Statements of Operations and Changes in Retained Earnings

Years Ended December 31,	*2001*	*2000*
Operating Revenues:		
Retail power revenues	$ 503,437,272	$ 391,578,285
Wholesale power revenues	108,523,610	108,132,297
Transmission and other	15,625,381	5,918,117
	627,586,263	505,628,699
Operating Expenses:		
Long-term purchased power	151,213,357	79,304,610
Short-term wholesale power purchases	224,421,729	212,402,254
Power marketing and system control	6,064,682	5,504,322
Generation	17,012,159	25,665,927
Transmission	30,260,132	21,726,234
Distribution	36,493,212	34,523,307
Customer service	27,532,059	22,179,214
Conservation	8,522,651	6,972,547
Administrative and general	39,140,392	37,020,250
City of Seattle occupation tax	30,648,911	24,002,685
Other taxes	21,916,749	18,857,370
Depreciation	61,538,960	55,498,917
	654,764,993	543,657,637
Net operating loss	(27,178,730)	(38,028,938)
Nonoperating Revenues (Expenses):		
Investment income	13,486,717	9,753,106
Interest expense	(72,109,397)	(48,097,827)
Amortization of debt expense	(1,786,694)	(5,054,837)
Gain on sale of Centralia Steam Plant	-	29,639,799
Other expense, net	(1,048,013)	(240,039)
	(61,45 7,387)	(13,999,798)
Fees, Grants, and Transfers:		
Capital	13,372,688	-
Operating	1,923,022	-
	15,295,710	-
Net Loss	(73,340,407)	(52,028,736)
Retained Earnings:		
Beginning of the year	247,990,953	300,019,689
End of the year	$ **174,650,546**	$ **247,990,953**

See notes to the financial statements.

Statements of Cash Flows

Years Ended December 31,	*2001*	*2000*
Operating Activities:		
Cash received from customers and counterparties	$ 671,289,411	$ 492,199,632
Cash paid to suppliers, employees, and counterparties	(931,423,126)	(376,818,442)
Taxes paid	(50,134,407)	(40,833,895)
Net cash provided by (used for) operating activities	(310,268,122)	74,547,295
Noncapital Financing Activities:		
Grant revenues received	1,014,343	-
Operating transfers received from the City of Seattle	315,000	-
Net cash provided by noncapital financing activities	1,329,343	-
Capital and Related Financing Activities:		
Proceeds from long-term debt, net of premium	798,479,496	100,491,983
Bond issue costs paid	(2,231,896)	(256,391)
Principal paid on long-term debt	(138,030,000)	(36,179,500)
Interest paid on long-term debt	(69,762,579)	(53,988,291)
Acquisition and construction of capital assets	(149,335,107)	(177,974,051)
Proceeds from sale of Centralia Steam Plant	-	41,399,047
Proceeds from sale of other property, plant, and equipment	476,683	406,836
Capital fees/Contributions in aid of construction	12,394,505	11,665,780
Net cash provided by (used for) capital and related financing activities	451,991,102	(114,434,587)
Investing Activities:		
Proceeds from long-term loans receivable	250,441	385,090
Long-term loans issued	(116,765)	(115,363)
Proceeds from sale of investments	567,239,517	8,216,000
Purchases of investments	(656,263,060)	-
Interest received on investments	11,280,508	8,161,645
Net cash provided by (used for) investing activities	(77,609,359)	16,647,372
Net Increase (Decrease) in Cash and Equity in Pooled Investments	65,442,964	(23,239,920)
Cash and Equity in Pooled Investments:		
Beginning of year	79,474,489	102,714,409
End of year	**$ 144,917,453**	**$ 79,474,489**

Reconciliation of Net Operating Income to Net Cash Provided by Operating Activities:

Net operating loss	$ (27,178,730)	$ (38,028,938)
Adjustments to reconcile net operating loss to net cash provided by (used for) operating activities:		
Depreciation and amortization	70,412,288	63,510,859
Cash provided by (used for) changes in operating assets and liabilities:		
Accounts receivable	32,957,358	(8,420,793)
Unbilled revenues	(25,928,733)	(3,277,080)
Other deferred charges	(316,162,037)	3,484,498
Materials and supplies	315,615	(1,524,255)
Prepayments, interest receivable, and other	10,087,199	5,062,837
Provision for injuries and damages	(327,102)	476,094
Accounts payable, taxes and other	(65,068,412)	53,005,566
Compensated absences	761,547	376,388
Other	9,862,885	(117,881)
Net Cash Provided by (Used for) Operating Activities	**$ (310,268,122)**	**$ 74,547,295**

Cash and Equity in Pooled Investments at December 31 Consists of:

Cash and cash equivalents	$ 13,653,054	$ 25,871,777
Equity in pooled investments	131,264,399	53,602,712
	$ 144,917,453	**$ 79,474,489**

See notes to the financial statements.

Notes to Financial Statements

Years Ended December 31, 2001 and 2000

Note 1: Operations and Summary of Significant Accounting Policies

The City Light Department (the Department) is the public electric utility of the City of Seattle (the City). The Department owns and operates certain generating, transmission, and distribution facilities and supplies electricity to approximately 354,000 customers. The Department supplies electrical energy to other City agencies at rates prescribed by City ordinances. The establishment of the Department's rates is within the exclusive jurisdiction of the City Council. A requirement of Washington State law provides that rates must be fair, nondiscriminatory, and fixed to produce revenue adequate to pay for operation and maintenance expenses and to meet all debt service requirements payable from such revenue. The Department pays occupation taxes to the City based on total revenues.

