingencies that might affect adversely its ability to make required payments of debt service to the U.S. Treasury Department.

That rate structure contained three different CRAC’s: a load based (LB) CRAC, which triggered based on costs related to market purchases to augment the federal base system and sales of surplus power; the financial based (FB) CRAC triggers if BPA’s reserve level falls below \$660 million; and the safety net (SN) CRAC triggers if BPA estimates that it would miss a payment to the U.S. Treasury.

Early in 2001, a combination of factors required BPA to purchase large amounts of power in the open market at the same time those prices were highly inflated. In discussions with customers prior to implementing the LB CRAC, BPA customers agreed to rate adjustments every six months, to allow for more accurate tracking of rapidly changing conditions

Every six months the CRAC levels are recalculated by BPA. At the beginning of 2006, BPA CRAC levels were 24.40% above the October 2001 base rate for the load based CRAC, 4.41% for the financial based CRAC and 1.75% for the safety net CRAC. In April of 2006, the load based CRAC was raised to 28.51% of the base rate, and the financial based CRAC was reduced to 0.45%. The safety net CRAC remained at 4.07%.

Also due to the high cost of market power purchases, BPA asked all customers to reduce their load by 10%. The district signed this “Rate Mitigation Agreement” in June of 2001. In addition to the energy conservation measures taken to reduce load, the district also decided to install generation capacity to help meet the load reduction.

The district secured a term loan for \$6 million to finance the construction of a natural gas generation facility utilizing two 2.3 megawatt Wartsila reciprocating engines. Also, in June of 2001 BPA signed a contract with the district to purchase the output of the generation from completion of the plant (planned for early in 2002) until September 30, 2003. The district signed a contract for gas supply matching the term of the purchase contract with BPA. The district agreed to participate in a BPA pilot program to delay planned transmission line construction on the Olympic Peninsula by operating the generating plant during times of anticipated peak load. BPA publishes an offered price on its Demand Exchange website which the district can accept if the offer is sufficient to purchase gas at spot market prices to operate for the requested period (since our long term contract expired on September 30, 2003.)

The district is free to operate the plant at other times for its own peaking requirements, meeting local utility load, selling into the market, emergency backup or other applications depending on the conditions at the time.

During 2005, BPA issued a draft contract to begin discussions with utilities whose contracts expire in the 2009-2011 time period. While the contract provisions are not final, based on the proposed contract provisions, BPA has indicated that the capacity of the Federal Columbia River Power System (FCRPS) may be reached soon. BPA is proposing to allocate the capacity of the existing FCRPS and maintain the relatively low cost of that resource by requiring any energy purchased in excess of that capacity to be at BPA’s cost of acquiring those additional resources.

Utilities that do not wish to rely on BPA to acquire resources for them at an as yet unknown “second tier” cost will need to acquire or contract for their own resources to meet loads beyond their allocated portion of the FCRPS.

The district entered a new BPA rate period on October 1, 2006. All previous CRAC’s, Load Based and Safety Net, were eliminated under the new rate schedule, however the new base rate without surcharges is approximately equal to the previous rate with all surcharges in place.

NOTE 11 - Litigation

There is no litigation pending or threatened against the district which could have a materially adverse effect upon its financial condition.

NOTE 12 - Bonneville Power Administration Conservation Programs

In October of 2001, the district began participating in several Bonneville Power Administration conservation programs.

The Conservation and Renewables Discount (C&RD) was funded by a one half mill (a mill is one one-thousandth of a dollar, \$.001) surcharge per kilowatt hour purchased from BPA. The district must document spending this amount (approximately \$300,000 per year, based on its 2000 kilowatt hour purchases) on qualifying conservation and/or renewable energy activities during the current rate period (through September of 2006).

Qualifying measures are determined by the Regional Technical Forum (RTF). The RTF is an advisory committee of the Northwest Power Planning Council, established in 1999 to develop standards to verify and evaluate conservation savings. members are appointed by the Council and include individuals experienced in conservation program planning, implementation and evaluation. If the district cannot document this spending, BPA will bill the district for the amount not spent and acquire the resources on its own.

The district successfully completed its obligation under this program and received a “close out” letter from BPA in 2005.

The district also participated in BPA’s Conservation Augmentation program. The district participated in programs to save energy through improvements in the compressed air systems used by large industrial customers (predominantly wood products) and improvements in commercial lighting systems. BPA provides reimbursement under this program unlike the C&RD (for which there is no reimbursement).

During late 2005 and early 2006 BPA held a series of meetings about potential changes to its conservation programs under new power sales contracts which would begin in October of 2006. A Conservation Rate Credit (CRC) program similar to the Conservation and Renewable Discount program and Conservation Acquisition Agreement (CAA) program similar to the Conservation Augmentation program were the result.

In March of 2006, the district signed an Early Adoption Agreement with BPA to begin operating the CRC program prior to the new power sales contract start in October.

In August of 2006, the district signed a Conservation Acquisition Agreement rolling all unused Conservation Augmentation funds into a new budget with additional funds to begin implementation of eligible programs under the CAA.

Both agreements include residential, commercial and industrial conservation measures. The CRC is an obligation under the BPA Power Sales Contract to spend at least \$325,000 per year on qualifying conservation activities without reimbursement. The CAA will reimburse the district up to \$710,000 for conservation measures installed under the CAA.

NOTE 13 - Preliminary Survey and Investigation Charges

Preliminary survey and investigation charges incurred for proposed projects are deferred pending construction of the facility or facilities. Charges relating to projects ultimately constructed are transferred to utility plant and charges relating to abandoned projects are charged to expense.

