



CHELAN COUNTY

# AUDIT COMMITTEE

2016 Annual Report  
February 21, 2017

## Introduction

The Audit Committee Charter calls for annual reporting to the Board of Commissioners and General Manager about activities, issues and related recommendations. The Audit Committee was created by Resolution No. 04-12597 as a governance best practice and to provide functional reporting independence for Internal Audit. The Committee consists of the President and Vice President of the Board of Commissioners with the Secretary serving as alternate, as well as the District's General Counsel, Senior Manager for Customer Utilities, Generation & Transmission, District Services and the Chief Financial/Risk Officer.

## Meetings Summary

### March 2016-First Quarter Meeting

The District's Lead Accounting Analyst provided an update on the 2015 PricewaterhouseCoopers (PwC) financial audit. Fieldwork is complete and no significant unresolved issues or control weaknesses have been identified. The audit report is anticipated in mid-April. This is the last year of the current three-year contract with PwC.

Enterprise Risk Management (ERM) provided the Committee with a quarterly update on key risks, new and modified items in the risk register.

Internal Audit updated the Committee on the 2016 Audit Plan status. A check-in of the 2014 Dam Safety audit was performed to determine the progress made on the audit opportunities for improvement previously communicated to management. Plans to address the remaining 4 opportunities for improvement will occur by year-end 2016.

The Compliance Manager reported to the Committee on the 2016 WECC Reliability Audit. Documents requested for the audit must be filed by April 1. The audit is scheduled to start on May 2 with the onsite portion on May 9-13, 2016.

### May 2016-Special Meeting

PwC presented the results of the 2015 financial statement audit. An unqualified (clean) opinion for the audit has been issued. No material weaknesses or significant deficiencies were noted in internal controls. Areas of focus included (1) management override of controls - no instances of management manipulation or fraud were found; (2) revenue recognition limited to "non-regulated" market-based sales – no material misstatements were noted; (3) capitalization of costs in utility plant – determine all items were recorded appropriately; (4) accounting for power contracts and derivatives - no exceptions were noted and no material misstatements or errors; (5) regulatory accounting – confirmed all current deferrals were appropriate and recalculated the current year amortization of regulatory balances without exception; (6) Bookout transactions – net presentation – bookout activity did not have an impact on the District's accounting for derivatives; (7) FEMA grant – no finding of noncompliance . The State Auditors will be auditing the compliance requirements of the FEMA grant in the Fall of 2016 and (8) GASB 68 adoption – validated the appropriateness of the accounting impact of the financial statements and that all necessary disclosures were made within the District's notes to the financial statements. PwC concluded that there were no material uncertainties related to events and conditions, specifically going concern

issues. Management disclosed all significant risks. No instances of fraud or illegal acts were found during the course of the audit.

### **June 2016-Second Quarter Meeting**

Internal Audit reported on the upcoming 2015 State audit. The annual accountability audit will start in October 2016. There will not be a single audit for 2015. The FEMA grant for the wildfires will be reported in the 2016 audit.

The Controller reported on the independent auditor evaluation and contract. The current contract with PricewaterhouseCoopers (“PwC”) expires in August 2016. One of the Audit Committee’s responsibilities is to review the external auditor’s performance and make a recommendation to either issue a new Request for Proposals or extend the current contract. The performance evaluation of PwC included review of the professional services agreement, consideration of best practices, survey of District staff, review of the Public Company Accounting Oversight Board (PCAOB) inspection report and review of peer reports. Other criteria considered was the audit leader’s knowledge and experience, cooperation with the State Auditor’s Office, fees, communication with the Audit Committee, responsiveness to requests and assistance/information offered outside of the audit. It was determined by District staff that PwC’s qualifications, performance and independence has been satisfactory. The Committee unanimously approved to authorize staff to enter into contract negotiations with PwC on terms satisfactory to the District for a term not to exceed 3 years

An update was provided on ERM to review key risks, items added to the risk register and future efforts.