The Department also provides nonenergy services to other City agencies and received $5.8 million in 2001 and $10.0 million in 2000 for such services. Included in accounts receivable at December 31, 2001 and 2000, are $1.1 million and $7.5 million, respectively, representing amounts due from other City departments for services provided, reimbursements, and interest receivable on cash and equity in pooled investments.

The Department receives certain services from other City agencies and paid approximately $35.2 million and $37.5 million, respectively, in 2001 and 2000 for such services. Included in accounts payable for the same time periods are $4.5 million and $6.2 million, respectively, representing amounts due other City departments for goods and services received.

Accounting Standards

The accounting and reporting policies of the Department are regulated by the Washington State Auditor's Office, Division of Municipal Corporations, and are based on the Uniform System of Accounts prescribed for public utilities and licensees by the Federal Energy Regulatory Commission (FERC). The financial statements are also prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Department has applied all applicable GASB pronouncements as well as the following pronouncements, except for those that conflict with or contradict GASB pronouncements: Statements and Interpretations of the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures. The more significant of the Department's accounting policies are described below.

In June 1999, GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. The objective of this statement is to enhance the understandability and usefulness of the general-purpose external financial reports of state and local governments to the citizenry, legislative and oversight bodies, bondholders, and creditors, and is effective for the Department in 2002. For the Department, this statement will require certain formatting changes to the basic financial statements as well as a required section covering management's discussion and analysis and certain other required supplementary information. The Department does not anticipate a material impact to the financial position or operations of the Department as a result of implementing this standard.

Nonexchange Transactions

In December 1998, GASB issued Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, that requires reporting nonexchange transactions as revenues effective for periods beginning after June 15, 2000. Capital fees from private sources were reported as a component of equity as contributions in aid of construction prior to implementation of GASB Statement No. 33. Capital fees, grants, and transfers in the amount of $15.3 million are reported for 2001 on the statements of operations and changes in retained earnings as nonoperating revenues as a result of the adoption of this standard. The cumulative effect of adoption of GASB Statement No. 33 will be made in conjunction with the implementation of GASB Statement No. 34 in 2002.

Derivative Instruments

In June 1998, FASB issued Statement of Financial Accounting Standards (SFAS) No. 133, *Accounting for Derivative Instruments and Hedging Activities.* This statement was amended in June 2000 by SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities.* Both statements are effective for fiscal years beginning after June 15, 2000, and were adopted by the Department in 2001. SFAS Nos. 133 and 138 require that the fair value of derivative financial instruments be recognized as either assets or liabilities on the Department's balance sheet and that changes in the fair value of a derivative instrument be included in earnings. The Department had outstanding sales and purchases of electric energy at December 31, 2001, under short-term forward contracts on electricity that meet the definition of a derivative in accordance with SFAS No. 133, and recorded an asset and deferred gain of $14.5 million, which is presented as energy contract assets on the balance sheet, and a liability and deferred loss of $0.9 million, respectively. In addition, the Department entered into a fixed for variable price gas swap in April 2001 to fix the fuel expense for the Klamath Falls Cogeneration Project from July 2001 through December 2002, and recorded an energy contract liability and deferred loss of $13.9 million and recognized $6.9 million for swap settlements which is reported in long-term purchased power expenses.

In accordance with City Council Resolution No. 30290, deferred losses are regulatory assets, and deferred gains are regulatory liabilities, pursuant to SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*. Thus, the adoption of SFAS Nos. 133 and 138 has no impact on recorded earnings. The Department's conclusions regarding the accounting treatment and financial statement effect of SFAS No. 133 could change based on interpretations of issues pending before the FASB.

Utility Plant

Utility plant is recorded at original cost, which includes both direct costs of construction or acquisition and indirect costs, including an allowance for funds used during construction. The allowance represents the estimated costs of financing construction projects and is computed using the Department's most recent long-term borrowing rate. The allowance totaled $5.7 million and $5.6 million in 2001 and 2000, respectively, and is reflected as a reduction of interest expense in the statements of operations and changes in retained earnings. Property constructed with capital fees received from customers is included in utility plant. Capital fees totaled $12.5 million in 2001 and $15.6 million in 2000. Provision for depreciation is made using the straight-line method based upon estimated economic lives, which range from three to 50 years, of related operating assets. The Department uses a half-year convention method on the assumption that additions and replacements are placed in service at mid-year. The composite depreciation rate was approximately 3.2% in 2001 and 3.1% in 2000. When operating plant assets are retired, their original cost together with removal costs, less salvage, is charged to accumulated depreciation. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and betterments is capitalized.

Restricted Assets

In accordance with the Department's bond resolutions, state law, or other agreements, separate restricted assets have been established. These assets are restricted for specific purposes, including the establishment of the Municipal Light & Power (ML&P) Bond Reserve Account, financing of the Department's ongoing Capital Improvement Program, and other purposes.

Compensated Absences

Permanent employees of the Department earn vacation time in accordance with length of service. A maximum of 480 hours may be accumulated and, upon termination, employees are entitled to compensation for unused vacation. At retirement, employees receive compensation equivalent to 25% of their accumulated sick leave. The Department accrues all costs associated with compensated absences, including payroll taxes.

Accounts Payable and Other

The composition of accounts payable and other is as follows:

	2001	*2000*
Vouchers payable	$ 8,544,835	$ 14,907,362
Power accounts payable	25,263,010	71,140,213
Interfund payable	4,527,245	6,224,826
Taxes payable	8,396,449	6,209,038
Claims payable, current	1,965,511	1,571,387
Guarantee deposit and contract retainer	2,951,291	3,375,745
Other accounts payable	542,315	291,163
	$ 52,190,656	$ 103,719,734

Revenue Recognition

Service rates are authorized by City of Seattle ordinances. Billings are made to customers on a monthly or bimonthly basis. Revenues for energy delivered to customers between the last billing date and the end of the year are estimated and reflected in the accompanying financial statements under the caption unbilled revenues.