NOTE 14 - Public Entity Risk Pools

- a. Liability Risk Pool - Public Utility Risk Management Services (“PURMS”) provides liability insurance coverage for its members participating in the Liability Risk Pool (“Liability Pool”) and their employees under an agreement entitled “PURMS Joint Self-Insurance Agreement” (amended and restated as of December 1, 2005, “SIA”). Under the SIA, from 1977 through 1995, the Liability Pool has had a self-insured retention (or “Liability Coverage Limit”) of \$500,000 per occurrence. Effective January 1, 1996, PURMS increased the Liability Coverage Limit to \$1,000,000 per occurrence.

At all times, PURMS also maintains Excess Liability Insurance for its members in the Liability Pool (“Excess Liability Insurance”). For 2006, the amount of the Excess Liability Insurance was \$35,000,000 with coverage attaching at the \$1,000,000 Liability Coverage Limit.

The Liability Pool is financed through assessments of its participating members (“Liability Assessment”) in accordance with the terms of the Liability General Assessment Formula (“Liability Assessment Formula”). Liability Assessments are levied at the beginning of each calendar year to replenish the Liability Pool to the Designated Liability Pool Balance, and at any time during the year that the Actual Liability Pool Balance becomes \$500,000 less than the Designated Liability Pool Balance. For 2006, the Designated Liability Pool Balance was \$2 million. As a result, during 2006, the Liability Pool maintained cash reserves between \$1.5 and \$2 million to pay for Liability Claims and Liability Pool Operational Expenses (“Liability Pool Reserves”).

The total paid for Liability Claims in 2006 was \$529,833 (including attorneys’ fees for defending claims but excluding Liability Pool Operational Expenses).

As of December 31, 2006, there were 216 known incidents and/or unresolved Liability Claims pending against one or more members or former members of the Liability Pool (“Pending Liability Claims”). The total dollar amount of the risk posed by these claims to such members and to the Liability Pool itself is unknown and can only be estimated. However, based on the total of the reserves established by the Administrator for these Pending Liability Claims that had not been paid out as of December 31, 2006, the Administrator estimates that there is approximately \$854,436 of outstanding liabilities to the Liability Pool relating to these claims.

In addition, in accordance with Washington State regulatory requirements applicable to public entity risk pools, on an annual basis, PURMS engages an independent qualified actuary to determine the claim financing levels and liabilities for unpaid claims and claims adjustment expenses for the Liability Pool (“Liability Pool Actuarial Report”). A copy of the Liability Pool Actuarial Report is provided to the Washington State Risk Manager (“State Risk Manager”) and made available to the Washington State Auditor’s Office (“State Auditor”).

Because the total dollar amount of the risk posed by the Pending Liability Claims cannot be known with certainty, no opinion can be provided as to the risk these claims pose to the solvency of the Liability Pool. However, since members participating in the Liability Pool are required under the SIA to pay their Liability Assessments levied any time the money held for the Liability Pools fall more than \$500,000 below the Designated Liability Pool Balance, assuming that these Assessment obligations of members under the SIA are enforceable and that the members are at the time solvent and pay such Assessments, the Liability Pool would have the assets to pay the Pending Liability Claims on behalf of its participating members regardless of the amount of risk such claims pose to the Liability Pool.

- b. Property Risk Pool - Effective April 1, 1997, the commission authorized PUD 3’s participation in the PURMS property risk pool and vehicle coverage.

PURMS provides property insurance coverage for its members participating in the Property Risk Pool (“Property Pool”) in accordance with the terms of the SIA (identified above). Under the SIA, from its inception in 1997 to present, the Property Pool has had a self-insured retention (or “Property Coverage Limit”) of \$250,000 per Property Loss.

At all times, PURMS also maintains Excess Property Insurance for its members in the Property Pool (“Excess Property Insurance”). For 2006, the amount of the Excess Property Insurance was \$150,000,000 with excess coverage attaching at the \$250,000 Property Coverage Limit for all Property Losses except those subject to increased retention levels for certain property risks (“Increased Retentions”).

The Property Pool is financed through Assessments of its participating members (“Property Assessments”) under the Property General Assessment Formula (“Property Assessment Formula”). Property Assessments are levied at the beginning of each calendar year to replenish the Property Pool to the Designated Property Pool Balance, and at any time during the year that the Actual Property Pool Balance becomes \$250,000 less than the Designated Property Pool Balance. From 1997 to November 21, 2002, the Designated Property Pool Balance was \$500,000. As a result, during that period of time, the Property Pool maintained cash reserves between \$250,000 and \$500,000 to pay Property Pool Operational Expenses (“Property Pool Reserves”).

Effective as of November 21, 2002, the Property Pool began providing its members with Automatic Extended Property Coverage for Property Losses that exceed the Property Pool’s \$250,000 Property Coverage Limit if those Losses were also subject to Increased Retentions under the Excess Property Insurance. Pursuant to PURMS Board Resolution No. 11-20-03-2, the Designated Property Pool Balance was increased over time from \$500,000 to \$750,000, and funding for the increased Property Pool Reserves was completed in 2005.

For 2006, the Designated Risk Pool Balance was \$750,000, thereby triggering a Property Assessment any time the Actual Property Pool Balance dropped below \$500,000. Under the Excess Property Insurance retentions effect for 2006, the maximum exposure to the Property Pool from a Property Loss that exceeded \$250,000, and that was subject to an Increased Retention, was \$500,000, less the applicable deductible, or maximum of \$250,000 more than the Property Coverage Limit.

The total paid for Property Claims in 2006 was \$414,443 (excluding attorney’s fees and Property Pool Operational Expenses).

As of December 31, 2006, there were 28 known Property Claims pending from the members of the Property Pool (“Pending Property Claims”). The total dollar value of the risk posed by these claims to the Property Pool is unknown and can only be estimated. However, based on the total of the reserves established by the Administrator for these Pending Property Claims that had not been paid out as of December 31, 2006, the Administrator estimates that there is approximately \$258,960 of outstanding liabilities to the Property Pool relating to these claims.

