

***The City of Seattle—
City Light Department***

Enterprise Fund of The City of Seattle

*Financial Statements as of and for the
Years Ended December 31, 2010 and 2009,
Required Supplementary Information, and
Independent Auditors' Report*

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

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INDEPENDENT AUDITORS' REPORT

Energy, Technology, and Civil Rights Committee
The City of Seattle—City Light Department
Seattle, Washington

We have audited the accompanying balance sheets of The City of Seattle—City Light Department (the Department) as of December 31, 2010 and 2009, and the related statements of revenues, expenses, and changes in equity and cash flows for the years then ended. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1 to the financial statements, the financial statements referred to above present only the Department and are not intended to present fairly the financial position and results of operations of The City of Seattle, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Department as of December 31, 2010, and 2009, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, the Department adopted the provisions of Governmental Accounting Standards Board Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, effective January 1, 2009. In addition, as discussed in Note 1 to the financial statements, the Department adopted the provisions of Governmental Accounting Standards Board Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, effective January 1, 2010.

Energy, Technology, and Civil Rights Committee
The City of Seattle—City Light Department

The Management's Discussion and Analysis and Schedules of Funding Progress information enclosed in this report are not a required part of the basic financial statements, but are 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.

Baker Tilly Viechow Krause, LLP

Madison, Wisconsin
April 30, 2011

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010, 2009, and 2008

The following discussion and analysis of the financial performance of The City of Seattle—City Light Department (the Department) provides a summary of the financial activities for the years ended December 31, 2010, 2009, and 2008. This discussion and analysis should be read in combination with the Department's financial statements, which immediately follow this section.

ORGANIZATION

The Department is the public electric utility of The City of Seattle (the City). As an enterprise fund of the City, the Department owns and operates certain generating, transmission, and distribution facilities and supplies electricity to approximately 399,000 customers in Seattle and certain surrounding communities. The Department also supplies electrical energy to other City agencies at rates prescribed by City ordinances.

OVERVIEW OF THE FINANCIAL STATEMENTS

The Department's accounting records are maintained in accordance with generally accepted accounting principles for proprietary funds as prescribed by the Governmental Accounting Standards Board (GASB) and, where not in conflict with GASB pronouncements, accounting principles prescribed by the Financial Accounting Standards Board (FASB). The Department's accounting records follow the Uniform System of Accounts for Public Licensees prescribed by the Federal Energy Regulatory Commission (FERC).

This discussion and analysis is intended to serve as an introduction to the Department's basic financial statements, which are comprised of the financial statements and the notes to the financial statements and include the following:

Balance Sheets, Statements of Revenues, Expenses, and Changes in Equity, and Statements of Cash Flows—The basic financial statements provide an indication of the Department's financial health. The balance sheets include all of the Department's assets and liabilities, using the accrual basis of accounting, as well as an indication about which assets can be utilized for general purposes, and which assets are restricted as a result of bond covenants and other commitments. The statements of revenues, expenses, and changes in equity report all of the revenues and expenses during the time periods indicated. The statements of cash flows report the cash provided and used by operating activities, as well as other cash sources such as investment income and cash payments for bond principal and capital additions and betterments.

Notes to the Financial Statements—The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

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CONDENSED BALANCE SHEETS

	December 31		
	2010	2009 (a)	2008 (a)(b)
Assets:			
Utility plant—net	\$2,073,105,948	\$1,955,519,016	\$1,803,642,985
Restricted assets	140,201,173	31,639,850	267,019,138
Current assets	234,991,204	186,779,956	223,131,080
Other assets	<u>221,485,452</u>	<u>202,600,671</u>	<u>191,905,392</u>
Total assets	<u>\$2,669,783,777</u>	<u>\$2,376,539,493</u>	<u>\$2,485,698,595</u>
Liabilities:			
Long-term debt	\$1,515,834,791	\$1,299,349,321	\$1,444,574,242
Noncurrent liabilities	55,034,256	49,677,868	39,142,190
Current liabilities	166,474,305	174,532,295	181,149,971
Deferred credits	<u>77,815,560</u>	<u>28,726,364</u>	<u>30,736,545</u>
Total liabilities	<u>1,815,158,912</u>	<u>1,552,285,848</u>	<u>1,695,602,948</u>
Equity:			
Invested in capital assets—net of related debt	737,531,065	733,612,153	654,821,258
Restricted	25,128,822	25,928,099	26,231,479
Unrestricted	<u>91,964,978</u>	<u>64,713,393</u>	<u>109,042,910</u>
Total equity	<u>854,624,865</u>	<u>824,253,645</u>	<u>790,095,647</u>
Total liabilities and equity	<u>\$2,669,783,777</u>	<u>\$2,376,539,493</u>	<u>\$2,485,698,595</u>

(a) GASB 51 – *Accounting and Financial Reporting for Intangible Assets* was implemented in 2010. Accordingly, certain reclassifications were made to the 2009 and 2008 balance sheets to conform to the 2010 presentation. See Note 2 in the accompanying financial statements.

(b) GASB 53 – *Accounting and Financial Reporting for Derivative Instruments* was implemented in 2009. Accordingly, certain reclassifications were made to the 2008 balance sheet to conform to the 2009 presentation. See Note 6 in the accompanying financial statements.

ASSETS

Utility Plant - Net

In 2010, the Department adopted GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. An intangible asset, as defined, is an asset that lacks physical substance, is nonfinancial in nature, and has a useful life extending beyond a single reporting period, and should be recognized only if it is identifiable. The Department has intangible assets that consist of easements, purchased and internally developed software, and transmission rights. In 2010, certain assets previously recorded as *Other assets* by the Department met the criteria for intangible assets under GASB 51 and have been reclassified to *Utility*

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MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010, 2009, and 2008

plant along with related accumulated amortization. These assets include capitalized relicensing costs for the Skagit, Boundary, and Tolt projects, and costs incurred under the High Ross Agreement. Accordingly, such costs in the balance sheets for 2009 and 2008 have been reclassified to be consistent with the 2010 presentation.

2010 Compared to 2009

Utility Plant Assets net of accumulated depreciation and amortization increased \$117.6 million to \$2,073.1 million in 2010. Utility Plant Assets were comprised of *Hydroelectric production plant* \$673.8 million which increased \$22.0 million, *Transmission plant* \$158.3 million which increased \$6.4 million, *Distribution plant* \$1,727.1 million which increased \$110.8 million, *General plant* \$291.2 million which increased \$11.3 million, and *Intangible assets* \$355.0 million which increased \$28.9 million. These increases were offset by a \$66.8 million increase in *Accumulated depreciation and amortization*.

The \$110.8 million increase in *Distribution plant* is primarily due to \$25.2 million for underground conductors, \$20.0 million for poles/towers, \$19.7 million for underground conduit, \$11.0 million for transformers, \$10.2 million for overhead conductors, \$5.8 million for streetlights, and \$5.0 million for overhead services. Other components of Utility Plant Assets included *Construction work-in-progress* \$147.0 million which decreased \$0.7 million, *Land and land rights* \$90.5 million which increased \$7.7 million, and other assets of \$14.4 million which decreased \$1.9 million. The \$7.7 million increase in *Land and land rights* is primarily due to the purchase of land bordering the North Service Center for \$2.9 million and land purchases at Skagit aided by State of Washington grants for \$3.4 million.

More information on the Department's capital assets can be found in Note 2 of the accompanying financial statements.

2009 Compared to 2008

Utility Plant Assets net of accumulated depreciation and amortization increased \$151.9 million to \$1,955.5 million in 2009. Utility Plant Assets were comprised of *Hydroelectric production plant* \$651.9 million which increased \$8.8 million, *Transmission plant* \$151.9 million which increased \$16.5 million, *Distribution plant* \$1,616.3 million which increased \$78.9 million, *General plant* \$279.9 million which increased \$14.8 million and *Intangible assets* \$326.1 million which increase \$20.6 million. These increases were offset by a \$65.4 million increase in *Accumulated depreciation and amortization*.

The \$78.9 million increase in *Distribution plant* is primarily due to \$20.8 million for underground conduit, \$18.4 million for underground conductors, \$11.3 million for transformers, \$9.8 million for poles and \$8.5 million for services. Other components of Utility Plant Assets included *Construction work-in-progress* \$147.8 million which increased \$35.4 million, *Land and land rights* \$82.8 million which increased \$40.9 million and other assets \$16.3 million which increased \$1.4 million. The \$40.9 million increase in *Land and land rights* is primarily due to the purchase of two Greyhound properties in the amount of \$39.1 million for a proposed new substation.

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MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010, 2009, and 2008

Restricted Assets

2010 Compared to 2009

Restricted assets increased by \$108.6 million to \$140.2 million in 2010. During 2010, a *Rate Stabilization Account* (RSA) was funded in the amount of \$79.3 million in accordance with Ordinance No. 123260 (see Note 3 in the accompanying financial statements for more information on the RSA). Initial funding for the RSA included \$25.0 million transferred from the *Contingency Reserve Account* established in 2005 by Ordinance No. 121812 and cash from operations.

At the end of 2010, there was a balance of \$57.0 million remaining in *Construction* funds from unspent 2010 bond proceeds that will continue to fund a portion of the capital improvement program in 2011. At the end of 2009, all of the bond proceeds from the 2008 bond issue had been spent.

Other restricted assets decreased by \$2.7 million primarily due to the fact that there was no debt service payment due on January 1, 2011 compared to the end of 2009 when a debt service payment was due on January 1, 2010.

2009 Compared to 2008

Restricted assets decreased by \$235.4 million to \$31.6 million in 2009, principally the result of drawing all of the \$235.9 million remaining bond proceeds from the 2008 bond issue. Funds in *Construction* were spent on the ongoing capital improvement program and \$72.0 million was used to repay all variable rate bonds in February 2009.

The *Contingency Reserve Account* remained constant at \$25.0 million from 2008. This account was established by Ordinance No. 121812 in 2005 and was restricted for extraordinary costs associated with the operation of the electric system.

Current Assets

2010 Compared to 2009

Current Assets increased by \$48.2 million to \$235.0 million at the end of the year.

Operating cash increased \$24.2 million driven primarily by changes in electric rates adopted for 2010 and reimbursements from *Construction* for capital expenditures partially offset by lower net wholesale power revenues, lower debt service as a result of advance refunding certain higher interest bearing prior lien bonds, and spending for normal operations during the year.