The Department's customer base is comprised of four identifiable groups, which accounted for electric energy sales as follows:

	2001	*2000*
Residential	37.3%	38.2%
Commercial	41.6	41.0
Industrial	12.3	12.1
Governmental	8.8	8.7
	100.0%	100.0%

Use of Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements. The Department used significant estimates in determining reported unbilled revenues, energy contract assets and liabilities, accumulated provision for injuries and damages, allowance for doubtful accounts, accrued sick leave, and other contingencies. Actual results may differ from those estimates.

Significant Risk and Uncertainty

The Department is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include prices on the wholesale market for short-term power, interest rates, water conditions, weather, and natural disaster related disruptions; terrorism; collective bargaining labor disputes; fish and other Endangered Species Act (ESA) issues; Environmental Protection Agency regulations; federal government regulations or orders concerning the operations, maintenance, and/or licensing of hydroelectric facilities; other governmental regulations; and the deregulation of the electrical utility industry.

Reclassifications

Certain 2000 account balances have been reclassified to conform to the 2001 presentation.

Note 2: Jointly Owned Plant

The Department was one of eight public and private utilities that constructed and owned as tenants-in-common a 1,343 megawatt (MW) coal-fired, steam-electric generating plant located near Centralia, Washington. The Department's ownership interest was 8% until May 7, 2000, when the plant was sold to TransAlta Corporation, a Canadian corporation. Proceeds received from the sale were $41.4 million and the gain on the sale was $29.6 million. The Department's share of operating expenses and plant investment associated with the Centralia Steam Plant is included in the accompanying financial statements until the date of sale.

Note 3: Cash and Equity in Pooled Investments and Investments

The City pools and invests all temporary cash surpluses for City departments. These residual investments may consist of deposits with qualified public depositories; obligations of the United States or its agencies or wholly owned corporations; obligations of eligible government-sponsored enterprises; and certain bankers' acceptances, commercial paper, general obligation bonds or warrants, repurchase agreements, reverse repurchase agreements, mortgage-backed securities, and derivative-based securities; and are in accordance with the Revised Code of Washington (RCW) 35.39.032 and 39.58. According to City policy, securities purchased will have a maximum maturity of no longer than 15 years, and the average maturity of all securities owned should be no longer than five years. Also by City policy, the City may operate a securities lending program, and there were transactions during 2001 and 2000. There were no securities lending program transactions outstanding at December 31, 2001 or 2000. The Department's equity in residual investments is reflected as cash and equity in pooled investments. The City's residual investment pool did not include reverse repurchase agreements at the end of 2001 or 2000; the City did not invest in such instruments during 2001 but did invest in such instruments in 2000. Derivative-based securities were owned by the City pool during 2001 and 2000 and at both year ends. These securities were callable U.S. government agency instruments. Earnings and adjustments to fair value from the investment pool are prorated monthly to City departments based on the average daily cash balances of participating funds.

Banks or trust companies acting as the City's agents hold most of the City's investments in the City's name, with respect to credit risk as defined in GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements.* All transactions are executed with authorized security dealers, financial institutions, or securities lending agents on a delivery versus payment basis.

The first $100,000 of bank deposits are federally insured. The Washington State Public Deposit Protection Commission (PDPC) collateralizes deposits in excess of $100,000. The PDPC is a multiple financial institution collateral pool. There is no provision for the PDPC to make additional pro rata assessments if needed to cover a loss. Therefore, the PDPC protection is of the nature of collateral, not of insurance.

Securities with maturities exceeding three months at time of purchase are reported at fair value on the balance sheets; the net increase (decrease) in the fair value of those investments is reported as part of investment income. At December 31, changes in the fair value of investments resulted in unrealized gains of $907,046 and $862,604 for 2001 and 2000, respectively.

The cash pool operates like a demand deposit account in that all City departments, including the Department, may deposit cash at any time and can also withdraw cash out of the pool without prior notice or penalty. Accordingly, the statements of cash flows reconcile to cash and equity in pooled investments.

Cash and cash equivalents included in cash and equity in pooled investments at December 31 consist of:

	2001	*2000*
Restricted assets:		
Municipal Light & Power Bond Reserve Account	$ 3,609,215	$ 15,682,128
Bond proceeds and other	3,236,017	1,171,566
Special deposits and other	6,605,501	3,375,745
	13,450,733	20,229,439
Current assets	202,321	5,642,338
	$ 13,653,054	$ 25,871,777

Equity in pooled investments, U.S. government securities, and investments that include commercial paper are reported at fair values based on quoted market prices for those or similar securities and are as follows at December 31:

	2001	*2000*
Restricted assets:		
Municipal Light & Power Bond Reserve Fund:		
Equity in pooled investments	$ 67,384,243	$ 37,404,895
U.S. government securities	-	13,348,344
Bond proceeds and other:		
Equity in pooled investments	60,323,459	2,798,232
Investments	102,274,374	-
	229,982,076	53,551,471
Current assets:		
Equity in pooled investments	3,556,697	13,399,585
	$ 233,538,773	$ 66,951,056

Note 4: Long-term Debt

Prior Lien Bonds

In March 2001, the Department issued $503.7 million in ML&P Improvements and Refunding Revenue Bonds that bear interest at rates ranging from 5.00% to 5.50% and mature serially from March 1, 2004, through 2026. The arbitrage yield for the 2001 bonds is 4.99%. Arbitrage yield, when used in computing the present worth of all payments of principal and interest on the bonds, produces an amount equal to the issue price of the bonds. Proceeds were used to finance certain capital improvements and conservation programs and to defease certain outstanding prior lien bonds. As of the end of the year, $161.7 million in proceeds remained from the 2001 bond issue that will be used to fund a significant portion of the ongoing capital improvement and conservation program.