In addition, in accordance with Washington State regulatory requirements applicable to public entity risk pools, on an annual basis, PURMS engages an independent qualified actuary to determine the claim financing levels and liabilities for unpaid claims and claims adjustment expenses for the Property Pool (“Property Pool Actuarial Report”). A copy of the Property Pool Actuarial Report is provided to the State Risk Manager and made available to the State Auditor.

Because the total dollar amount of the risk posed by the Pending Claims cannot be known with certainty, no opinion can be provided as to the risk these Pending Property Claims pose to the solvency of the Property Pool. However, since members participating in the Property Pool are required under the SIA to pay their Property Assessments levied any time the money held for

the Property Pool falls more than \$250,000 below the Designated Property Pool Balance, assuming that these Assessment obligations of members under the SIA are enforceable and that the members are at the time solvent and pay such Assessments, the Property Pool would have the assets to pay the Pending Property Claims on behalf of its participating members regardless of the amount of the risk such claims pose to the Property Pool.

- c. Health and Welfare Risk Pool - PURMS provides health and welfare insurance coverage for the employees of each of its members participating in the Health and Welfare Risk Pool ("H&W Pool") in accordance with the terms of the Health and Welfare Coverage of the SIA ("H&W Coverage") and the terms of each member's respective Coverage Booklet provided to its employees. The H&W Pool was established as one of PURMS' Risk Pools effective March 31, 2000. The district joined the fund as of January 1, 2002, after being self-insured for a number of years.

Under the terms of the SIA and the H&W General Assessment Formula ("H&W Assessment Formula"), the H&W Pool was initially funded with cash reserves for paying H&W Pool Operational Expenses and H&W Claims ("H&W Pool Reserves") in an amount approximately equal to the sum of three (3) times the amount of each member's historical average monthly H&W Claims experience ("H&W Claims Experience") for its respective employees and their dependents. (Hereinafter, "employees" includes "dependents"). By amendment to the SIA effective December 1, 2005, the H&W Pool Reserves may be established from time to time by Majority Vote of the Board at no lower than 2.5 and no greater than 3.0 times the total of all members' H&W Claims Experience. As of December 31, 2006 the H&W Pool Reserves were established at 2.5 times the total of all members' H&W Claims Experience.

The H&W Pool's operations are financed through assessments of its participating members ("H&W Assessments") in accordance with the H&W General Assessment Formula. Under the H&W Assessment Formula, each month, each member of the H&W Pool is assessed for: (a) the cost the H&W Pool incurred during the preceding month for the H&W Claims for such member's employees ("H&W Claims Costs"); and (b) for such member's share of Shared H&W Costs. "Shared H&W Costs" consist of administrative expenses incurred by the H&W Pool, premiums for Stop-Loss Insurance, PPO charges and Shared H&W Claims. Thus, under the H&W Assessment Formula, each month, the Operational Expenses of the H&W Pool and all members' H&W Claims Costs for that month are paid and the H&W Pool Reserves are fully replenished.

The exposure of each H&W Pool member to the H&W Claims Costs of its employees is limited by two different pairs of stop-loss points ("Stop-Loss Points"). The first pair of Stop-Loss Points is established annually by the Excess Stop-Loss Insurance that the H&W Pool acquires and maintains for its members. These Stop-Loss Points represent the dollar amounts at which the Stop-Loss Insurance attaches and begins paying either the H&W Claim Costs relating to an individual employee's total medical claims for the year ("H&W Pool Individual Stop Loss Point") or the H&W Claims Costs of all employees of all members for the year ("H&W Pool Aggregate Stop Loss Point"). For 2006, the H&W Pool Individual Stop Loss Point was \$150,000 per employee and the H&W Pool Aggregate Stop Loss Point was \$8,200,000 for the combined H&W Claims Costs of the employees of all members of the H&W Pool.

In addition, each H&W Pool member's exposure to the H&W Claims Costs of its employees is further limited by even lower Stop-Loss Points determined by the H&W Pool for its members ("Member Stop-Loss Points"). Medical expenses that exceed these Stop-Loss Points become "Shared H&W Claims" and therefore are assessed as "Shared H&W Costs" which are paid by all H&W Pool members. The "Member" Stop-Loss Points are calculated annually under the H&W Assessment Formula based on the amounts of the Individual and Aggregate Stop-Loss Points established for the year by the Stop-Loss Insurance. As a result of this process, each member is assigned a dollar amount at which any further payments by the H&W Pool on claims for a particular employee constitute Shared H&W Costs ("Member's Individual Stop-Loss Point") and a dollar amount at which any further payments by the H&W Pool on the H&W Claims of all of a member's employees constitute Shared H&W Costs ("Member's Aggregate Stop-Loss Point").

The total paid by the H&W Pool for H&W Claims costs in 2006 was \$6,190,334 (including Shared H&W Claims but excluding H&W Pool Operational Expenses).

As of December 31, 2006, there were no "open" H&W Claims pending for employees of members of the H&W Pool. The actual total exposure of the H&W Pool to H&W Claims Costs at any particular point in time cannot be known with certainty. However, the Administrator estimates that, as of December 31, 2006, the total "incurred-but-not-reported" claims for the H&W Pool was approximately \$400,768 ("IBNR Claims"). State regulatory requirements for an annual audit by an actuary do not apply to the H&W Pool because it maintains Stop-Loss Insurance.

Because IBNR Claims can only be estimated, no opinion can be provided as to the risk those claims pose to the solvency of the H&W Pool. However, since members participating in the H&W Pool are required under the SIA to pay their H&W Assessments levied on a monthly basis to fully replenish the H&W Pool Reserves, assuming that these Assessment obligations of members under the SIA are enforceable and that the members are at the time solvent and pay such Assessments, the H&W Pool would have

the assets to pay the IBNR Claims on behalf of its participating members regardless of the amount of the risk those claims pose to the H&W Pool.