Accounts receivable, net, which includes interfund receivables, increased \$15.4 million mainly due to higher retail electric sales of nearly \$13.0 million resulting from the 13.8% rate increase effective January 1, 2010 and the 4.5% rate increase implemented on May 1, 2010 to fund the RSA. Other accounts receivables increased \$2.6 million for wholesale power and \$2.2 million for federal bond interest subsidies. Increases in the allowance for doubtful accounts for retail electric sales and sundry sales attributable to the continuing recessionary local economy accounted for the majority of the change in the net balance.

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Unbilled revenues were higher by \$9.5 million due for the most part to the rate increases during 2010. *Materials and supplies* inventory was lower by \$1.3 million, in connection with an initiative to improve management in this area. Other increases totaling \$0.4 million net were incurred during the normal course of operations.

2009 Compared to 2008

Current assets decreased by \$36.4 million to \$186.8 million during 2009 related to decreases in *Operating cash* of \$30.4 million, *Accounts receivable* of \$3.3 million, and other of \$2.7 million.

Operating cash was lower due to a significant decrease in net wholesale revenues, investment earnings, spending to fund a portion of the capital improvement program from operations, spending for normal operations, and offset by receipts for retail power revenues.

Retail electric power *Accounts receivable* increased \$2.0 million in part due to BPA's pass-through rate increase of 1.8% in October 2009 which was offset by lower *Wholesale power receivables* of \$3.4 million at the end of 2009. Other receivables declined \$1.9 million generally as a result of lower *Capital contributions receivables* at the end of the year.

Other current assets decreased \$2.7 million because of reduced *Materials and supplies* inventory available at year end related to an initiative to improve material and supply management.

Other Assets

2010 Compared to 2009

ASC 980-10-05, *Effects of Regulatory Accounting*, provides for the deferral of certain utility costs and related recognition in future years as the costs are recovered through future rates. Deferred costs are authorized by resolutions passed by the Seattle City Council and include capitalized conservation costs, deferral of payments to the Province of British Columbia under the High Ross Agreement, regulatory deferred charges associated with energy transactions, and other deferred charges.

During 2010, deferral of payments to the Province of British Columbia, and deferred relicensing costs for the Skagit, Boundary, and Tolt projects were reclassified to plant in service as a result of implementing GASB 51 noted above in Utility Plant – net.

Other assets increased by \$18.9 million to \$221.5 million attributable almost entirely to the increase in *Deferred conservation costs, net* of \$16.3 million. The Department continues to place a high priority on conservation investment as the primary means to maintain the necessary long-term balance between electric demand and supply. Additional increases in deferred assets were related to net deferred bond-related costs and a loan to another city department for improving lighting efficiency in the city owned building housing the Department's administrative offices.

Details for Other deferred charges and assets, net, are provided in Note 11 of the accompanying financial statements.

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2009 Compared to 2008

Other assets increased \$10.7 million to \$202.6 million in 2009. *Deferred conservation costs, net* increased \$12.6 million and were offset by a net decrease of \$1.9 million in other charges incurred in the normal course of operations.

LIABILITIES

Long-Term Debt

2010 Compared to 2009

Long-term debt increased a net \$216.5 million to \$1,515.8 million in 2010. In late May 2010, the Department issued \$791.8 million of revenue and refunding revenue bonds. Specifically, \$181.6 million of 2010A series taxable Build America Bonds, \$596.9 million of 2010B series tax-exempt power improvement and refunding revenue bonds, and \$13.3 million of 2010C series taxable Recovery Zone Economic Development bonds were issued to fund the ongoing capital improvement program and to advance refund certain higher interest bearing prior lien revenue bonds. A total of \$570.7 million prior lien revenue bonds were advance refunded. In addition, \$67.4 million of prior lien bonds were repaid as scheduled during 2010. The balance of \$62.8 million was a net increase of bond premium, bond discount, and classification of bonds due within a year.

Debt to capitalization ratio was 64.3% at the end of 2010, an increase from the 62.6% ratio of 2009. The incremental increase was anticipated in accordance with the revised financial policies adopted in March 2010 and the increased need for debt funding of the capital program in both 2009 and 2010 due to lower net wholesale revenues.

Net revenues available to pay debt service were equal to 1.78x principal and interest on all bonds for 2010, slightly lower than the revised policy target of 1.8x due for the most part to lower net wholesale revenues and deferral of RSA revenues during 2010.

Bond ratings for the 2010 bonds and other outstanding parity bonds were affirmed at Aa2 from Moody's Investors Service and AA- from Standard and Poor's.

Note 7 of the accompanying financial statements provides additional information on the Department's long-term debt.

2009 Compared to 2008

Long-term debt decreased a net \$145.2 million to \$1,299.3 million in 2009. No bonds were issued in 2009, and as noted above in *Restricted assets*, \$72.0 million in variable bonds were repaid in February 2009. Furthermore, \$74.4 million of parity bonds were repaid during 2009.

The Department's debt to capitalization ratio at the end of 2009 was 62.6% compared to 65.9% at the end of 2008. Progress was made during 2009 towards a goal to achieve a debt to capitalization ratio of 60.0% by 2010. This goal was revised in March 2010 to specify that over any six year period, the Department should finance 40% of capital expenditures through cash from operations. Net revenues available to pay debt service were equal to 1.38x principal and interest on all bonds for 2009, lower than the policy target of 2.0x due

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primarily to lower wholesale revenues in 2009. Revised financial policies adopted in March 2010 specified a debt service coverage policy target of 1.8x.

During 2009, bond ratings on the Department's revenue bonds remained strong at Aa2 from Moody's Investors Service and AA- from Standard and Poor's.

Debt Service Coverage

Following is a table that provides additional detail for the Department's debt service coverage for years 2010, 2009, and 2008. The target level for debt service coverage was 1.8x on all bonds for 2010 in accordance with current financial policies (which include a Rate Stabilization Account that will result in greater compliance of actual debt service coverage with the policy-specified level). Previous financial policies had a target level of 2.0x for 2009 and 2008.

Debt Service Coverage	December 31		
	2010	2009	2008
Revenues:			
Total operating revenues	\$ 732,977,819	\$ 723,128,042	\$ 877,392,652
Less: Valuation of exchange power revenues	(33,034,404)	(30,130,061)	(82,224,825)
BPA Con Aug revenue	(6,043,110)	(5,963,898)	(5,901,204)
Investment income (a)	3,846,132	4,142,550	5,192,538
Gain on sale of property	80,959	28,921	3,149,564
Other income (expense), net, excluding CIAC	4,226,011	(445,469)	499,225
Total revenues	<u>\$ 702,053,407</u>	<u>\$ 690,760,085</u>	<u>\$ 798,107,950</u>
Expenses:			
Operation and maintenance	\$ 515,712,055	\$ 521,187,812	\$ 590,733,404
Add: FERC land use fees adjustment (b)	1,909,474	-	-
Less: Amortization and depreciation			
charged to operations (c)	(17,388,862)	(15,937,594)	(15,165,110)
Valuation of exchange power purchases	(33,103,126)	(31,888,325)	(81,664,264)
Non-cash write-offs	(387,247)	(1,644,036)	(3,459,159)
Net non-cash claims	(6,823,203)	(9,218,102)	1,019,033
Subtotal	<u>459,919,091</u>	<u>462,499,755</u>	<u>491,463,904</u>
Taxes, excluding City Taxes (d)	<u>31,721,855</u>	<u>28,564,999</u>	<u>28,006,654</u>
Total expenses	<u>\$ 491,640,946</u>	<u>\$ 491,064,754</u>	<u>\$ 519,470,558</u>
Revenue available for debt service	<u>\$ 210,412,461</u>	<u>\$ 199,695,331</u>	<u>\$ 278,637,392</u>
Debt service			
Parity	\$ 118,371,944	\$ 144,805,235	\$ 128,216,351
Subordinate lien (e)	-	59,003	7,461,748
Total debt service	<u>\$ 118,371,944</u>	<u>\$ 144,864,238</u>	<u>\$ 135,678,099</u>
Debt service coverage ratio	<u>1.78</u>	<u>1.38</u>	<u>2.05</u>

(a) Excludes GASB 31 adjustments for fair market value investments.

(b) Non-cash adjustment due to favorable court decision regarding FERC fees. Net effect for 2010 was non-cash reduction of expenses.

(c) Excludes amortization of bond issue costs.

(d) City taxes take a junior lien to debt service.

(e) Excludes variable rate bonds repaid in February 2009 and funded from proceeds of the 2008 bond issue.

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MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010, 2009, and 2008

Environmental Liabilities

The Department implemented GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, effective in 2008. Environmental liabilities were \$35.3 million, \$29.1 million, and \$18.7 million at December 31, 2010, 2009, and 2008, respectively. The liabilities are primarily attributable to the estimated cost of remediating contaminated sediments in the lower Duwamish Waterway, a designated federal Superfund site. The Department is considered a potentially responsible party for contamination in the Duwamish River due to land ownership or use of property located along the river. Not included in environmental liabilities is an estimate of \$8.0 million for remediation work that will be capitalized as work is performed for land purchased from Greyhound for a proposed new substation.

More information on environmental liabilities is found in Note 14 of the accompanying financial statements.

Deferred Credits

Deferred credits totaled \$77.8 million, \$28.7 million, and \$30.7 million at December 31, 2010, 2009, and 2008, respectively. The significant activity occurred during 2010 principally the result of implementation and funding of the RSA in accordance with Ordinance No. 123260. Funding of the RSA from operating cash has the corresponding effect of deferring operating revenues in a *Rate stabilization deferred revenue* account. Operating revenues deferred from RSA transactions totaled \$54.3 million for 2010. See Note 3 in the accompanying financial statements for more information on the RSA.

RESULTS OF OPERATIONS

Condensed Revenues and Expenses

	Year Ended December 31		
	2010	2009	2008
Operating revenues	\$ 732,977,819	\$ 723,128,041	\$ 877,392,652
Nonoperating revenues	<u>8,624,761</u>	<u>4,337,406</u>	<u>11,413,710</u>
Total revenues	<u>741,602,580</u>	<u>727,465,447</u>	<u>888,806,362</u>
Operating expenses	672,461,588	664,155,748	730,692,842
Nonoperating expenses	<u>65,149,303</u>	<u>72,565,163</u>	<u>66,449,323</u>
Total expenses	<u>737,610,891</u>	<u>736,720,911</u>	<u>797,142,165</u>
Capital contributions	21,745,947	35,900,980	36,440,773
Capital grants	<u>4,633,584</u>	<u>7,512,482</u>	<u>3,485,684</u>
Net income	<u>\$ 30,371,220</u>	<u>\$ 34,157,998</u>	<u>\$ 131,590,654</u>

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SUMMARY

2010 Compared to 2009

Net income for 2010 was \$30.4 million, a decrease of \$3.8 million or 11.1% from 2009 net income of \$34.2 million. Higher retail power revenues were offset by deferral of RSA revenues, lower net wholesale revenues, lower capital contributions, and higher taxes. In addition, lower administrative and general, interest, and other expenses were offset by higher power-related expenses. Operating expenses were again held below budget for 2010.