The debt service on the refunding bonds requires a cash flow of $194.67 million, including $70.07 million in interest. The difference between the cash flows required to service the old and the new debt and complete the refunding totaled ($0.3) million, and the aggregate economic gain totaled $5.13 million at net present value.

In December 2000, the Department issued $98.8 million in ML&P Revenue Bonds that bear interest at rates ranging from 4.5% to 5.625% and mature serially from December 1, 2006, through 2025. Proceeds from the 2000 bond issue were used to finance a portion of the Department's ongoing capital improvement and conservation program.

Prior lien bonds outstanding at December 31, 2001, totaled $1.37 billion. Principal redemptions extend through 2026, with interest to be paid at rates ranging from 4.50% to 6.00%. Future debt service requirements on these bonds are as follows:

Year ending December 31,	*Principal redemptions*	*Interest requirements*	*Total*
2002	$ 38,291,500	$ 72,403,329	$ 110,694,829
2003	39,250,000	70,472,017	109,722,017
2004	47,650,000	68,296,087	115,946,087
2005	50,176,000	65,766,732	115,942,732
2006	52,750,000	63,192,604	115,942,604
Thereafter	1,138,145,000	588,728,721	1,726,873,721
	$1,366,262,500	$ 928,859,490	$ 2,295,121,990

The Department is required by ordinance to fund reserves for prior lien bond issues in an amount equal to the lesser of (a) the maximum annual debt service on all bonds secured by the reserve account or (b) the maximum amount permitted by the Internal Revenue Code (IRC) of 1986 as a reasonably required reserve or replacement fund. Upon issuance of the 2001 bonds, the maximum annual debt service on prior lien bonds increased from $92.1 million to $115.9 million. The IRC's requirement increased from $77.3 million to $105.6 million. At December 31, 2001, the balance in the reserve account was $70.9 million at fair value. The reserve must be fully funded by March 15, 2006.

In addition to the 2001 refunding revenue bonds, the Department has previously issued several refunding revenue bonds for the purpose of defeasing certain outstanding prior lien bonds. Refunding revenue bonds were issued in 1998 and 1993. Proceeds from the refunding bonds were placed in separate irrevocable trusts to provide for all future debt service payments on the bonds defeased. Accordingly, neither the assets of the respective trust accounts nor the liabilities for the defeased bonds are reflected in the Department's financial statements. The bonds defeased in 2001, 1998, and 1993 had outstanding balances at cost of $98.3 million, $94.7 million, and $8.2 million as of December 31, 2001, respectively. Funds held in the respective trust accounts on December 31, 2001, will be sufficient to service and redeem the defeased bonds.

Subordinate Lien Bonds

The Department is authorized to issue a limited amount of adjustable rate revenue bonds, which are subordinate to prior lien bonds with respect to claim on revenues. Subordinate lien bonds may be issued to the extent that the new bonds will not cause the aggregate principal amount of such bonds then outstanding to exceed the greater of $70 million or 15% of the aggregate principal amount of prior lien bonds then outstanding. Subordinate bonds may be remarketed daily, weekly, short-term, or long-term and may be converted to prior lien bonds when certain conditions are met.

In December 1996, the Department issued ML&P Adjustable Rate Revenue Bonds in the amount of $19.8 million, subject to a mandatory redemption schedule spanning the period from June 1, 2002, to June 1, 2021. These bonds were marketed weekly at an interest rate ranging from 1.05% to 4.70% during 2001. Proceeds were used to finance a portion of the capital improvement and conservation program.

The 1990 bonds and 1991 Series B bonds outstanding at December 31, 2001, were $20.7 million and $18.3 million, respectively, and were marketed on a short-term basis during 2001, with interest rates ranging from 1.55% to 5.00%.

The 1991 Series A bonds and the 1993 bonds were $25.0 million and $19.6 million, respectively, at December 31, 2001, and were priced weekly at interest rates from 1.00% to 5.00% in 2001.

As of December 31, 2001, the Department had outstanding subordinate lien bonds totaling $103.4 million. Future principal redemptions and interest requirements on these bonds, based on estimated interest rates ranging from 3.00% to 4.008% through year 2021, are as follows:

Year ending December 31,	*Principal redemptions*	*Interest requirements*	*Total*
2002	$ 3,360,000	$ 2,690,344	$ 6,050,344
2003	3,585,000	3,176,954	6,761,954
2004	4,115,000	3,181,340	7,296,340
2005	4,445,000	3,158,375	7,603,375
2006	4,775,000	3,194,871	7,969,871
Thereafter	83,120,000	20,697,388	103,817,388
	$ 103,400,000	$ 36,099,272	$ 139,499,272

Revenue Anticipation Notes

In March 2001, the Department issued $182.2 million in ML&P Revenue Anticipation Notes (RANs). $136.7 million of the RANs bear interest at a rate of 4.50%, and $45.5 million bear interest at a rate of 5.25%. The arbitrage yield of the RANs is 3.75%. The RANs mature in March 2003 and are special limited obligations of the Department payable from and secured by gross revenues. Proceeds were used to finance 2001 operating expenses. The RANs are on a lien subordinate to prior lien bonds and subordinate lien bonds; there is no reserve account securing repayment, and there is no debt service coverage requirement. Debt service requirements for the RANs are as follows:

Year ending December 31,	*Principal redemptions*	*Interest requirements*	*Total*
2002	$ -	$ 8,541,075	$ 8,541,075
2003	182,210,000	4,199,362	186,409,362
	$ 182,210,000	$ 12,740,437	$ 194,950,437

Fair Value

The fair value of the Department's bonds and RANs is estimated based on the quoted market prices for the same or similar issues or on the current rates offered to the Department for debt of the same remaining maturities. Carrying amounts and fair values are as follows at December 31:

	2001		*2000*	
	Carrying amount	*Fair value*	*Carrying amount*	*Fair value*
Long-term debt:				
Prior lien bonds	$1,377,523,172	$1,385,989,653	$ 994,611,605	$ 925,154,114
Subordinate lien bonds	103,123,038	103,400,000	105,505,173	105,800,000
RANs	184,422,967	186,594,405	-	-
	$1,665,069,177	$1,675,984,058	$1,100,116,778	$ 1,030,954,114

Amortization

Bond issue costs, discounts, and premiums are amortized using the effective interest method over the term of the bonds.

The excess of costs incurred over the carrying value of bonds refunded on early extinguishment of debt is amortized as a component of interest expense using both the straight-line and bonds-outstanding methods over the terms of the issues to which they pertain. Deferred refunding costs amortized to interest expense totaled $2.1 million in 2001 and $4.0 million in 2000. Deferred refunding costs in the amount of $40.2 million and $37.2 million are reported as a component of long-term debt in the 2001 and 2000 balance sheets, respectively.

Note Payable

In late December 2001, the City of Seattle authorized an interfund loan (note payable) to the Department from the City's Consolidated (Residual) Cash Portfolio in an amount up to $110.0 million, of which $100.0 million was outstanding as of December 31, 2001. The purpose of the note payable is for working capital and is due on or before March 31, 2003. The loan was repaid on January 1, 2002, and will be carried as a negative operating cash balance. The interest rate for the note payable is equal to the rate of return earned by the City's Consolidated (Residual) Cash Portfolio. For December 2001, the rate of return was 5.341%.

Note 5: Seattle City Employees' Retirement System

The Seattle City Employees' Retirement System (SCERS) is a single-employer public employee retirement system, covering employees of the City of Seattle and administered in accordance with Chapter 41.28 of the Revised Code of Washington and Chapter 4.36 of the Seattle Municipal Code. SCERS is a department of the City of Seattle.

All employees of the City of Seattle are eligible for membership in SCERS with the exception of uniformed police and fire personnel who are covered under a retirement system administered by the state of Washington. As of the actuarial valuation date, there were 4,716 annuitants receiving benefits and 8,936 active members of SCERS. In addition, 1,263 vested terminated employees were entitled to future benefits, and 174 terminated employees had restored their contributions due to the provisions of the portability statutes and may be eligible for future benefits.

SCERS provides retirement, death, and disability benefits. Retirement benefits vest after five years of credited service, while death and disability benefits vest after 10 years of service. Retirement benefits are calculated, generally, as 2% multiplied by years of creditable service, multiplied by average salary, based on the highest 24 consecutive months, excluding overtime. The benefit is actuarially reduced for early retirement.

Actuarially recommended contribution rates both for members and for the employer were 8.03% of covered payroll during 2001 and 2000.

SCERS issues stand-alone financial statements that may be obtained by writing to the Seattle City Employees' Retirement System, 801 Third Avenue, Suite 300, Seattle, Washington 98104; telephone: (206) 386-1292.

Employer contributions for the City of Seattle were $32.7 million, $30.8 million, and $29.7 million in 2001, 2000, and 1999, respectively, and the annual required contributions were made in full.

Actuarial data	
Valuation date	January 1, 2001
Actuarial cost method	Entry age
Amortization method	Level percent
Amortization period of the funding excess from January 1, 2001	30 years
Asset valuation method	Market

*Actuarial assumptions**	*Percentage*
Investment rate of return	8.00 %
Projected general wage increases	4.50
Cost-of-living year-end bonus dividend	0.67

* Underlying price inflation at 4.0%.

Schedule of funding progress for the City of Seattle (dollar amounts in millions):

Actuarial valuation date	*Actuarial value of assets (a)*	*Actuarial accrued liabilities (AAL) entry age [1] (b)*	*Funding Excess [2] (b-a)*	*Funding ratio (a/b)*	*Covered payroll [3] (c)*	*Funding excess as a percentage of covered payroll ((b-a)/ c)*
1/1/1999	$ 1,375.0	$ 1,326.6	$ (48.4)	103.6 %	$ 370.4	(13.1) %
1/1/2000	1,582.7	1,403.1	(179.6)	112.8	370.4	(48.5)
1/1/2001	1,493.1	1,490.3	(2.8)	100.2	383.7	(.7)

1. Actuarial present value of benefits less actuarial present value of future normal costs based on entry age actuarial cost method.
2. Actuarial accrued liabilities less actuarial value of assets: funding excess if negative.
3. Covered payroll includes compensation paid to all active employees on which contributions are calculated.

Note 6: Deferred Compensation

The Department's employees may contribute to the City of Seattle's Voluntary Deferred Compensation Plan (the Plan). The Plan, available to City employees and officers, permits participants to defer a portion of their salary until future years. The deferred compensation is paid to participants and their beneficiaries upon termination, retirement, death, or unforeseeable emergency.