- d. State and Independent Audits – Each of PURMS’ Risk Pools is audited annually by the State Auditor’s Office. In addition, as required by State regulations, PURMS provides quarterly financial reports to the State Risk Manager reflecting the claims and administrative expenses of the Risk Pools, and bi-annually, the State Risk Manager performs its own audit of PURMS’ Risk Pools. Finally, on an annual basis, PURMS engages the services of the accounting firm of Moss Adams to perform a claims audit for each of the Risk Pools.

NOTE 15 - Post Employment Benefits Other Than Pension Benefit

In addition to the pension benefits described in Note 7, the district provides post employment health care benefits, in accordance with the International Brotherhood of Electrical Workers Local Union No. 77 agreement, to employees who retire from the district after a minimum of ten years of service.

The district medical plan pays the same for claims on costs incurred by retirees and their dependents as it does active employees.

Employer contributions are financed on pay-as-you-go basis. Expenses for post-retirement health care benefits are recognized as retirees report claims.

During the year 2006, expenses of \$604,147 were recognized for post-retirement health care, including premiums and claims for all 45 eligible retirees and their eligible dependents.

NOTE 16 - Participation in Northwest Open Access Network, Inc. d.b.a. NoaNet

The district, along with 13 other Washington State Public Utility Districts and Energy Northwest, is a member of NoaNet, a Washington nonprofit mutual corporation. NoaNet was incorporated in February 2000 to provide a broadband communications backbone, over Public Benefit Fibers leased from Bonneville Power Administration. This communications backbone throughout Washington will assist its members in the efficient management of load, conservation and acquisition of electric energy as well as other purposes. The network began commercial operation in January 2001.

In July 2001, NoaNet issued \$27 million in telecommunications network revenue bonds (taxable) to finance the repayment of the founding members and the costs of initial construction, operations and maintenance. The bonds become due beginning in December 2003 through 2016 with interest due semi-annually at rates ranging from 5.05% to 7.09%. Each member of NoaNet has entered into a repayment agreement to guarantee the debt of NoaNet. The district’s guarantee is limited to approximately 10% interest. In addition, in January 2003 NoaNet opened a \$5 million line of credit with Bank of America to fund capital expenses.

The management of NoaNet anticipates meeting debt obligations through profitable operations but it will be necessary for NoaNet to assess members to cover operating deficits during the initial years of operation. The district’s share of assessments and related contributions to NoaNet of \$242,116 and \$242,246 in 2006 and 2005, respectively, has been expensed as incurred. Assessments for 2007 will be determined by the NoaNet board of directors if needed for debt service payments on outstanding bonds.

NoaNet recorded net losses of \$1,979,484 (unaudited) and \$3,252,785 for 2006 and 2005, respectively. The district’s proportionate share of these losses is less than \$200,000 for 2006. Financial statements for NoaNet may be obtained by writing to: Northwest Open Access Network, Corporate Office – Seattle, 21507 42nd Avenue South #J-4, SeaTac, Washington 98198. A website is available at www.noanet.net.

The district’s connection to NoaNet and construction of its local fiber optic loop occurred in June 2001 at a cost of approximately \$3,000,000. In November 2005, four members (including Mason County PUD No. 3) increased their percentage shares in NoaNet by contributing additional funds under a capital contribution agreement. As of December 31, 2006, the district’s percentage interest in NoaNet is 7.88%.

NOTE 17 - Telecommunications Services

The district was a founding member of NoaNet in 1999, so with the passage of wholesale telecommunications authority by the 2000 state legislature, high-speed communication capability was brought to Mason County. The district acts as a wholesaler for several retailers that provide services over the fiber optic network to consumers in the area.

Mason County PUD No. 3 uses its fiber optic network for internal communications, communications with other utilities, and long-haul data transmission via the Northwest Open Access Network. The district leases the capacity in excess of what it needs to retailers.

A summary of telecommunications revenues, expenses and capital investment for 2006 is listed as follows:

Telecommunications Revenues, Expenses and Capital Investment
For the year ending December 31, 2006

Operating Revenue	
Wholesale Fiber Services to ISP	\$ 380,191
Dark Fiber Lease	8,037
Installation Charges	17,051
Total	405,279
Operating Expenses	
Operating Expenses	1,191,635
Depreciation	462,572
Taxes Other than Income	(330)
Total	1,653,877
Nonoperating Revenue	
	63,168
Net Income (Loss)	
	(1,185,430)
Capital Investment	
Current Year Net Plant	(203,668)
Cumulative Net Plant	\$ 8,933,288

NOTE 18 - VEBA Trust

In February 2004 the Board of Commissioners directed the Finance Manager/Auditor to notify MSA Voluntary Employees' Beneficiary Association ("VEBA") that the district would be terminating its membership in the state-wide, employer directed, tax exempt medical savings account trust. Because of concerns regarding the financial difficulties of a company in which a major portion of the trust funds were invested, it was decided to explore other possibilities for a trust. After months of research, on May 11, 2004, the board voted to proceed with implementing a trust for VEBA for employees of Washington PUDs with PUD 3 self-administering the plan. Annette Creekpau, Finance Manager/Auditor, was named as trustee. On May 14, 2004, funds in the amount of \$1,042,089 were transferred from the MSA VEBA investments to the district. They were subsequently transferred for investment in Vanguard Federal Money Market Funds until employees had an opportunity to choose from three Vanguard Fund investment options.

The district has set up a 501 (c)(9) trust with the assistance and advice from an attorney with expertise in this area, and filed the appropriate forms with the IRS to establish the new trust. The trust is administered by the district under supervision of the trustee. The final approval from IRS for the trust was received by the trustee in early 2005. The funds held in trust belong to the employees not the district.