2009 Compared to 2008

Net income for 2009 was \$34.2 million, significantly lower than 2008 net income of \$131.6 million by \$97.4 million or 74.0%. Lower net wholesale energy revenues plus higher BPA power costs were the primary reasons for the decline in net income. Additionally, higher non-power operating expenses and interest expense contributed in comparison to 2008 to the lower net income; however, operating expenses were held below the budgeted amount in 2009.

REVENUES

2010 Compared to 2009

Total Operating Revenues were \$733.0 million, an increase of \$9.9 million or 1.4% from 2009. *Retail power* revenues at \$624.2 million increased \$79.1 million, *Wholesale power* revenues at \$74.5 million decreased \$14.2 million, *Other power* revenues at \$66.7 did not change, *RSA deferred* revenues at \$(54.3) million decreased \$54.3 million, and *Other operating* revenues at \$21.9 million decreased \$0.7 million. *Retail power* revenues were significantly higher due to the 13.8% rate increase and 4.5% temporary rate surcharge implemented at the beginning of the year and in May 2010, respectively. Revenues were reduced by *Transfers from/(to) rate stabilization account* of \$(54.3) million in 2010 in accordance with Ordinance No. 123260. Those transfers to the RSA were comprised of revenues from the 4.5% rate surcharge and principally debt service savings from advance refunding of certain prior lien bonds, and were recorded as *Deferred revenue* on the balance sheet.

Net wholesale energy revenues were \$50.0 million for 2010, a decrease of \$14.1 million or 22.0% from net revenues of \$64.1 million in 2009. The Department is a net seller in the wholesale energy market and extremely low water conditions in the Northwest region early in 2010 along with lower wholesale power prices during the year reduced revenue derived from wholesale sales.

2009 Compared to 2008

Total Operating Revenues were \$723.1 million, a decrease of \$154.3 million or 17.6 % from 2008. *Retail power* revenues at \$545.1 million, decreased \$2.8 million, *Wholesale power* revenues at \$88.7 million decreased \$80.3 million, *Other Power* revenues at \$66.7 decreased \$75.8 million, and *Other operating* revenues at \$22.6 million increased \$4.6 million. *Wholesale power* revenues were substantially lower because of somewhat less energy available for sale due to a less than average water year, along with significantly lower wholesale energy prices on the spot market during 2009. *Other Power* revenues of \$30.1 million declined \$52.1 million as a result of fewer non-monetary power exchanges transacted during 2009 and valued at lower fair value energy prices in accordance with ASC 820, *Fair Value Measurements and Disclosure*.

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Furthermore, monetary power-related transactions of \$36.7 million were lower by \$23.6 million, mainly the result of lower basis transactions at contractual prices.

Net wholesale energy revenues were \$64.1 million for 2009, a decrease of \$52.4 million or 45.0% from net revenues of \$116.5 million in 2008. Lower wholesale energy prices during the year greatly reduced the amount of revenue derived from wholesale sales.

EXPENSES

2010 Compared to 2009

Total operating expenses were \$672.5 million, an increase of \$8.3 million or 1.3% from \$664.2 million in 2009.

Power-related expenses at \$352.1 million were higher by \$13.7 million or 4.0%. These expenses were comprised of *BPA purchased power* of \$163.3 million, which increased \$9.6 million, *Short-term power purchases* of \$24.5 million, which decreased \$0.1 million, *Power-related wholesale purchases* of \$25.1 million, which decreased \$2.6 million, and other *Power-related* expenses, including *Transmission* and *Generation* of \$139.2 million, which increased \$6.8 million.

BPA purchased power increased due to higher Block and Slice (fixed and variable power products offered by BPA) power purchases and lower Residential Exchange Program credits. Other *Power-related* expenses were higher by \$12.0 million on account of increased purchased power from the Priest Rapids power contract and two renewable energy power contracts. These expenses were offset primarily by lower *Generation* of \$6.2 million mainly because of a favorable court decision regarding FERC land use fees paid in 2009 that are being applied in large part against 2010 and 2011 FERC fees.

Non-power operating expenses of \$163.6 million decreased \$19.1 million or 10.5% from \$182.7 million in 2009, due to cost control efforts. Lower administrative and general expenses of \$17.0 million accounted for the significant portion of the decrease in expenses. For the second consecutive year, the Department held operating and maintenance expenses below the budgeted level as a response to the decrease in *Wholesale* revenues. In addition, lower expenses were incurred for risk management liabilities including for the numerous Duwamish superfund sites, industrial insurance, and judgment claims.

Taxes of \$70.4 million increased \$8.1 million because of the higher revenues, and *Depreciation and amortization* of \$86.4 million increased \$5.7 million due to the additions to plant.

2009 Compared to 2008

Total operating expenses were \$664.2 million, a decrease of \$66.5 million or 9.1% from \$730.7 million in 2008.

Power-related expenses at \$338.4 million were lower by \$76.4 million or 18.4%. These expenses consisted of *BPA purchased power* of \$153.7 million, which increased \$16.0 million, *Short-term power purchases* of \$24.6 million, which decreased \$27.9 million, *Power-related wholesale purchases* of \$27.7 million, which decreased \$66.9 million, and other *Power-related* expenses, including *Transmission* and *Generation* of \$132.4 million, which increased \$2.4 million.

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010, 2009, and 2008

BPA purchased power increased \$16.0 million in large part because credits associated with the Residential Exchange Program were lower in 2009 compared to 2008. *Short-term power purchases* decreased \$27.9 million and are associated with net wholesale energy revenues discussed within Operating Revenues above. *Power-related wholesale purchases* decreased \$50.7 million for fair value valuations of non-monetary power exchange contracts, and decreased \$16.2 million principally for power basis transactions valued at contractual prices; also discussed at Operating Revenues above.

Non-power operating expenses of \$182.7 million increased \$6.8 million or 3.9% from \$175.9 million in 2008. Administrative and general expenses increased \$7.0 million in large part due to higher expenses for ongoing environmental clean-up associated with remediation work for the numerous Duwamish superfund sites. In addition, health care, pensions and other administrative expenses were slightly higher. The Department held operating and maintenance expenditures below the budgeted level during 2009 as a response to the decrease in *Wholesale* revenues.

Taxes of \$62.3 million increased \$0.4 million, and *Depreciation and amortization* of \$80.7 million increased \$2.6 million.

OTHER NONOPERATING INCOME AND EXPENSE

2010 Compared to 2009

Nonoperating Revenues (Expenses)—Nonoperating (expenses) decreased \$11.7 million to \$56.5 million in 2010 from \$68.2 million in 2009 due to the following:

Nonoperating income increased \$4.4 million to \$8.7 million in 2010, attributable mainly to a settlement from a potentially responsible party for environmental cleanup of a Duwamish superfund site, federal interest subsidies to be received for the 2010 bonds, and higher noncapital grants.

Nonoperating expense decreased \$7.3 million to \$65.2 million in 2010. The 2010 bonds were issued with a large premium, and bond premium amortization was the major contributor to the decrease.

Capital Contributions and Grants—Capital contributions and grants decreased by \$17.1 million to \$26.3 million in 2010. Capital contributions declined \$14.2 million to \$21.7 million due essentially to lower in-kind contributions of \$12.8 million and lower suburban infrastructure undergrounding contributions of \$1.3 million. In 2009, large in-kind contributions were received for electrical infrastructure work on the Alaskan Way Viaduct project that did not recur in 2010. Capital grants decreased \$2.9 million from 2009 for a total of \$4.6 million.

2009 Compared to 2008

Nonoperating Revenues (Expenses)—Nonoperating (expenses) increased \$13.2 million to \$68.2 million in 2009 from \$55.0 million in 2008 as a result of the following:

Nonoperating income decreased \$7.1 million to \$4.3 million from 2008, principally on account of lower *Investment income* of \$3.3 million attributable to lower cash balances and interest rates during the year. *Other nonoperating income* decreased \$3.8 million.

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010, 2009, and 2008

Nonoperating expense increased \$6.1 million from \$66.4 million in 2008, mainly the result of higher interest expense for the parity bonds issued in December 2008.

Capital Contributions and Grants—Capital contributions and grants increased by \$3.5 million to \$43.4 million in 2009. Capital grants totaled \$7.5 million for an increase of \$4.0 million from 2009 largely on account of two grants. Grants were higher by \$2.4 million for electrical work for a major project to improve traffic congestion in an industrial area and by \$0.8 million received from the U.S. Department of Natural Resources for the purchase of land to protect critical habitat. Lower combined capital contributions of \$7.2 million for general installations, non-standard installations, and suburban infrastructure undergrounding for Burien were offset by higher in-kind contributions of \$6.7 million for electrical infrastructure work on the Alaskan Way Viaduct project.

RISK MANAGEMENT

The Department began implementing an Enterprise Risk Management (ERM) process in 2008 to establish a full spectrum approach to risk management that links strategic planning and other important decision making functions through a standardized process of identifying, assessing, monitoring, and responding to risks across all business units of the Department.

An ERM Council, comprised of the Chief of Staff, Power Supply & Environmental Affairs Officer, Customer Service & Energy Delivery Officer, Chief Financial Officer, Regulatory Compliance Officer, Human Resources Officer, and the Director of Risk Management & Strategic Planning was formed by the Superintendent to guide the development of a risk-aware culture and risk management capabilities and accountability throughout the utility.

A Risk Oversight Council (ROC) oversees wholesale power marketing activities. It is comprised of the Chief Financial Officer (Chair), Power Supply & Environmental Affairs Officer, Director of Risk Management & Strategic Planning, the Director of Power Contracts & Resource Acquisition (non-voting member), the Manager of Power Marketing (non-voting member) and Manager of Power Operations (non-voting member). The ROC guides the continuous improvement of energy risk management activities and capabilities, approves hedging strategies, hedging plans, and approves changes to relevant operating procedures.

The Risk Management & Strategic Planning Division facilitates the development of ERM efforts across the Department; manages wholesale energy market credit risk; and carries out the middle office functions of the Department's wholesale energy market participation which include risk controls development, and independent reporting of market positions and policy compliance.