Effective January 1, 1999, the Plan became an eligible deferred compensation plan under Section 457 of the IRC of 1986, as amended, and a trust exempt from tax under IRC Sections 457(g) and 501(a). The Plan is operated for the exclusive benefit of participants and their beneficiaries. No part of the corpus or income of the Plan shall revert to the City or be used for, or diverted to, purposes other than the exclusive benefit of participants and their beneficiaries.

The Plan is not reported in the financial statements of the City or the Department.

It is the opinion of the City's legal counsel that the City has no liability for investment losses under the Plan. Under the Plan, participants select investments from alternatives offered by the Plan Administrator, who is under contract with the City to manage the Plan. Investment selection by a participant may be changed from time to time. The City does not manage any of the investment selections. By making the selection, participants accept and assume all risks inherent in the Plan and its administration.

Note 7: Long-term Purchased Power and Wholesale Power Transactions

Bonneville Power Administration

The Department purchased electric energy from the U.S. Department of Energy, Bonneville Power Administration (BPA) under a long-term contract, which expired September 30, 2001.

Until August 1, 1996, the Department was an actual computed requirements customer of BPA and was entitled to buy from BPA the energy required to fill the variance between its customer load and its firm power resources. The Department had a right to displace this entitlement, by payment of an availability charge. Effective August 1, 1996, the contract with BPA was amended, through the remaining life of the contract, to limit purchases to 195 average megawatts (aMW) delivered flat throughout the year. The Department could displace part of this amount by paying an availability charge; almost no BPA energy was displaced in 2001 and 1.3 aMW was displaced in 2000. Power purchased under this contract was 195.0 aMW through September 30, 2001, and 193.7 aMW in 2000. The 1996 contract amendment required payment of a diversity fee of $2 million, which was amortized through September 30, 2001.

In October 2000, the Department entered into a new agreement to purchase power from BPA for a 10-year period beginning October 1, 2001, under the Block and Slice Power Sales Agreement. Under the terms of the agreement the Department will receive firm power of 154 aMW in the first year, 144.8 aMW in the second through fifth years of the contract, and 259.2 aMW in the last 5 years of the contract as a block of power shaped to the Department's monthly net requirements, defined as the difference between projected monthly load and firm resources available to serve that load. Additional amounts of power will be purchased and received throughout the term of the contract under the Slice portion of the contract. The terms of the Slice product specify that the Department will receive a fixed percentage (4.6676%) of the actual output of the Federal Columbia River Power System. The price of the Slice power is based on the same percentage (4.6676%) of the expected costs of the system and is subject to adjustments based on actual costs. Under critical water conditions, the Department is expected to receive approximately 280.6 aMW of energy in the first year of the contract, and 330 aMW for the remaining term of the contract, from the Slice product. The actual amounts of firm and non-firm energy will vary with water conditions, federal generating capabilities, and fish and wildlife restoration requirements. Estimated payments over the 10-year contract total $1.6 billion. Amendments to the contract through March 2002 provided that BPA will pay the Department for energy savings in federal fiscal years 2002 and 2003. The Department has received $9.9 million as of April 15, 2002, and will receive a total of $27.7 million through July 2003 for these energy reductions. The estimated reduction of energy associated with these payments is 9.8 aMW the first year of the contract and 19.0 aMW in years two through ten.

In 1983, the Department entered into separate net billing agreements with BPA and Energy Northwest (formerly the Washington Public Power Supply System), a municipal corporation and joint operating agency of the state of Washington, with respect to sharing costs for the construction and operation of three nuclear generating plants. Under these agreements, the Department is unconditionally obligated to pay Energy Northwest a pro rata share of the total annual costs, including debt service, to finance the cost of construction, whether or not construction is completed, delayed, or terminated, or operation is suspended or curtailed. The net billing agreements provide that these costs be recovered through BPA rates. One plant is in commercial operation. Construction of the other two plants has been terminated.

Lucky Peak

In 1984, the Department entered into a purchase power agreement with four irrigation districts to acquire 100% of the net output of a hydroelectric facility constructed in 1988 at the existing Army Corps of Engineers Lucky Peak Dam on the Boise River near Boise, Idaho. The irrigation districts are owners and license holders of the project. The agreement, which expires in 2038, obligates the Department to pay all ownership and operating costs, including debt service, over the term of the contract, whether or not the plant is operating or operable.

The power purchased under this agreement was 21.5 aMW and 38.8 aMW in 2001 and 2000, respectively. To properly reflect its rights and obligations under this agreement, the Department includes as an asset and liability the outstanding principal of the project's debt, net of the balance in the project's reserve account.

British Columbia—Ross Dam

In 1984, an agreement was reached between the Province of British Columbia and the City of Seattle under which British Columbia will provide the Department with power equivalent to that which would result from an addition to the height of Ross Dam. The agreement was ratified through a treaty between Canada and the United States in the same year. The power is to be received for 80 years and began in 1986. The Department will make annual payments to British Columbia of $21.8 million through 2020, which represent the estimated cost the Department would have incurred for financing had the addition been constructed. The payments are charged to expense over a period of 50 years, through 2035.

The Department is also paying equivalent operation and maintenance costs. Payments made for this purpose totaled $160,774 and $153,499 in 2001 and 2000, respectively. The power purchased under this agreement was 35.1 aMW and 33.8 aMW and up to 143 MW and 175 MW of actual peak capacity in 2001 and 2000, respectively.

In addition to the direct costs of power under the agreement, the Department incurred costs of approximately $8 million in prior years related to the proposed addition and was obligated to help fund the Skagit Environmental Endowment Commission through four annual $1 million payments. These costs have been deferred and are being amortized to purchased power expense over 35 years.