The December 31, 2006 market value of the trust was \$1,899,156. The allocations between investment options were: 22.9% in the Vanguard Federal Money Market Fund, 27.9% in the Vanguard Balanced Fund, and 49.2% in the Vanguard US 500 Stock Fund. During 2006, \$495,126 in contributions from both employees and employer was added; \$307,054 was paid out in 641 claims, and there was a gain of \$190,860 on the investments held in the trust.

STATISTICAL SECTION

Mason County Public Utility District No. 3
Shelton, Mason County, Washington
Financial Results
For the years ending December 31 - Unaudited

	2006	2005	2004	2003	2002
OPERATING REVENUES					
Electric Revenues					
Residential Sales	\$ 26,140,240	\$ 24,051,725	\$ 23,166,516	\$ 22,433,267	\$ 22,366,839
Outdoor Lighting	541,219	515,524	513,330	502,120	506,029
Fixed Rate Facilities	413	564	959	1,199	1,131
Commercial	11,031,717	10,049,534	9,265,698	9,157,959	9,277,119
Large Industrial	2,922,458	3,079,556	2,888,372	2,738,929	2,828,778
Public Authorities	-	-	-	-	-
Sales for Resale	-	-	-	-	-
Total Electric Revenues	<u>\$ 40,636,047</u>	<u>\$ 37,696,903</u>	<u>\$ 35,834,875</u>	<u>\$ 34,833,474</u>	<u>\$ 34,979,896</u>
Generation Revenues					
Sales for Resale	\$ -	\$ -	\$ -	\$ 1,467,444	\$ 2,574,553
Purchase Displacement	11,840	7,350	11,200	627,448	-
	<u>\$ 11,840</u>	<u>\$ 7,350</u>	<u>\$ 11,200</u>	<u>\$ 2,094,892</u>	<u>\$ 2,574,553</u>
Telecom Revenues					
Commercial	\$ 388,228	\$ 330,239	\$ 292,491	\$ 174,768	\$ 144,286
Other Revenues					
Forfeited Discounts	\$ 37,072	\$ 37,420	\$ 39,700	\$ 33,730	\$ 46,580
Miscellaneous Service Revenue	2,027,154	1,865,022	1,484,738	1,681,251	999,749
Electric Pole Rental Fees	166,320	170,126	162,806	158,132	134,461
Miscellaneous Electric Operating Revenue	141,803	112,163	112,073	109,530	110,560
Total Other Revenues	<u>\$ 2,372,349</u>	<u>\$ 2,184,731</u>	<u>\$ 1,799,317</u>	<u>\$ 1,982,643</u>	<u>\$ 1,291,350</u>
TOTAL OPERATING REVENUES	\$ 43,408,464	\$ 40,219,223	\$ 37,937,883	\$ 39,085,777	\$ 38,990,085
OPERATING EXPENSES					
Purchased Power	\$ 22,160,973	\$ 21,095,946	\$ 20,872,530	\$ 20,797,617	\$ 20,066,443
Operation	3,087,790	2,256,733	2,290,180	3,508,664	4,178,280
Maintenance	4,389,823	2,629,800	2,336,816	2,271,860	2,231,141
Customer Accounts	1,482,642	1,536,440	1,317,541	1,333,627	1,311,429
Customer Service	776,217	346,086	334,551	459,361	497,083
Administration & General	3,561,293	4,755,392	4,297,399	3,782,824	3,461,681
Maintenance of General Plant	539,625	534,186	472,559	463,827	453,282
Total Operating Expenses	<u>\$ 35,998,363</u>	<u>\$ 33,154,583</u>	<u>\$ 31,921,576</u>	<u>\$ 32,617,780</u>	<u>\$ 32,199,339</u>
GROSS OPERATING INCOME	\$ 7,410,101	\$ 7,064,640	\$ 6,016,307	\$ 6,467,997	\$ 6,790,746
NON-OPERATING REVENUES					
Revenue from Contracting Work	\$ 16,749	\$ 24,580	\$ 7,959	\$ 24,974	\$ 5,623
Rental Income	62,628	37,761	24,992	30,772	26,261
Interest Earnings & Misc.	594,197	456,622	278,214	293,364	509,547
Misc Non-Operating Income	762,034	82,565	82,069	192,769	181,795
Total Non-Operating Revenues	<u>\$ 1,435,608</u>	<u>\$ 601,528</u>	<u>\$ 393,234</u>	<u>\$ 541,879</u>	<u>\$ 723,226</u>
NON-OPERATING EXPENSES					
Taxes	\$ 1,620,619	\$ 1,489,142	\$ 1,319,611	\$ 1,325,264	\$ 1,300,419
Cost of Contracting Work & Other	16,670	15,247	6,463	12,046	13,394
Total Non-Operating Expenses	<u>\$ 1,637,289</u>	<u>\$ 1,504,389</u>	<u>\$ 1,326,074</u>	<u>\$ 1,337,310</u>	<u>\$ 1,313,813</u>
NET INCOME BEFORE DEPRECIATION AND AMORTIZATION	\$ 7,208,420	\$ 6,161,779	\$ 5,083,467	\$ 5,672,566	\$ 6,200,159
DEBT SERVICE	\$ 2,585,710	\$ 2,653,275	\$ 2,221,050	\$ 2,685,045	\$ 2,128,117
DEBT SERVICE COVERAGE	2.79	2.32	2.29	2.11	2.91

Mason County Public Utility District No. 3
Shelton, Mason County, Washington
Financial Results
For the years ending December 31 - Unaudited