Hydro Risk

Due to the Department's primary reliance on hydroelectric generation, the weather can significantly affect its operations. Hydroelectric generation depends on the amount of snow-pack in the mountains upstream of the Department's hydroelectric facilities, springtime snow-melt and run-off and rainfall. Hydroelectric operations also are influenced by flood control and environmental matters, including protection of fish. In low-water years, the Department's generation is reduced and the use of wholesale purchased power will increase in order to meet load. Normally, the Department experiences electricity usage peaks in winter; however, extreme weather conditions affecting either heating or cooling needs could cause the Department's seasonal fluctuations to be more pronounced and increase costs. In addition, economic trends (increase or decrease in

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010, 2009, and 2008

business activity, housing sales and development of properties) can affect demand and change or increase costs.

Energy Market Risk

For the Department, energy market risk is the risk of adverse fluctuations in the price of wholesale electricity, which is compounded by volumetric changes affecting the availability of, or demand for electricity. Factors that contribute to energy market risk include: regional planned and unplanned generation plant outages, transmission constraints or disruptions, the number of active creditworthy market participants willing to transact, and environmental regulations that influence the availability of generation resources.

The Department's exposure to hydro volumetric and market risk is managed by the Power Management Executive with the oversight of the ROC. The Department engages in market transactions to meet its load obligations and to realize earnings from surplus energy resources. Except for limited intraday and interday marketing to take advantage of owned hydro storage, the Department does not take market positions in anticipation of generating revenue.

With a significant portion of the Department's revenue expected from wholesale energy market sales, great emphasis is placed on the management of risks associated with this activity. Policies, procedures, and processes designed to manage, control and monitor these risks are in place. A formal front, middle, and back office structure is in place to ensure proper segregation of duties.

The Department measures the risk in its energy portfolio on a weekly basis using a Monte Carlo model that incorporates not only price risk, but also the volumetric risk associated with its hydro-dominated power portfolio. Scenario analysis is used for stress testing.

Credit Risk

Credit risk is the risk of loss that would be incurred as a result of nonperformance by counterparties of their contractual obligations. If a counterparty failed to perform on its contractual obligation to deliver electricity, then the Department may find it necessary to procure electricity at current market prices, which may be higher than the contract price. If a counterparty failed to pay its obligation in a timely manner, this would have an impact on the Department's revenue and cash flow. As with market risk, the Department has policies governing the management of credit risk.

Wholesale counterparties are assigned unsecured credit limits based on publicly available and proprietary financial information. A third-party's proprietary credit scoring model is used to classify counterparties into one of several categories with permissible ranges of unsecured credit limits. Specific counterparty credit limits are set within this prescribed range based on qualitative and quantitative factors. Credit limits are also used to manage counterparty concentration risk. The Department has a concentration of credit risk related to geographic location and counterparties as it transacts in the western United States. This concentration of counterparties and of geographic location may impact the Department's overall exposure to credit risk, either positively or negatively, because counterparties may be similarly affected by changes in conditions.

Credit limits, exposures and credit quality are actively monitored. Despite such efforts, defaults by counterparties may periodically occur. The Department transacts with counterparties on an uncollateralized and collateralized basis. Posted collateral may be in the form of cash or letters of credit and may represent prepayment or credit exposure assurance.

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

BALANCE SHEETS

AS OF DECEMBER 31, 2010 AND 2009

	2010	2009
ASSETS		
UTILITY PLANT—At original cost:		
Plant-in-service—excluding land	\$ 3,205,420,242	\$ 3,025,981,197
Less accumulated depreciation and amortization	<u>(1,384,291,476)</u>	<u>(1,317,482,371)</u>
Total plant-in-service—net	1,821,128,766	1,708,498,826
Construction work-in-progress	147,035,115	147,809,570
Nonoperating property—net of accumulated depreciation	5,137,743	5,122,638
Assets held for future use	9,273,472	11,260,732
Land and land rights	<u>90,530,852</u>	<u>82,827,250</u>
Total utility plant—net	<u>2,073,105,948</u>	<u>1,955,519,016</u>
RESTRICTED ASSETS:		
Rate stabilization account	79,265,627	-
Contingency reserve account	-	25,000,000
Construction		
Cash and equity in pooled investments	18,193,252	-
Investments	38,788,172	-
Debt service	17,698	2,510,783
Special deposits and other restricted assets	<u>3,936,424</u>	<u>4,129,067</u>
Total restricted assets	<u>140,201,173</u>	<u>31,639,850</u>
CURRENT ASSETS:		
Cash and equity in pooled investments	56,931,666	32,694,670
Accounts receivable (includes \$2,794,440 and \$3,777,444 at fair value), net of allowance of \$10,764,864 and \$7,138,288	78,989,489	64,847,784
Interfund receivable	2,848,670	1,579,395
Unbilled revenues	69,682,891	60,198,421
Materials and supplies at average cost	24,828,843	26,127,543
Prepayments, interest receivable, and other current assets	<u>1,709,645</u>	<u>1,332,143</u>
Total current assets	<u>234,991,204</u>	<u>186,779,956</u>
OTHER ASSETS:		
Deferred conservation costs—net	178,436,794	162,136,725
Endangered Species Act costs—net	2,626,689	2,418,433
Other deferred charges and assets—net	<u>40,421,969</u>	<u>38,045,513</u>
Total other assets	<u>221,485,452</u>	<u>202,600,671</u>
TOTAL ASSETS	<u>\$ 2,669,783,777</u>	<u>\$ 2,376,539,493</u>

See notes to financial statements.

	2010	2009
LIABILITIES		
LONG-TERM DEBT:		
Revenue bonds	\$ 1,536,775,000	\$ 1,383,050,000
Plus bond premium	71,227,523	25,152,248
Less bond discount	(81,078)	(195,531)
Less deferred charges on advanced refunding	(33,401,654)	(27,922,396)
Less revenue bonds—current portion	<u>(58,685,000)</u>	<u>(80,735,000)</u>
Total long-term debt	<u>1,515,834,791</u>	<u>1,299,349,321</u>
NONCURRENT LIABILITIES:		
Accumulated provision for injuries and damages	36,500,185	32,771,188
Compensated absences	13,979,516	13,458,624
Other noncurrent liabilities	<u>4,554,555</u>	<u>3,448,056</u>
Total noncurrent liabilities	<u>55,034,256</u>	<u>49,677,868</u>
CURRENT LIABILITIES:		
Accounts payable and other current liabilities	60,087,069	60,310,868
Interfund payable	7,129,392	6,918,981
Accrued payroll and related taxes	4,636,384	4,306,367
Compensated absences	1,560,966	1,330,512
Accrued interest	34,375,494	20,930,567
Long-term debt—current portion	<u>58,685,000</u>	<u>80,735,000</u>
Total current liabilities	<u>166,474,305</u>	<u>174,532,295</u>
DEFERRED CREDITS:		
Deferred revenue - rate stabilization account	54,265,627	-
Other deferred credits (includes \$799,220 and \$1,713,502 at fair value)	<u>23,549,933</u>	<u>28,726,364</u>
Total deferred credits	<u>77,815,560</u>	<u>28,726,364</u>
Total liabilities	<u>1,815,158,912</u>	<u>1,552,285,848</u>
EQUITY		
Invested in capital assets, net of related debt	737,531,065	733,612,153
Restricted:		
Rate stabilization account	25,000,000	-
Contingency reserve account	-	25,000,000
Special deposits and other purposes	<u>128,822</u>	<u>928,099</u>
Total restricted	<u>25,128,822</u>	<u>25,928,099</u>
Unrestricted—net	<u>91,964,978</u>	<u>64,713,393</u>
Total equity	<u>854,624,865</u>	<u>824,253,645</u>
TOTAL LIABILITIES AND EQUITY	<u>\$ 2,669,783,777</u>	<u>\$ 2,376,539,493</u>

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN EQUITY FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009

	2010	2009
OPERATING REVENUES:		
Retail power revenues	\$ 624,193,642	\$ 545,110,850
Short-term wholesale power revenues	74,534,644	88,650,460
Other power-related revenues	66,574,190	66,782,044
Transfers from/(to) rate stabilization account	(54,265,627)	-
Other operating revenues	<u>21,940,970</u>	<u>22,584,687</u>
Total operating revenues	<u>732,977,819</u>	<u>723,128,041</u>
OPERATING EXPENSES:		
Long-term purchased power—Bonneville	163,337,484	153,685,459
Long-term purchased power—other	60,253,026	48,317,603
Short-term wholesale power purchases	24,484,395	24,570,643
Other power expenses	35,288,255	36,112,877
Generation	22,367,691	28,621,886
Transmission	46,254,212	47,074,084
Distribution	54,630,469	57,005,441
Customer service	36,136,821	35,661,790
Conservation	16,793,710	16,920,830
Administrative and general	56,165,993	73,217,198
City of Seattle occupation tax	38,649,174	33,664,082
Other taxes	31,731,773	28,610,571
Depreciation and amortization	<u>86,368,585</u>	<u>80,693,284</u>
Total operating expenses	<u>672,461,588</u>	<u>664,155,748</u>
NET OPERATING INCOME	<u>60,516,231</u>	<u>58,972,293</u>
NONOPERATING REVENUES (EXPENSES):		
Investment income	2,689,867	2,612,978
Interest expense	(69,369,190)	(69,111,778)
Amortization of refunding loss	(5,136,250)	(4,576,532)
Amortization of bond premium	10,586,818	3,569,395
Amortization of bond discount and issue costs	(1,230,681)	(1,433,287)
Noncapital grants	2,969,721	1,695,507
Gain on sale of property	80,959	28,921
Other income (expense)—net	<u>2,884,214</u>	<u>(1,012,961)</u>
Total nonoperating expenses	<u>(56,524,542)</u>	<u>(68,227,757)</u>
NET INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS AND GRANTS	<u>3,991,689</u>	<u>(9,255,464)</u>
CAPITAL CONTRIBUTIONS AND GRANTS:		
Capital contributions	21,745,947	35,900,980
Capital grants	<u>4,633,584</u>	<u>7,512,482</u>
Total capital contributions and grants	<u>26,379,531</u>	<u>43,413,462</u>
NET INCOME	30,371,220	34,157,998
EQUITY:		
Beginning of year	<u>824,253,645</u>	<u>790,095,647</u>
End of year	<u>\$ 854,624,865</u>	<u>\$ 824,253,645</u>

See notes to financial statements.