Klamath Falls

In November 2000, the Department and the City of Klamath Falls, Oregon, entered into an agreement for the purchase of energy and capacity from the Klamath Falls Cogeneration Project, a 500 MW unit consisting of two combustion turbines fueled by natural gas and a steam generator. Under the terms of the contract, the Department receives 100 MW of capacity from the project beginning on the project's online date of July 29, 2001, and for five years thereafter, with an option to renew the contract for an additional five years. The power purchased under this agreement was 37.2 aMW. The Department assumes gas price and exchange rate risks for natural gas from Alberta, Canada. In April 2001, the Department entered into a separate contract to swap variable Canadian dollar gas prices for a fixed U.S. dollar gas price. Estimated payments total $155.8 million through July 31, 2006.

Wind Generation

In October 2001, the Department entered into an agreement with PacifiCorp Power Marketing, Inc. (PPMI) for the purchase of energy and associated environmental attributes primarily from the State Line Wind Project, a facility consisting of 399 660-kW wind turbines located in Walla Walla County, Washington and Umatilla County, Oregon. The Department will receive firm energy with an aggregate maximum delivery rate per hour of 50 MW from January 1, 2002, through July 31, 2002, and 100 MW from August 1, 2002, through December 31, 2021. The Department will also receive additional firm energy with an aggregate maximum delivery rate per hour of 25 MW from January 1, 2004, through June 30, 2004, and 50 MW from July 1, 2004, through December 31, 2021, from the State Line Wind Project or other qualifying new wind generation facility. PPMI may deliver, at their option, additional energy with a maxiumu delivery rate per hour of 25 MW beginning in 2004 from other new qualifying wind generation projects. The Department entered into a related 10-year agreement to purchase integration and exchange services from PacifiCorp, which receives State Line energy at the Wallula Substation in Walla Walla County, Washington, and another related 20-year agreement to sell integration and exchange services to PPMI. Net payments under the three contracts for purchase power and related integration and exchange services received and provided are estimated to be $467.4 million.

Other Long-term Purchase Power Agreements

The Department also purchases energy from Public Utility Districts (the PUDs) No. 1 of Pend Oreille County and No. 2 of Grant County, under agreements expiring October 31, 2005; the Grand Coulee Project Hydroelectric Authority (the Authority), which includes the South, East, and Quincy Columbia Basin Irrigation Districts under 40-year agreements that expire from 2022 to 2027; and the Columbia Storage Power Exchange, until expiration of the agreement on March 31, 2003. Power purchased under these contracts was 77.4 aMW in 2001 and 87.3 aMW in 2000. Rates under the PUD, excluding Pend Oreille County, and Authority contracts represent the share of the operating and debt service costs in proportion to the share of total energy to which the Department is entitled, whether or not these plants are operating or operable.

Three new contracts were executed in March 2002 with Grant County to replace the contract expiring October 31, 2005. The agreements are effective November 1, 2005, and run concurrent with the term of the future federal relicense period.

Estimated Payments Under Purchase Power Contracts

The Department's estimated payments under its contracts with BPA, excluding receipts from BPA for energy savings in accordance with amendments to the BPA Block and Slice Power Sales Agreement through March 2002; the PUDs; irrigation districts; power exchange corporation; Lucky Peak Project; British Columbia – Ross Dam; Klamath Falls; and with PPMI and PacifiCorp for wind energy and net integration and exchange services for the period from 2002 through 2021 are:

Year ending December 31,	*Estimated payments*
2002	$ 240,362,641
2003	233,151,008
2004	243,790,651
2005	246,406,166
2006	229,894,505
Thereafter	1,571,689,830
	$ 2,765,294,801

Payments under these long-term contracts totaled $135.0 million in 2001 and $50.3 million in 2000. Energy received represented 99.7% of the Department's total purchases under firm power contracts during 2001 and 99.8% during 2000.

Wholesale Power Transactions

Power transactions in response to seasonal resource and demand variations include purchases and sales at market under short-term agreements and exchanges of power under long and short-term contracts. Wholesale power purchase contract commitments outstanding at December 31, 2001 and 2000 were $2.9 million and $42.5 million, respectively. For power sales forward contracts, there were $42.7 million outstanding as of December 31, 2001, and no outstanding commitments as of December 31, 2000. Fluctuations in annual precipitation levels and other weather conditions materially affect the energy output from the Department's hydroelectric facilities. Accordingly, power transactions in and out may vary significantly from year to year.

In March 1998, the Department was certified as a scheduling coordinator with the California Independent System Operator to submit schedules and sell power and ancillary services in California.

Note 8: Other Assets

Other assets are comprised of deferred conservation costs and other deferred charges. Deferred conservation costs, net, represent programmatic conservation costs. City Council-passed resolutions authorize the debt financing and deferral of all programmatic conservation costs incurred by the Department. These costs are to be recovered through rates over 20 years.

Other deferred charges, net, consist of the following at December 31:

	2001	*2000*
Deferred power costs	$ 300,000,000	$ -
British Columbia–Ross Dam	22,574,618	13,701,177
Unrealized losses from fair valuations of:		
Gas price swap	13,860,917	-
Short-term forward sales of electric energy	915,407	-
Skagit relicensing and environmental	12,388,412	11,555,540
Unamortized debt expense	4,103,307	2,206,129
Puget Sound Energy interconnection and substation	2,148,197	2,291,110
General work in process to be billed	1,124,420	2,453,084
Other	414,850	1,611,405
	$ 357,530,128	$ 33,818,445

Deferred power costs incurred for short-term wholesale power purchases during 2001 will be recovered through rates over the next two years and possibly longer, pursuant to SFAS No. 71 and Ordinance 120385. Unamortized charges for the deferral of debt payments relating to Ross Dam will be amortized between 2021 and 2035. The balance of these charges, excluding billable work in progress, are being amortized to expense over four to 36 years.