	2001	2000	1999	1998	1997
OPERATING REVENUES					
Electric Revenues					
Residential Sales	\$ 20,666,406	\$ 19,599,437	\$ 19,424,792	\$ 18,355,634	\$ 18,232,683
Outdoor Lighting	484,757	442,951	436,762	228,064	116,325
Fixed Rate Facilities	699	918	694	986	836
Commercial	8,616,814	5,821,031	5,975,043	6,098,553	5,810,688
Large Industrial	2,282,894	2,125,673	2,252,079	2,198,384	2,145,192
Public Authorities	-	1,947,951	1,882,643	1,455,469	1,660,399
Sales for Resale	402,398	172,336	172,984	225,175	101,628
Total Electric Revenues	<u>\$ 32,453,968</u>	<u>\$ 30,110,297</u>	<u>\$ 30,144,997</u>	<u>\$ 28,562,265</u>	<u>\$ 28,067,751</u>
Generation Revenues					
Sales for Resale	\$ -	\$ -	\$ -	\$ -	\$ -
Purchase Displacement	-	-	-	-	-
	<u>\$ -</u>				
Telecom Revenues					
Commercial	\$ -	\$ -	\$ -	\$ -	\$ -
Other Revenues					
Forfeited Discounts	\$ 42,100	\$ 51,120	\$ 53,510	\$ 46,640	\$ 50,250
Miscellaneous Service Revenue	136,738	133,773	136,775	140,469	148,953
Electric Pole Rental Fees	115,151	67,307	64,508	63,962	62,778
Miscellaneous Electric Operating Revenue	114,575	102,520	108,405	83,550	92,663
Total Other Revenues	<u>\$ 408,564</u>	<u>\$ 354,720</u>	<u>\$ 363,198</u>	<u>\$ 334,621</u>	<u>\$ 354,644</u>
TOTAL OPERATING REVENUES	\$ 32,862,532	\$ 30,465,017	\$ 30,508,195	\$ 28,896,886	\$ 28,422,395
OPERATING EXPENSES					
Purchased Power	\$ 15,727,800	\$ 14,212,649	\$ 13,975,628	\$ 13,386,231	\$ 13,380,323
Operation	1,629,310	1,969,505	1,638,600	1,536,309	1,395,011
Maintenance	2,678,639	2,252,790	1,819,233	1,615,639	4,739,832
Customer Accounts	1,077,400	1,168,371	1,252,250	866,419	1,168,940
Customer Service	412,743	166,133	163,894	202,510	356,295
Administration & General	3,237,750	2,561,213	2,520,290	2,117,776	2,185,367
Maintenance of General Plant	460,309	359,531	363,487	254,400	182,501
Total Operating Expenses	<u>\$ 25,223,951</u>	<u>\$ 22,690,192</u>	<u>\$ 21,733,382</u>	<u>\$ 19,979,284</u>	<u>\$ 23,408,269</u>
GROSS OPERATING INCOME	\$ 7,638,581	\$ 7,774,825	\$ 8,774,813	\$ 8,917,602	\$ 5,014,126
NON-OPERATING REVENUES					
Revenue from Contracting Work	\$ 9,165	\$ 3,592	\$ 17,484	\$ 9,058	\$ 17,275
Rental Income	-	-	-	-	-
Interest Earnings & Misc.	788,529	827,153	622,661	651,229	549,849
Misc Non-Operating Income	265,122	72,891	79,751	81,641	2,596,078
Total Non-Operating Revenues	<u>\$ 1,062,816</u>	<u>\$ 903,636</u>	<u>\$ 719,896</u>	<u>\$ 741,928</u>	<u>\$ 3,163,202</u>
NON-OPERATING EXPENSES					
Taxes	\$ 1,152,700	\$ 1,052,419	\$ 1,061,062	\$ 1,053,217	\$ 1,082,648
Cost of Contracting Work & Other	12,619	3,291	13,631	13,723	16,134
Total Non-Operating Expenses	<u>\$ 1,165,319</u>	<u>\$ 1,055,710</u>	<u>\$ 1,074,693</u>	<u>\$ 1,066,940</u>	<u>\$ 1,098,782</u>
NET INCOME BEFORE DEPRECIATION AND AMORTIZATION	\$ 7,536,078	\$ 7,622,751	\$ 8,420,016	\$ 8,592,590	\$ 7,078,546
DEBT SERVICE	\$ 1,460,444	\$ 2,052,914	\$ 2,033,903	\$ 2,011,242	\$ 2,063,529
DEBT SERVICE COVERAGE	5.16	3.71	4.14	4.27	3.43

Mason County Public Utility District No. 3
Shelton, Mason County, Washington
Historical Customers, Energy Sales and Revenues
For the years ending December 31 - Unaudited

	2006	2005	2004	2003	2002
Number of Customers					
Residential	29,279	28,619	27,657	27,177	26,638
Commercial (1)	2,160	2,121	2,074	2,039	1,950
Large Industrial (2)	1	1	1	1	1
Other (3)	89	89	86	88	89
Total	31,529	30,830	29,818	29,305	28,678

Energy Sales (kWh)					
Residential	389,004,242	369,780,401	363,915,264	350,011,988	351,661,448
Commercial	184,284,662	171,614,419	162,880,230	158,716,217	162,559,086
Large Industrial	70,416,000	74,793,600	69,436,800	64,123,200	70,992,000
Other	2,114,701	2,067,158	2,046,464	2,120,681	2,042,676
Total	645,819,605	618,255,578	598,278,758	574,972,086	587,255,210

Revenues from Sales of Energy					
Residential	\$ 26,140,240	\$ 24,051,725	\$ 23,166,516	\$ 22,433,267	\$ 22,366,839
Commercial (1)	11,031,717	10,049,534	9,265,698	9,157,959	9,277,119
Large Industrial (2)	2,922,458	3,079,556	2,888,372	2,738,929	2,828,778
Other (3)	541,632	516,088	514,289	503,319	507,160
Sale for Resale	-	-	-	-	-
Total	\$ 40,636,047	\$ 37,696,903	\$ 35,834,875	\$ 34,833,474	\$ 34,979,896

Annual kWh per Customer					
Residential	13,286	12,921	13,158	12,879	13,201
Commercial	85,317	80,912	78,534	77,840	83,364
Large Industrial	70,416,000	74,793,600	69,436,800	64,123,200	70,992,000
Other	23,761	23,226	23,796	24,099	22,951
Average - All Classes	20,483	20,054	20,064	19,620	20,478

Revenue per kWh (in cents)					
Residential	0.07	0.07	0.06	0.06	0.06
Commercial	0.06	0.06	0.06	0.06	0.06
Large Industrial	0.04	0.04	0.04	0.04	0.04
Other	0.26	0.25	0.25	0.24	0.25
Average - All Classes	0.06	0.06	0.06	0.06	0.06

(1) Includes commercial customers and public authorities.