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009

	2010	2009
OPERATING ACTIVITIES:		
Cash received from customers and counterparties	\$ 730,818,339	\$ 672,137,809
Interfund operating cash received	3,366,325	4,828,827
Cash paid to suppliers, employees, and counterparties	(436,163,978)	(422,684,884)
Interfund operating cash paid	(26,284,430)	(26,352,163)
Taxes paid	(69,955,913)	(60,682,273)
Net cash provided by operating activities	<u>201,780,343</u>	<u>167,247,316</u>
NONCAPITAL FINANCING ACTIVITIES:		
Noncapital grants received	2,915,613	1,613,781
Gains from bankruptcy distributions	5,220	28,921
Bonneville receipts for conservation	10,303	217,857
Payment to vendors on behalf of customers for conservation augmentation	(29,732,576)	(24,104,827)
Net cash used in noncapital financing activities	<u>(26,801,440)</u>	<u>(22,244,268)</u>
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Proceeds from long-term debt, net of premium	853,837,102	-
Payment to trustee for defeased bonds	(595,556,501)	-
Bond issue costs paid	(3,415,163)	(7,449)
Principal paid on long-term debt	(67,360,000)	(146,325,000)
Interest paid on long-term debt	(51,045,065)	(70,514,238)
Acquisition and construction of capital assets	(192,389,859)	(214,654,943)
Interfund payments for acquisition and construction of capital assets	(3,993,386)	(4,062,930)
Capital contributions	10,336,783	14,699,438
Interfund receipts for capital contributions	3,137,410	635,332
Capital grants received	2,145,651	7,617,342
Interest received for suburban infrastructure improvements	1,322,919	980,335
Proceeds on sale of property	90,000	-
(Increase) in other deferred assets and charges	(610,174)	(953,131)
Interfund (increase) in other deferred assets and charges	(3,524)	(12,038)
Net cash used in capital and related financing activities	<u>(43,503,807)</u>	<u>(412,597,282)</u>
INVESTING ACTIVITIES:		
Proceeds from investments	136,164,270	125,779,341
Purchases of investments	(175,034,038)	-
Interest received on investments and on cash and equity in pooled investments	1,404,820	2,188,127
Net cash provided by (used in) investing activities	<u>(37,464,948)</u>	<u>127,967,468</u>
NET INCREASE (DECREASE) IN CASH AND EQUITY IN POOLED INVESTMENTS	94,010,148	(139,626,766)
CASH AND EQUITY IN POOLED INVESTMENTS:		
Beginning of year	<u>64,334,520</u>	<u>203,961,286</u>
End of year	<u>\$ 158,344,668</u>	<u>\$ 64,334,520</u>

	2010	2009
RECONCILIATION OF NET OPERATING INCOME TO		
NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net operating income	\$ 60,516,231	\$ 58,972,293
Adjustments to reconcile operating income to net cash provided by operating activities:		
Non-cash items included in operating income:		
Depreciation	88,171,881	82,571,691
Amortization of deferred credits	(6,037,962)	(5,963,898)
Amortization of other deferred charges	15,212,202	13,695,456
Bad debt expense	8,030,451	5,271,105
Power revenues	(62,315,573)	(57,084,168)
Power expenses	62,731,786	59,574,802
Provision for injuries and damages	6,823,203	9,218,102
Other non-cash items	7,215,326	1,536,744
Change in:		
Accounts receivable	(25,245,191)	(4,962,528)
Unbilled revenues	(9,484,469)	(118,995)
Materials and supplies	549,634	5,067,627
Prepayments, interest receivable, and other receivables	(419,181)	(363,476)
Other deferred assets and charges	(1,809,624)	1,470,203
Provision for injuries and damages and claims payable	(3,094,205)	(865,695)
Accounts payable and other payables	6,670,207	(771,947)
Rate stabilization deferred revenue	54,265,627	-
Total adjustments	<u>141,264,112</u>	<u>108,275,023</u>
Net cash provided by operating activities	<u>\$ 201,780,343</u>	<u>\$ 167,247,316</u>
SUPPLEMENTAL DISCLOSURES OF NONCASH ACTIVITIES:		
In-kind capital contributions	\$ 6,803,624	\$ 19,559,652
Amortization of debt related costs—net	4,219,887	(2,440,424)
Change in valuation of deferrals on power exchange	914,282	(1,497,299)
Allowance for funds used during construction	5,144,714	3,833,222
Power exchange revenues	28,933,256	25,844,065
Power exchange expenses	(29,001,978)	(27,698,491)
Power revenue netted against power expenses	17,426,315	7,241,424
Power expense netted against power revenues	(15,877,381)	(24,217,655)

See notes to financial statements.

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

NOTES TO FINANCIAL STATEMENTS

AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009

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 is an enterprise fund of the City. The Department owns and operates certain generating, transmission, and distribution facilities and supplies electricity to approximately 399,000 customers. The Department supplies electrical energy to other City agencies at rates prescribed by City ordinances, and to certain neighboring communities under franchise agreements. The establishment of the Department's rates is within the exclusive jurisdiction of the Seattle 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's revenues for services provided to other City departments were \$15.0 million and \$15.9 million for electrical energy, and \$7.8 million and \$6.6 million for non-energy services, in 2010 and 2009, respectively.

The Department receives certain services from other City departments and paid \$39.7 million in 2010 and \$39.1 million in 2009, for such services. Amounts paid include central cost allocations from the City for services received including treasury services, risk financing, purchasing, data processing systems, vehicle maintenance, personnel, payroll, legal, administrative, and building rentals, including for the Department's administrative offices.

The Department's due from other City departments totaled \$2.8 million and \$1.6 million at December 31, 2010 and 2009. The Department's due to other City departments totaled \$7.1 million and \$6.9 million at December 31, 2010 and 2009. The balances due from and to are the result of transactions incurred in the normal course of operations.

Basis of Presentation and Accounting Standards—The financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America as applied to governmental units. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Department has applied and is current through 2010 with all applicable GASB pronouncements as well as Accounting Standards Codification (ASC) of the Financial Accounting Standards Board (FASB), except for those that conflict with or contradict GASB pronouncements.

Effective January 1, 2010, the Department adopted Statement No. 51 of the GASB, *Accounting and Financial Reporting for Intangible Assets*. Statement No. 51 establishes accounting and financial reporting standards for intangible assets. This Statement provides guidance related to the definition, recognition, and amortization of intangible assets. Statement No. 51 also requires intangible assets within its scope to be reported as capital assets. The effect of implementing Statement No. 51 of the GASB is described in Note 2.

THE CITY OF SEATTLE—CITY LIGHT DEPARTMENT

NOTES TO FINANCIAL STATEMENTS

AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009

Effective January 1, 2009, the Department adopted Statement No. 53 of the GASB, *Accounting and Financial Reporting for Derivative Instruments*. This Statement addresses the recognition, measurement, and disclosure of information regarding derivative instruments. This Statement is similar to ASC 815, *Derivatives and Hedging* (formerly Statement No. 133 of the FASB, *Accounting for Derivative Instruments and Hedging Activities* and Statement No. 138 of the FASB, *Accounting for Certain Derivative Instruments and Certain Hedging Activities, an amendment of FASB Statement No. 133*), which the Department implemented in 2001. Similar to ASC 815, Statement No. 53 requires that the fair value of hedging derivative instruments be recognized as either assets or liabilities on the Department's balance sheet and that changes in the fair value of an investment derivative instrument be included in earnings. The effect of implementing Statement No. 53 of the GASB is noted in Note 6.

Fair Value Measurements—Descriptions of the Department's accounting policies on fair value measurements for items reported on the balance sheet at December 31, 2010 and 2009, are as noted in the following paragraph, Note 5 Accounts Receivable, and Note 10 Long-Term Purchased Power, Exchanges, and Transmission. Additional disclosures required by ASC 820 are provided in Note 15 Fair Value Measurements.

Fair Value of Financial Instruments—The Department's financial instruments are reported on the balance sheet at December 31, 2010 and 2009, as Restricted assets and Cash and equity in pooled investments and investments are measured at fair value. These instruments consist primarily of the Department's share of the City-wide pool of investments and its dedicated investments (see Note 4). Gains and losses on these financial instruments are reflected in Investment income in the Statements of revenues, expenses, and changes in equity. Long-term debt at December 31, 2010 and 2009, is disclosed at fair value (see Note 7).

Equity—The Department classifies its equity into three components as follows:

- **Invested in capital assets—net of related debt**—This component consists of capital assets, net of accumulated depreciation and amortization, reduced by the net outstanding debt balances related to capital assets net of unamortized debt expenses.
- **Restricted**—This component consists of equity with constraints placed on use. Constraints include those imposed by creditors (such as through debt covenants and excluding amounts considered in net capital, above), grants, or laws and regulations of other governments, or by enabling legislation, The City of Seattle Charter, or by ordinances legislated by the Seattle City Council.
- **Unrestricted**—This component consists of assets and liabilities that do not meet the definition of “invested in capital assets—net of related debt” or “restricted.”

Restricted and Unrestricted Equity—The Department's policy is to use restricted equity for specified purposes and to use unrestricted equity for operating expenses. The Department does not currently incur expenses for which both restricted and unrestricted equity is available.

In September 2005, the Bond Reserve Account was liquidated and a portion of these funds was used to establish a Contingency Reserve Account in the amount of \$25.0 million in accordance with City of Seattle Ordinance No. 121812. This account was restricted for extraordinary costs associated with the operation of the electrical system. There was no associated liability for the Contingency Reserve Account as of December 31, 2009. In May 2010, the \$25.0 million in the Contingency Reserve Account

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was transferred to the Rate Stabilization Account in accordance with City of Seattle Ordinance No. 123260 (see Note 3).

Assets Held for Future Use—These assets include property acquired but never used by the Department in electrical service and therefore, held for future service under a definitive plan. Also included is property previously used in service but retired and held pending its reuse in the future under a definitive plan. As of December 31, 2010 and 2009, assets held for future use included the following electrical plant assets: substations, ducts and vaults, and transmission lines totaling \$9.3 million and \$11.3 million, respectively.

Materials and Supplies—Materials and supplies are generally used for construction, operation and maintenance work, not for resale. They are valued utilizing the average cost method and charged to construction or expense when used.

Revenue Recognition—Service rates are authorized by City 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 as unbilled revenue within retail power revenues.

The Department's customer base accounted for electric energy sales at December 31, 2010 and 2009, as follows:

	2010	2009
Residential	36.5 %	37.2 %
Nonresidential	63.5	62.8
Total	100.0 %	100.0 %

Revenues earned in the process of delivering energy to customers, wholesale energy transactions, and related activities are considered operating revenues in the determination of net income. Investment income, nonexchange transactions, and other revenues are considered nonoperating revenues.

Expense Recognition—Expenses incurred in the process of delivering energy to customers, wholesale energy transactions, and related activities are considered operating expenses in the determination of net income. Debt interest expense, debt related amortization, and certain other expenses are considered nonoperating expenses.