Note 9: Deferred Credits

Deferred credits consist of the following at December 31:

	2001	*2000*
Unrealized gains from fair valuation of short-term forward sales of electric energy	$ 14,490,436	$ -
Levelized lease payments for Seattle office	1,263,337	1,595,373
Prepaid capital fees	1,819,000	-
Unspent transfer from the City of Seattle	965,977	-
Other	533,015	120,611
	$ 19,071,765	$ 1,715,984

Note 10: Provision for Injuries and Damages

The Department is self-insured for casualty losses to its property, for environmental cleanup, and for certain losses arising from third-party damage claims. The Department establishes liabilities for claims based on estimates of the ultimate cost of claims. The length of time for which such costs must be estimated varies depending on the nature of the claim. Actual claims costs depend on such factors as inflation, changes in doctrines of legal liability, damage awards, and specific incremental claim adjustment expenses. Claims liabilities are recomputed periodically using actuarial and statistical techniques to produce current estimates, which reflect recent settlements, claim frequency, industry averages, city-wide cost allocations, and other economic and social factors. Liabilities for lawsuits, claims, and workers' compensation were discounted over a period of 11 to 16 years in 2001 and 12 to 16 years in 2000 at the City's average annual rate of return on investments, which was 5.341% in 2001 and 6.167% in 2000. Liabilities for environmental cleanup and for casualty losses to the Department's property do not include claims that have been incurred but not reported (IBNR) and are not discounted due to uncertainty with respect to regulatory requirements and settlement dates, respectively.

The schedule below presents the changes in the provision for injuries and damages during 2001 and 2000:

	2001	*2000*
Unpaid claims at January 1	$ 8,023,794	$ 6,628,762
Payments	(2,664,709)	(1,501,512)
Incurred claims	2,731,731	2,896,544
Unpaid claims at December 31	$ 8,090,816	$ 8,023,794

The provision for injuries and damages is included in current and noncurrent liabilities as follows:

	2001	*2000*
Noncurrent liabilities	$ 6,125,305	$ 6,452,407
Accounts payable and other	1,965,511	1,571,387
	$ 8,090,816	$ 8,023,794

Note 11: Commitments and Contingencies

Operating Leases

In December 1994, the City entered into an agreement on behalf of the Department for a 10-year lease of office facilities in downtown Seattle commencing February 1, 1996. In early 1996, the City purchased the building in which these facilities are located, thus becoming the Department's lessor.

The Department also has two other long-term operating leases for smaller facilities used for office and storage purposes.

Expense under the leases totaled $3.3 million and $3.5 million in 2001 and 2000, respectively. Deferred credits related to the 10-year lease of office facilities in downtown Seattle totaled $1.3 million and $1.6 million at December 31, 2001 and 2000, respectively.

Minimum payments under the leases are:

Year ending December 31,	*Minimum payments*
2002	$ 3,515,583
2003	3,488,500
2004	3,360,971
2005	3,371,641
2006	280,970
	$ 14,017,665

Other

Associated with the FERC operating license for the Skagit Hydroproject, which is in effect until the year 2025, are settlement agreements that commit the Department to undertake certain mitigation activities. The mitigation cost was estimated at December 31, 2001, to be $42.9 million, of which $31.6 million has been expended.

The estimated financial requirement for the Department's 2002 capital improvement and conservation program is $135.4 million, and the Department has substantial contractual commitments relating thereto.

Some fish species that inhabit waters where hydroelectric projects are owned by the Department or where the Department purchases power have been listed under the ESA as either threatened or endangered. In 1995, the National Marine Fisheries Service (NMFS) developed a broad species recovery plan for the Columbia River Basin and supplemental plans in 1998 and 2000, based on Biological Opinions relating to the Columbia and Snake River fisheries. As a result, the Department's power generation at its Boundary Project has been reduced in the fall and winter when the region experiences its highest sustained energy demand, and the Boundary Project's firm capability has also been reduced. In addition, the Department now receives power under a contract with the BPA that provides the City with a percentage of the total BPA generation and the Department would thus be affected by changes in flows required in the Biological Opinions. In the opinion of the Department, it is unlikely that new Biological

Opinions will result in significant changes in flows that would affect the Boundary Project, Priest Rapids, and BPA system. While it is unclear how other fish listings, including bull trout and Chinook salmon, may affect the Department's hydroelectric projects and operations, the Department has entered into agreements that include extensive measures to protect fish and were intended to mitigate potential impacts of its projects on the Cedar, Skagit, and South Fork Tolt rivers. In addition, the Department is conducting research on these species to monitor their population health and identify potential impacts. The Department is carrying out an ESA Early Action program that will assist in the recovery of Chinook and bull trout and address any further impacts on these species.

All hydroelectric projects must satisfy the requirements of the Clean Water Act to obtain a FERC license. An agreement was reached for the Newhalem Creek plant on minimum stream flows necessary to protect fish; these flows were incorporated into the FERC license issued in 1997. The Department has installed a new intake system capable of delivering the approved instream flows. The completion of the intake system, including all improvements and testing, was reported to FERC August 2001. The new system has been performing reliably since this time.

Effective November 22, 1999, the Department committed to pay a total of $11.6 million over 10 years, ending in 2008 to Pend Oreille County on behalf of the county and certain school districts and towns located therein to compensate for loss of revenues and additional financial burdens associated with the Department's operation of the Boundary Hydroelectric Project on the Pend Oreille River. The combined impact compensation and retroactive payment totaled $1.1 million for 2001 and $1.0 million for 2000.