### **September 2016-Third Quarter Meeting**

Internal Audit presented an executive summary for the Skaha Hatchery Construction Closeout Review which was completed in June 2016. The audit scope included (1) review of the hatchery construction closeout; (2) review of the asset management plan; and (3) analysis of annual work plans and invoice review process. The audit determined there to be sufficient assurance that the hatchery was constructed in conformance with the design criteria in the agreement to achieve the operating intent. The auditors verified the total expended by the District for hatchery design and construction and confirmed the resolution amount approved for design and construction of the hatchery was not exceeded. Weaknesses were identified over contracting authority and tracking of program expenses.

Internal Audit briefly reviewed the Safety Departmental Review – Incident Analysis and the Workers’ Compensation Follow-Ups with the Committee. An additional follow-up will occur in November 2016 to ensure that the Incident Analysis Manual adequately addressed the opportunities for improvement and a second follow-up will occur in 2017 to ensure it was properly implemented. In the Worker’s Compensation follow-up, the auditors noted that all recommendations have been resolved.

An update was provided on ERM to review key risks, items added to the risk register and new and modified risks. ERM previewed the new Key Risk Report that they are proposing to use in the future. The new report ranks the risk using five dimensions: estimated likelihood; estimated impact; estimated velocity; estimated preparedness/influence; and potential reputation damage.

PricewaterhouseCoopers (“PwC”) provided an overview of the upcoming 2016 audit plan. Areas of emphasis include Alcoa’s decision to idle operations at Wenatchee Works and the impact to the Chelan County PUD

PUD's power sales contract with Alcoa; continued debt repayments; and adoption of GASB 72: Fair value measurement and application. They will also concentrate on significant risks including management override of controls and revenue recognition for non-regulated/market-based sales. Other areas of audit emphasis include capital versus expense classification, accounting for power contracts and other derivatives, regulatory assets, and accruals and long-term debt. Year-end field work will be performed from February 27-March 17, 2017 with an anticipated report date in April. The report to the Audit Committee on the audit results will be in May 2017.

The District's Compliance Manager reported that the Governance/Risk/Compliance Request for Proposals was issued and six proposals have been received. Demonstrations by the vendors will be conducted the third week in October. It was also reported that FERC was on sight in July for a dam safety inspection. No concerns were reported at that time. The District should receive a written report in the near future.

General Counsel reported to the Committee that the WECC audit reported no findings.

### **January 2017-Fourth Quarter Meeting**

The State Auditor's Office presented the results of the 2015 accountability audit. The results and recommendations were shared in detail with District management and personnel as they were developed. The audit report does not include any findings. Exit recommendations were to continue to strengthen controls for tracking and safeguarding tool room inventories and to establish a formal process, by resolution, to obtain quotes and maintain a list of vendors specifically for obtaining quotes through the process. The next scheduled audit will be conducted in 2017 and will cover accountability for public resources and compliance for federal programs.

The Controller updated the Committee on significant year-end accounting items as follows; Pension Accounting, Rock Island B1-B4, Rock Island B6, and Alcoa Curtailment. Other year-end accounting items that were not material included Slice Revenue, FEMA Reimbursement for 2015 Chelan Complex Fire and Fiber/Telecom Inventory Adjustments. The Controller also reported on the PricewaterhouseCoopers ("PwC") 2016 financial statement audit. PwC will be on site starting February 27 for approximately three weeks.

Internal Audit presented two Executive Summaries, a follow-up to the Dam Safety audit and follow-up of the Safety Department Incident Analysis review. It was concluded that the Incident Reporting and Investigation Standard has been adequately updated and final follow-up for program implementation will occur in the latter half of 2017. Internal audit provided the committee with a summary of Internal Audit reports from September 2004 through December 2016. Status of where Internal Audit ended the year with their 2016 work plan was reviewed. The 2017 Internal Audit work plan was reviewed and approved by the committee.

Enterprise Risk Management group presented an update on ERM to review updated key risk definitions, Tier 1 risks and new/modified items in the risk register. The identification of key risks and categorization of Tier 1 and Tier 2 risks has evolved. Key risks were originally based on likelihood and impact, with subjective emphasis in the selection of key risks. To help standardize the key risk identification process, velocity, preparedness and reputation damage were added. All five dimensions of risks are used to create a Risk Criticality Score.