Administrative and General Overhead Costs Applied—Certain administrative and general overhead costs are allocated to construction work-in-progress, major data processing systems development, programmatic conservation, relicensing mitigation projects, and billable operations and maintenance activities based on rates established by cost studies. Pension and benefit costs are fully allocated to capital and operations and maintenance activities based on a percentage of labor dollars. The administrative and general overhead costs applied totaled \$32.5 million and \$29.7 million in 2010 and 2009, respectively. Pension and benefit costs were \$36.3 million and \$35.3 million in 2010 and 2009, respectively. Administrative and general expenses, net of total applied overhead, were \$56.2 million and \$73.2 million in 2010 and 2009, respectively.

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Interest Charged to Construction—Interest is charged for funds used during construction of plant assets and to nonbillable construction work-in-progress. Interest charged represents the estimated costs of financing construction projects and is computed using the Department’s weighted-average interest rate for all bonds outstanding at the end of the year. Interest charged to construction totaled \$5.1 million and \$3.8 million in 2010 and 2009, respectively, and is reflected as a reduction of interest expense in the statements of revenues, expenses, and changes in equity.

Nonexchange Transactions—Capital contributions and grants in the amount of \$29.3 million and \$45.1 million are reported for 2010 and 2009, respectively, in the statements of revenues, expenses, and changes in equity as nonoperating revenues from nonexchange transactions. Capital contributions and grants revenues are recognized based on the accrual basis of accounting. In-kind capital contributions are recognized in the period when all eligibility requirements have been met as described in GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, based on either the internal engineer’s estimate of the current cost of comparable plant-in-service or the donor’s actual cost. Federal and state grant revenues are recognized as earned and are subject to contract and other compliance audits.

Compensated Absences—Regular employees of the Department earn vacation time in accordance with length of service. A maximum of 480 hours may be accumulated for the most tenured employees and, upon termination, employees are entitled to compensation for unused vacation. Upon retirement, employees receive compensation equivalent to 25% of their accumulated sick leave. Effective 2006, only employees represented by unions who voted in favor of a Healthcare Reimbursement Arrangement (HRA), receive 35% of their sick leave balance tax-free through an HRA account for healthcare expenses post retirement. Because of the special tax arrangement, the sick leave balance may only go into the HRA account; it may not be taken as a cashout. The HRA program is administered by an independent third party administrator, Meritain Health. HRA investments are managed by HRA VEBA Trust. The Department accrues all costs associated with compensated absences, including payroll taxes.

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 allowance for doubtful accounts, unbilled revenues, power exchanges, accumulated provision for injuries and damages and workers’ compensation, environmental liabilities, accrued sick leave, other postemployment benefits, 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 financial market liquidity and economic uncertainty; prices on the wholesale markets for short-term power transactions; interest rates and other inputs and techniques for fair valuation; water conditions, weather, climate change, and natural disaster-related disruptions; terrorism; collective bargaining labor disputes; fish and other Endangered Species Act (ESA) issues; Environmental Protection Agency (EPA) regulations; federal government regulations or orders concerning the operations, maintenance, and/or licensing of hydroelectric facilities; other governmental regulations; restructuring of the electrical utility industry; and the costs of constructing transmission facilities that may be incurred as part of a northwest regional transmission system, and related effects of this system on transmission rights, transmission sales, surplus energy, and governance.

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Reclassifications—Certain 2009 account balances have been reclassified to conform to the 2010 presentation, including reclassifications in accordance with the provisions of GASB Statement No. 51 (see Note 2).

2. UTILITY PLANT

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 capitalization threshold was \$5,000 in 2010 and 2009. Plant constructed with capital contributions or contributions in-aid-of construction received from customers is included in utility plant. Capital contributions totaled \$21.7 million in 2010 and \$35.9 million in 2009. Provision for depreciation and amortization is made using the straight-line method based upon estimated economic lives, which range from 3 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 and amortization rate was approximately 2.7% in 2010 and 2.8% in 2009. When operating plant assets are retired, their original cost together with retirement costs and removal costs, less salvage, is charged to accumulated depreciation or amortization, if applicable. The cost of maintenance and repairs is charged to expense as incurred, while the cost of replacements and betterments is capitalized. The Department periodically reviews long-lived assets for impairment to determine whether any events or circumstances indicate the carrying value of the assets may not be recoverable over their economic lives. No impairment was identified in 2010 or 2009.

Effective January 1, 2010, the Department adopted Statement No. 51 of the GASB, *Accounting and Financial Reporting for Intangible Assets*, which establishes accounting and financial reporting standards for intangible assets. Intangible assets lack physical substance, are nonfinancial in nature, have useful lives extending beyond a single reporting period, and should be recognized only if they are identifiable. All intangible assets covered under Statement No. 51 must be reported as capital assets. The Department's intangible assets consist of easements, purchased and internally developed software, and transmission rights, which were previously capitalized under Utility plant. In addition, certain assets previously reported in Other assets by the Department met the criteria for intangible assets according to this Statement. These included capitalized relicensing costs for Skagit and Boundary hydroelectric projects, Tolt hydroelectric project mitigation costs, and costs capitalized under the High Ross Agreement.

Certain amounts included in the balance sheet for 2009 have been reclassified to reflect the implementation of Statement No. 51. There was no change in total equity and there was no effect to the Statement of Revenues, Expenditures, and Changes in Equity for 2009.

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Utility plant-in-service at original cost, excluding land, at December 31, 2010, and 2009, was:

	Hydroelectric Production	Transmission	Distribution	General	Intangible	Total
2010						
Original cost:						
Beginning balance	\$ 651,870,767	\$ 151,905,644	\$ 1,616,260,362	\$ 279,867,262	\$ 326,077,162	\$3,025,981,197
Capital acquisitions	24,554,685	6,764,227	110,917,114	13,550,718	28,945,736	184,732,480
Dispositions	(2,601,102)	(402,728)	(10,371,039)	(2,128,142)	-	(15,503,011)
Transfers and adjustments	-	-	10,294,309	(84,733)	-	10,209,576
Total original cost	<u>673,824,350</u>	<u>158,267,143</u>	<u>1,727,100,746</u>	<u>291,205,105</u>	<u>355,022,898</u>	<u>3,205,420,242</u>
Accumulated depreciation and amortization:						
Beginning balance	336,615,683	68,262,995	603,294,327	173,655,798	135,653,568	1,317,482,371
Increase in accumulated depreciation and amortization	13,224,728	3,320,809	49,955,774	14,353,445	10,612,113	91,466,869
Retirements	(4,092,305)	(459,384)	(18,667,690)	(2,537,991)	-	(25,757,370)
Transfers and adjustments	-	-	52,958	-	-	52,958
Retirement work-in-progress	<u>347,240</u>	<u>8,789</u>	<u>609,150</u>	<u>81,469</u>	<u>-</u>	<u>1,046,648</u>
Total accumulated depreciation and amortization	<u>346,095,346</u>	<u>71,133,209</u>	<u>635,244,519</u>	<u>185,552,721</u>	<u>146,265,681</u>	<u>1,384,291,476</u>
Ending balance	<u>\$ 327,729,004</u>	<u>\$ 87,133,934</u>	<u>\$ 1,091,856,227</u>	<u>\$ 105,652,384</u>	<u>\$ 208,757,217</u>	<u>\$1,821,128,766</u>
2009						
Original cost:						
Beginning balance	\$ 643,111,977	\$ 135,414,201	\$ 1,537,406,713	\$ 265,047,221	\$ 305,439,746	\$2,886,419,858
Capital acquisitions	10,914,503	8,417,662	76,790,782	18,763,178	20,637,416	135,523,541
Dispositions	(2,155,713)	(1,176,219)	(6,083,713)	(3,943,137)	-	(13,358,782)
Transfers and adjustments	-	9,250,000	8,146,580	-	-	17,396,580
Total original cost	<u>651,870,767</u>	<u>151,905,644</u>	<u>1,616,260,362</u>	<u>279,867,262</u>	<u>326,077,162</u>	<u>3,025,981,197</u>
Accumulated depreciation and amortization:						
Beginning balance	327,304,795	66,826,131	566,739,630	165,218,003	125,912,283	1,252,000,842
Increase in accumulated depreciation and amortization	12,965,897	3,151,662	47,219,480	12,518,322	9,741,285	85,596,646
Retirements	(3,211,240)	(1,713,498)	(9,193,700)	(3,990,467)	-	(18,108,905)
Retirement work-in-progress	<u>(443,769)</u>	<u>(1,300)</u>	<u>(1,471,083)</u>	<u>(90,060)</u>	<u>-</u>	<u>(2,006,212)</u>
Total accumulated depreciation and amortization	<u>336,615,683</u>	<u>68,262,995</u>	<u>603,294,327</u>	<u>173,655,798</u>	<u>135,653,568</u>	<u>1,317,482,371</u>
Ending balance	<u>\$ 315,255,084</u>	<u>\$ 83,642,649</u>	<u>\$ 1,012,966,035</u>	<u>\$ 106,211,464</u>	<u>\$ 190,423,594</u>	<u>\$1,708,498,826</u>

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3. RATE STABILIZATION ACCOUNT

The Seattle City Council passed ordinances to establish, set parameters and provide a funding mechanism for a Rate Stabilization Account (RSA). The RSA was established to reduce the need for rapid and substantial Seattle City Light rate increases solely to comply with Seattle City Light bond covenants.

In March 2010, the Seattle City Council adopted Resolution No. 31187 and Ordinance No. 123260, establishing revised financial policies and additional parameters for the RSA created by Ordinance No. 121637 in 2004. The revised financial policies include three main elements: (a) additional parameters for the funding, operation, and expenditure of amounts within the RSA, together with the creation of automatic rate surcharges to replenish the RSA; (b) a rate-setting guideline to maintain debt service coverage of 1.8x; and (c) a requirement for revenue funding a portion of the Department's capital program so that, on average, it will be 40% funded from operating cash.

Ordinance No. 123260 identified the sources of significant funding of the RSA and specified that the RSA is to be accessed when surplus power sales deviate from planned amounts. The RSA would be drawn down to supplement revenues when surplus power sales revenues are below the forecasted amount, and conversely, deposits would be made to the RSA if the surplus power sales revenues are greater than forecasted.