(2) Simpson Timber Company.

(3) Includes outdoor lighting and unmetered signs.

Mason County Public Utility District No. 3
Shelton, Mason County, Washington
Historical Customers, Energy Sales and Revenues
For the years ending December 31 - Unaudited

	2001	2000	1999	1998	1997
Number of Customers					
Residential	26,091	26,003	25,583	25,115	24,819
Commercial (1)	1,939	1,838	1,806	1,762	1,732
Large Industrial (2)	1	1	1	1	1
Other (3)	86	84	82	85	81
Total	28,117	27,926	27,472	26,963	26,633

Energy Sales (kWh)

Residential	344,668,590	357,713,571	356,340,701	329,084,469	327,149,551
Commercial	156,783,759	176,972,462	159,380,906	148,830,267	147,926,292
Large Industrial	64,771,200	64,425,600	69,422,400	67,301,300	66,435,130
Other	2,030,171	2,024,901	1,982,193	2,123,759	1,928,850
Total	568,253,720	601,136,534	587,126,200	547,339,795	543,439,823

Revenues from Sales of Energy

Residential	\$ 20,666,406	\$ 19,599,437	\$ 19,424,792	\$ 18,355,634	\$ 18,232,683
Commercial (1)	8,616,814	7,768,982	7,857,686	7,554,022	7,471,087
Large Industrial (2)	2,282,894	2,125,673	2,252,079	2,198,384	2,145,192
Other (3)	485,456	443,869	437,456	229,050	117,161
Sale for Resale	402,398	112,336	172,984	225,175	101,628
Total	\$ 32,453,968	\$ 30,050,297	\$ 30,144,997	\$ 28,562,265	\$ 28,067,751

Annual kWh per Customer

Residential	13,210	13,757	13,929	13,103	13,181
Commercial	80,858	96,285	88,251	84,467	85,408
Large Industrial	64,771,200	64,425,600	69,422,400	67,301,300	66,435,130
Other	23,607	24,106	24,173	24,985	23,813
Average - All Classes	20,210	21,526	21,372	20,300	20,405

Revenue per kWh (in cents)

Residential	0.06	0.05	0.05	0.06	0.06
Commercial	0.05	0.04	0.05	0.05	0.05
Large Industrial	0.04	0.03	0.03	0.03	0.03
Other	0.24	0.22	0.22	0.11	0.06
Average - All Classes	0.06	0.05	0.05	0.05	0.05

(1) Includes commercial customers and public authorities.

(2) Simpson Timber Company.

(3) Includes outdoor lighting and unmetered signs.

Mason County Public Utility District No. 3
Shelton, Mason County, Washington
Uncollectible Account Analysis
For the years ending December 31 - Unaudited

	2006	2005	2004	2003	2002
Electric Receipts (1)	\$ 37,713,589	\$ 34,617,347	\$ 32,946,503	\$ 32,094,545	\$ 32,151,118
Write-offs	\$ 154,831	\$ 135,068	\$ 113,085	\$ 204,751	\$ 120,764
Percentage Written Off	0.41%	0.39%	0.29%	0.58%	0.38%
Allowance	\$ 136,496	\$ 114,314	\$ 213,392	\$ 112,243	\$ 119,565
Payments from Agencies	\$ 38,187	\$ 28,297	\$ 24,578	\$ 26,913	\$ 32,618
Payments to Agencies	\$ 3,933	\$ 6,055	\$ 7,518	\$ 9,308	\$ 11,676
Percent of Write-offs Collected	24.66%	20.95%	21.73%	13.14%	27.01%

(1) Does not include sale for resale or Large Industrial.

**Mason County Public Utility District No. 3
 Shelton, Mason County, Washington
 Uncollectible Account Analysis
 For the years ending December 31 - Unaudited**

	2001	2000	1999	1998	1997
Electric Receipts (1)	\$ 29,768,676	\$ 27,812,288	\$ 27,719,934	\$ 25,820,931	\$ 24,820,931
Write-offs	\$ 123,981	\$ 139,594	\$ 122,282	\$ 82,730	\$ 86,425
Percentage Written Off	0.42%	0.50%	0.44%	0.32%	0.35%
Allowance	\$ 116,967	\$ 89,418	\$ 87,487	\$ 81,730	\$ 84,068
Payments from Agencies	\$ 23,668	\$ 31,542	\$ 26,088	\$ 17,842	\$ 26,513
Payments to Agencies	\$ 8,771	\$ 11,965	\$ 10,040	\$ 8,490	\$ 11,584
Percent of Write-offs Collected	19.09%	22.60%	21.33%	21.57%	30.68%

(1) Does not include sale for resale or Large Industrial.