Ordinance No. 123260 established a target size for the RSA of no less than \$100.0 million and no greater than \$125.0 million, and authorized the imposition of automatic temporary surcharges on electric rates, ranging between 1.5% and 4.5% when the RSA balance falls below specified levels:

RSA Balance	Action
RSA below \$90.0 million	Automatic 1.5% surcharge
RSA below \$80.0 million	Automatic 3.0% surcharge
RSA below \$70.0 million	Automatic 4.5% surcharge
RSA below \$50.0 million	City Council must initiate rate review and determine actions to replenish RSA to \$100.0 million within 12 months

A 4.5% rate surcharge was in place from May 1, 2010 through December 31, 2010 to initially fund the RSA, along with \$25.0 million transferred from the Contingency Reserve Account established by Ordinance No. 121812 in 2005, and other operating transfers. The Rate stabilization account at December 31, 2010 consisted of the following:

	2010
Rate stabilization account	
Contingency reserve account transfer	\$ 25,000,000
2010 RSA rate surcharge	16,110,655
2010 RSA interest income	154,972
2010 operating revenue	<u>38,000,000</u>
Total	<u>\$ 79,265,627</u>

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To account for RSA transactions, the Seattle City Council passed Resolution No. 31244 authorizing the deferral or recognition of revenue associated with the deposits and withdrawals of the amounts in the RSA in accordance with Accounting Standards Codifications (ASC) 980-405-25-25-1 *Regulated Operations-Liabilities-Recognition-Regulator Imposed Liabilities* and ASC 980-605-25-25-1-4 *Regulated Operations – Revenue Recognition – Recognition – Alternative Revenue Programs* and subsequent amendments.

The regulatory liability account Deferred revenue—rate stabilization account at December 31, 2010 consisted of the following:

	2010
Deferred revenue—rate stabilization account	
2010 RSA rate surcharge	\$ 16,110,655
2010 RSA interest income	154,972
2010 operating revenue	<u>38,000,000</u>
Total	<u>\$ 54,265,627</u>

The Statement of revenues, expenses and changes in equity revenue account Transfers from/(to) rate stabilization account at December 31, 2010 consisted of the following:

	2010
Transfers from/(to) rate stabilization account	<u>\$ (54,265,627)</u>

4. CASH AND EQUITY IN POOLED INVESTMENTS AND INVESTMENTS

Cash and Equity in Pooled Investments—Cash resources of the Department are combined with cash resources of the City to form a pool of cash that is managed by the City’s Department of Finance and Administrative Services (FAS). Under the City’s investment policy, all temporary cash surpluses in the pool are invested. The Department’s share of the pool is included in the balance sheets under the caption “Cash and equity in pooled investments” or accounts within restricted assets. The pool operates like a demand deposit account in that all 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. The City considers investments in financial instruments having a maturity of 90 days or less as a cash equivalent.

Custodial Credit Risk of Deposits—Custodial risk is the risk that, in the event of bank failure for one of the City’s depository institutions, the City’s deposits may not be returned in a timely manner, or in the case of collateralized securities, the City may not be able to recover the collateral held in the possession of an outside party.

The City has very limited custodial credit risk of its deposits due to insurance provided by the Federal Deposit Insurance Corporation (FDIC) as well as protection provided by the Washington State Public Deposit Protection Commission (PDPC) as established in RCW 39.58. The PDPC makes and enforces regulations and administers a program to ensure public funds deposited in banks and thrifts are protected if a financial institution becomes insolvent. The PDPC approves which banks and thrifts can hold state

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and local government deposits and monitors collateral pledged to secure uninsured public deposits. This secures public treasurers' deposits when they exceed the amount insured by the FDIC by requiring banks and thrifts to pledge securities as collateral.

As of December 31, 2010, the City held \$95,000 in its cash vault. Additional small amounts of cash were held in departmental revolving fund accounts with the City's various custodial banks, all of which fell within the FDIC's \$250,000 standard maximum deposit insurance amount. Any of the City's cash not held in its vault, or a local depository, was held in the City's operating fund (investment pool), and at the close of every business day, any cash remaining in the operating fund is swept into an overnight repurchase agreement that matures the next day.

Investments—The Department's cash resources may be invested by FAS separate from the cash and investments pool. Investments are managed in accordance with the City's investment policy, with limits and restrictions applied at the City-wide level rather than to specific investments of the Department.

The City is authorized to purchase U.S. Treasury and government agency securities, certificates of deposits, and other investment deposits issued by Washington State depositories that qualify under the Washington State Deposit Protection Act as defined by RCW 39.58, bankers' acceptances purchased in the secondary market, commercial paper purchased in the secondary market and having received the highest rating by at least two nationally recognized rating agencies, repurchase and reverse repurchase agreements with "primary dealers" that have executed master repurchase agreements, public funds in the local government investment pool (LGIP) in the State Treasury, and other securities as authorized by law.

The City of Seattle has the following policies in managing its investments:

- The City seeks to preserve principal while maximizing income and maintaining liquidity to meet the City's need for cash.
- Investment decisions should further the City's social policies established by ordinance or policy resolutions of the City Council.
- A City social policy shall take precedence over furthering the City's financial objectives when expressly authorized by City Council resolution, except where otherwise provided by law or trust principles.
- Securities purchased shall have a maximum maturity of fifteen years, and the average maturity of all securities shall be less than five years.
- All transactions are executed on a delivery-versus-payment basis.
- The standard of prudence to be used by investment personnel shall be the "Prudent Person Rule" and will be applied in the context of managing an overall portfolio.
- Securities shall not be purchased with trading or speculation as the dominant criterion for the selection of the security.

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Investments are recorded at fair value based on quoted market prices in accordance with Statement No. 31 of the GASB. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

As of December 31, 2010 and 2009, the Department’s dedicated investments and the City’s pool and other investments were as follows:

2010	Fair Value				Weighted-Average Maturity (Days)
	Dedicated Investments of the Department	City Pool	Other City Dedicated Pool	Total	
Repurchase agreements	\$ -	\$ 56,365,904	\$ -	\$ 56,365,904	3
U.S. treasuries and U.S. government-backed securities	-	39,624,611	-	39,624,611	398
U.S. government agencies securities	38,493,063	624,898,866	43,041,093	706,433,022	655
U.S. government agency mortgage-backed securities	-	3,105,145	-	3,105,145	771
Commercial paper	-	256,364,545	-	256,364,545	21
Municipal bonds	-	1,020,110	-	1,020,110	213
Total	<u>\$ 38,493,063</u>	<u>\$ 981,379,181</u>	<u>\$ 43,041,093</u>	<u>\$1,062,913,337</u>	
Portfolio weighted-average maturity					458

2009	Fair Value				Weighted-Average Maturity (Days)
	Dedicated Investments of the Department	City Pool	Other City Dedicated Pool	Total	
Repurchase agreements	\$ -	\$ 116,779,375	\$ -	\$ 116,779,375	4
U.S. treasuries and U.S. government-backed securities	-	13,495,781	83,569,314	97,065,095	301
U.S. government agencies securities	-	475,648,453	-	475,648,453	558
U.S. government agency mortgage-backed securities	-	7,510,832	-	7,510,832	14
Commercial paper	-	221,242,855	16,289,929	237,532,784	52
Municipal bonds	-	10,136,607	-	10,136,607	223
Total	<u>\$ -</u>	<u>\$ 844,813,903</u>	<u>\$ 99,859,243</u>	<u>\$ 944,673,146</u>	
Portfolio weighted-average maturity					335

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As of December 31, 2010 and 2009, the Department's share of the City pool was as follows:

	2010	2009
Cash and equity in pooled investments:		
Restricted assets	\$ 101,413,002	\$ 31,639,850
Current assets	<u>56,931,666</u>	<u>32,694,670</u>
Total	<u>\$ 158,344,668</u>	<u>\$ 64,334,520</u>
Balance as a percentage of City pool	16.1 %	7.6 %

Interest Rate Risk—Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. The City's investment policy limits the maturity of individual securities to fifteen years and limits the weighted average maturity of the total investment portfolio to no longer than five years.

Credit Risk—Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The City mitigates credit risk in many ways.

By state statutes and investment policy, the City may purchase securities that carry the highest credit ratings issued by Moody's Investors Service, Standard & Poor's, and/or Fitch Ratings. Securities purchased must have the following ratings: Securities backed by issuers with long-term credit ratings of Aaa, Aa1, and Aa2 by Moody's Investors Service; AAA, AA+, and AA by Standard & Poor's; and AAA, AA+, and AA by Fitch Ratings; and securities backed by issuers having short-term ratings of MIG1, VMIG1, and P1 by Moody's Investors Service; A-1+ and A-1 by Standard & Poor's; and F1+ and F1 by Fitch Ratings.

The City invests in U.S. Treasury securities which are considered free of credit risk, and in securities backed by the full faith and credit of the U.S. government, such as bonds issued by the Department of Housing and Urban Development (HUD). These securities have the highest long-term and short-term credit ratings of Aaa and P1 by Moody's Investors Service, AAA, and A-1+ by Standard & Poor's and AAA and F1+ by Fitch Ratings. The City also invests in securities issued by U.S. government sponsored enterprises including Federal National Mortgage Association, Federal Home Loan Bank, Federal Home Loan Mortgage Corporation, and Federal Farm Credit Bank. These securities were rated Aaa by Moody's Investors Service and AAA by Standard & Poor's.

Material credit risk in the City's investment portfolio resides in its holdings of commercial paper and municipal securities. In accordance with state statutes and its internal investment policy, the City manages that credit risk by purchasing securities backed by issuers having long-term and short-term credit ratings as noted above. The City also subscribes to asset-backed commercial paper research from Moody's Investors Service and Fitch Ratings, conducts internal due diligence of commercial paper and municipal issuers, and maintains an "approved list" of commercial paper issuers based upon internal and external credit research.

Concentration of Credit Risk—Concentration risk is the risk of loss attributed to the magnitude of investments in a single issuer other than the U.S. government or U.S. government-guaranteed issuer. In accordance with its investment policy and state statutes, the City manages concentration risk by limiting

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its investments in any one issuer as follows: 10% of the portfolio per bank for certificates of deposit or bankers' acceptances; 5% per commercial paper or municipal bond issuer; and 20% per U.S. government agency, excluding investments maturing less than one year from date of purchase. U.S. government agency collateralized mortgage obligations and pass-through securities are not subject to maximum agency limitations but are limited to a maximum asset allocation of 25% of the total portfolio.

The City's investments in single issuers, including those maturing less than one year from date of purchase, and amounting to 5% or more of the total portfolio as of December 31, 2010 and 2009, are shown in the following table.