**Mason County Public Utility District 3
Shelton, Mason County, Washington
Comparative Tax Costs
For the years ending December 31**

	Current Rate	2006	2005	2004	2003	2002
State Public Utility Tax	3.873%	\$ 1,596,247	\$ 1,460,042	\$ 1,360,927	\$ 1,286,317	\$ 1,256,733
State Privilege Tax	2.140%	878,294	754,337	743,610	755,211	697,926
City of Shelton Utility Tax	6.000%	574,468	561,876	543,104	519,716	521,620
Leasehold Tax	12.840%	14,873	20,010	14,224	14,053	10,853
Payroll Taxes	Various	599,101	587,265	526,534	527,171	493,935
L & I, Employment Security	Various	113,715	123,419	142,741	188,077	166,948
Miscellaneous Taxes	Various	<u>69,962</u>	<u>54,331</u>	<u>53,319</u>	<u>117,409</u>	<u>47,237</u>
Total Taxes		\$ 3,846,660	\$ 3,561,280	\$ 3,384,459	\$ 3,407,954	\$ 3,195,252
Total Operating Revenues		\$ 43,408,464	\$ 40,219,223	\$ 37,937,883	\$ 39,085,777	\$ 38,990,085
% of Operating Revenues		8.86%	8.85%	8.92%	8.72%	8.20%

**Mason County Public Utility District 3
Shelton, Mason County, Washington
Comparative Tax Costs
For the years ending December 31**

	Current Rate	2001	2000	1999	1998	1997
State Public Utility Tax	3.873%	\$ 1,105,090	\$ 1,054,803	\$ 1,057,517	\$ 1,024,948	\$ 1,023,641
State Privilege Tax	2.140%	652,267	652,854	617,821	594,144	613,058
City of Shelton Utility Tax	6.000%	465,233	437,154	439,740	424,604	431,405
Leasehold Tax	12.840%	7,495	4,229	3,958	3,904	3,886
Payroll Taxes	Various	468,167	442,064	419,713	400,594	417,207
L & I, Employment Security	Various	148,527	125,277	122,781	176,038	163,038
Miscellaneous	Various	<u>51,312</u>	<u>38,280</u>	<u>46,372</u>	<u>35,369</u>	<u>66,292</u>
Total Taxes		\$ 2,898,091	\$ 2,754,661	\$ 2,707,902	\$ 2,659,601	\$ 2,718,527
Total Operating Revenue		\$ 32,862,532	\$ 30,456,017	\$ 30,508,195	\$ 28,896,886	\$ 28,422,395
% of Operating Revenue		8.82%	9.04%	8.88%	9.20%	9.56%

**Mason County Public Utility District No. 3
Shelton, Mason County, Washington
Demographic Statistics for the years ending December 31 - Unaudited**

	2006	2005	2004	2003	2002
Population of County (1)	53,100	51,900	50,800	52,288	51,199
Unemployment Rate (2)	5.9%	6.1%	7.4%	8.6%	8.3%
Median Household Income (3)	\$ 45,188	\$ 42,804	\$ 42,065	\$ 41,663	\$ 41,978
Heating Degree Days (4)	5,240	5,135	5,024	5,146	5,626
Rainfall in Shelton (5)	80.9"	59.7"	52.9"	75.1"	53.4"
New electric connects by Mason County PUD No. 3	821	895	727	663	517
Number of Electric Customers	31,528	30,830	29,818	29,305	28,678
Residential Rate December 31 (cent/kWh)	5.66	5.32	5.16	5.16	5.16

Principal Employers in County

Employer (6)	Product/Service	2006		1996	
		Employees	Rank	Employees	Rank
Little Creek Casino Hotel	Casino and hotel	696	1	349	4
Shelton School District	Education provider	675	2	625	3
Washington Correction Center	State prison	581	3	625	2
Mason General Hospital	Medical facility	495	4	310	5
Wal-Mart	Retail store	420	5	210	9
Mason County	Government	411	6	305	6
Simpson Timber Company	Lumber	400	7	928	1
Taylor Shellfish	Shellfish	400	8	-	-
Olympic Panel Products	Plywood, veneer	360	9	-	-
North Mason School District	Education provider	350	10	252	7
Stock Market Foods	Groceries	-	-	228	8
Fir Lane Terrace	Care provider	-	-	175	10

(1) Source: NW Income Indicators Project - WSU

(2) Source: Washington State Employment Security Department

(3) Source: Washington State OFM

(4) Source: National Weather Service Forecast Office

(5) Source: Shelton-Mason County Journal Mason County Profile and City of Shelton

(6) Source: Shelton-Mason County Journal Visitors' Guide and Mason County Profile

**Mason County Public Utility District No. 3
 Shelton, Mason County, Washington
 Demographic Statistics for the years ending December 31 - Unaudited**

	2001	2000	1999	1998	1997
Population of County (1)	50,261	49,584	48,753	48,454	48,318
Unemployment Rate (2)	7.7%	6.4%	5.9%	5.8%	6.3%
Median Household Income (3)	\$ 42,217	\$ 41,267	\$ 39,586	\$ 38,512	\$ 36,519
Heating Degree Days (4)	5,800	5,668	5,572	5,125	5,007
Rainfall in Shelton (5)	63.6"	49.5"	82.1"	78.7"	85.3"
New electric connects by Mason County PUD No. 3	484	499	548	573	663
Number of Customers	28,117	27,926	27,472	26,963	26,633
Residential Rate December 31 (cent/kWh)	5.16	4.49	4.49	4.49	4.49

(1) Source: NW Income Indicators Project - WSU

(2) Source: Washington State Employment Security Department

(3) Source: Washington State OFM

(4) Source: National Weather Service Forecast Office

(5) Source: Shelton-Mason County Journal Mason County Profile and City of Shelton

(6) Source: Shelton-Mason County Journal Visitors' Guide and Mason County Profile

Back Cover: Mason County PUD No. 3 Apprentice Lineman Randy VanAagten works on a PUD electrical service in the Shelton area. In the background, Mount Rainer rises from Washington State's Cascade Mountain range. Photo Credit, Terri Oberg



MASON COUNTY PUBLIC UTILITY DISTRICT No. 3
P.O. Box 2148
SHELTON, WA 98584
(360) 426-8255
WWW.MASONPUD3.ORG