Issuer	2010		2009	
	Fair Value	Percent of Total Investments	Fair Value	Percent of Total Investments
Federal National Mortgage Association (Fannie Mae)	\$ 276,373,623	26 %	\$ 99,106,306	10 %
Federal Home Loan Bank	218,644,903	21	198,997,599	21
Federal Home Loan Mortgage Corporation (Freddie Mac)	114,398,438	11	111,610,027	12
Federal Farm Credit Bank	100,121,203	9	73,445,353	8
U.S. treasuries	-	-	97,065,095	10
Wells Fargo	-	-	116,779,375	12
Commercial paper - Sheffield Receivables Corporation	54,343,164	5	-	-
Total	<u>\$ 763,881,331</u>	<u>72 %</u>	<u>\$ 697,003,755</u>	<u>73 %</u>

The Department's dedicated investments in which 5% or more is invested in any single issuer as of December 31, 2010 and 2009 were as follows:

Issuer	2010		2009	
	Fair Value	Department Percent of Total Investments	Fair Value	Department Percent of Total Investments
Federal Home Loan Bank	\$ 38,493,063	100 %	\$ -	- %
Total	<u>\$ 38,493,063</u>	<u>100 %</u>	<u>\$ -</u>	<u>- %</u>

Custodial Credit Risk—Investments—The custodial credit risk for investments is the risk that, in the event of failure of the counterparty, the City will not have access to, or be able to recover, its investments or collateral securities that are in the possession of an outside party. The City minimizes custodial credit risk for its investments by having its investment securities held by the City's contractual custodial agent and not by the counterparty or the counterparty's trust department or agent. Additionally, the City mitigates custodial risk by settling its trades delivery versus payment through the City's contractual custodial agent.

By investment policy, the City maintains a list of approved securities dealers for transacting business. For repurchase agreements, the City transacts only with large primary dealers with investment grade

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credit ratings provided by at least two of the nationally recognized statistical rating organizations (NRSROs). The City also conducts its own due diligence as to the financial wherewithal of its counterparties.

The City mitigates counterparty custodial risk from repurchase agreements by using a third-party custodian for tri-party repos. The City conforms with industry standard requiring execution of a master repurchase agreement with each counterparty prior to transacting a repurchase agreement, execution of a third-party custodial agreement between the City, the broker, and the clearing bank, before transacting a third-party repurchase agreement, and over-collateralizing by a minimum of 102%. By investment policy, the underlying securities the City is willing to accept as collateral must have the highest credit ratings of at least two NRSROs. Throughout 2010, the collateral underlying the City's repurchase agreements excluded securities other than U.S. Treasury, agencies, and agency mortgage-backed pass-throughs.

Foreign Currency Risk—The City Treasury investment pool and securities held for dedicated funds portfolios do not invest in foreign currencies.

Reverse Repurchase Agreements—RCW 35.39.030 and City investment policy allow the investment of City monies in excess of current City needs in reverse repurchase agreements. However, the City does not engage itself in this type of investment strategy.

The City of Seattle's Comprehensive Annual Financial Report may be obtained by writing to The City of Seattle, Department of Finance and Administrative Services, P.O. Box 94680, Seattle, WA 98124-4689; telephone: (206) 684-8306, or obtained on-line at <http://www.seattle.gov/cafrs/>.

5. ACCOUNTS RECEIVABLE

Accounts receivable at December 31, 2010 and 2009, consist of:

	Retail Electric	Wholesale Power	Other Operating	Operating Subtotal	Nonoperating Subtotal	Total
2010						
Accounts receivable	\$ 56,010,841	\$ 15,569,969	\$ 8,260,644	\$ 79,841,454	\$ 9,912,899	\$ 89,754,353
Less allowance for doubtful accounts	<u>(6,274,400)</u>	<u>(814,275)</u>	<u>(3,676,189)</u>	<u>(10,764,864)</u>	<u>-</u>	<u>(10,764,864)</u>
	<u>\$ 49,736,441</u>	<u>\$ 14,755,694</u>	<u>\$ 4,584,455</u>	<u>\$ 69,076,590</u>	<u>\$ 9,912,899</u>	<u>\$ 78,989,489</u>
2009						
Accounts receivable	\$ 43,112,309	\$ 12,990,648	\$ 3,888,849	\$ 59,991,806	\$ 11,994,266	\$ 71,986,072
Less allowance for doubtful accounts	<u>(4,341,181)</u>	<u>(814,275)</u>	<u>(1,982,832)</u>	<u>(7,138,288)</u>	<u>-</u>	<u>(7,138,288)</u>
	<u>\$ 38,771,128</u>	<u>\$ 12,176,373</u>	<u>\$ 1,906,017</u>	<u>\$ 52,853,518</u>	<u>\$ 11,994,266</u>	<u>\$ 64,847,784</u>

Wholesale power receivable includes \$2.8 million at December 31, 2010, and \$3.7 million at December 31, 2009, for exchange energy at fair value under long-term contracts (see Notes 10 and 15).

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6. SHORT-TERM ENERGY CONTRACTS AND DERIVATIVE INSTRUMENTS

The Department engages in an ongoing process of resource optimization, which involves the economic selection from available energy resources to serve the Department's load obligations and using these resources to capture available economic value. The Department makes frequent projections of electric loads at various points in time based on, among other things, estimates of factors such as customer usage and weather, as well as historical data and contract terms. The Department also makes recurring projections of resource availability at these points in time based on variables such as estimates of streamflows, availability of generating units, historic and forward market information, contract terms, and experience. On the basis of these projections, the Department purchases and sells wholesale electric capacity and energy to match expected resources to expected electric load requirements, and to realize earnings from surplus energy resources. These transactions can be up to 18 months forward. Under these forward contracts, the Department commits to purchase or sell a specified amount of energy at a specified time, or during a specified time in the future. Except for limited intraday and interday trading to take advantage of owned hydro storage, the Department does not take market positions in anticipation of generating revenue. Energy transactions in response to forecasted seasonal resource and demand variations require approval by the Department's Risk Oversight Council.

Effective January 1, 2009, the Department adopted Statement No. 53 of the GASB, *Accounting and Financial Reporting for Derivative Instruments*, which requires that changes in fair values of investment derivative instruments be recorded on the statement of revenues, expenses, and changes in equity and that changes in fair values of effective hedging derivative instruments be recorded as deferrals on the balance sheet, except as provided by the normal purchase and normal sales exception to that standard. It is the Department's policy to apply the normal purchase and normal sales exception of Statement No. 53 as appropriate. Certain forward purchase and sale of electricity contracts meet the definition of a derivative instrument, but are intended to result in the purchase or sale of electricity delivered and used in the normal course of operations. Accordingly, the Department considers these forward contracts as normal purchase and normal sales under Statement No. 53. These transactions are not required to be recorded at fair value in the financial statements.

The aggregate contract amounts, fair value, and unrealized gain (loss) of the Department's commodity derivative instruments qualifying as normal purchases and normal sales at December 31 follows:

2010	Aggregate Contract Amount	Aggregate Fair Value	Unrealized Gain (Loss)
Sales	\$ 8,027,513	\$ 7,296,124	\$ 731,389
Purchases	11,894,685	11,139,187	(755,498)
	<u>\$ 19,922,198</u>	<u>\$ 18,435,311</u>	<u>\$ (24,109)</u>
2009	Aggregate Contract Amount	Aggregate Fair Value	Unrealized Gain (Loss)
Sales	\$ 14,971,214	\$ 14,624,226	\$ 346,988
Purchases	3,746,000	3,686,756	(59,244)
	<u>\$ 18,717,214</u>	<u>\$ 18,310,982</u>	<u>\$ 287,744</u>

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Fair value measurements at December 31, 2010 and 2009 used an income valuation technique consisting of Platts M2M Power Curves and interest rates from HIS Global Insight that are used to calculate discount rates. Risk, such as for nonperformance and inactive markets, was evaluated internally resulting in no valuation adjustments to forward power contracts.

All derivative instruments not considered as normal purchases and normal sales are to be recorded within the financial statements. In 2010, the Seattle City Council adopted a resolution granting the Department authority to enter into certain physical put and call options that would not be considered normal purchases and normal sales under Statement No. 53. The Department did not have any such activity for 2010 and 2009. In addition, the Seattle City Council has deferred recognition of the effects of reporting the fair value of derivative financial instruments for rate-making purposes, and maintains regulatory accounts to defer the accounting impact of these accounting adjustments in accordance with ASC 980-10-05, *Effect of Regulatory Accounting* (see Notes 11 and 12).

Market Risk—Market risk is, in general, the risk of fluctuation in the market price of the commodity being traded and is influenced primarily by supply and demand. Market risk includes the fluctuation in the market price of associated derivative commodity instruments. Market risk may also be influenced by the number of active, creditworthy market participants, and to the extent that nonperformance by market participants of their contractual obligations and commitments affects the supply of, or demand for, the commodity.

Credit Risk—Credit risk relates to the potential losses that the Department would incur as a result of nonperformance by counterparties of their contractual obligations to deliver energy or make financial settlements. Changes in market prices may dramatically alter the size of credit risk with counterparties, even when conservative credit limits are established. The Department seeks to mitigate credit risk by: entering into bilateral contracts that specify credit terms and protections against default; applying credit limits and duration criteria to existing and prospective counterparties; and actively monitoring current credit exposures. The Department also seeks assurances of performance through collateral requirements in the form of letters of credit, parent company guarantees, or prepayment.

The Department has concentrations of suppliers and customers in the electric industry including: electric utilities; electric generators and transmission providers; financial institutions; and energy marketing and trading companies. In addition, the Department has concentrations of credit risk related to geographic location as it operates in the western United States. These concentrations of counterparties and concentrations of geographic location may impact the Department's overall exposure to credit risk, either positively or negatively, because the counterparties may be similarly affected by changes in conditions.

Other Operational and Event Risk—There are other operational and event risks that can affect the supply of the commodity, and the Department's operations. Due to the Department's primary reliance on hydroelectric generation, the weather, including spring time snow melt, runoff, and rainfall, can significantly affect the Department's operations. Other risks include regional planned and unplanned generation outages, transmission constraints or disruptions, environmental regulations that influence the availability of generation resources, and overall economic trends.

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7. LONG-TERM DEBT

At December 31, 2010 and 2009, the Department’s long-term debt consisted of the following prior lien or parity bonds:

LONG-TERM

	Fixed Rate	Maturity Year	Original Issuance	2010	2009
Prior Lien Bonds:					
2010A ML&P Build America Bonds	4.447%–5.570%	2040	\$ 181,625,000	\$ 181,625,000	\$ -
2010B ML&P Improvement and Refunding Revenue Bonds	2.000%–5.000%	2026	596,870,000	596,870,000	-
2010C ML&P Recovery Zone Economic Development Bonds	5.590%–5.590%	2040	13,275,000	13,275,000	-
2008 ML&P Revenue and Refunding Revenue Bonds	4.000%–6.000%	2029	257,375,000	241,805,000	251,015,000
2004 ML&P Improvement and Refunding Revenue Bonds	3.000%–5.250%	2029	284,855,000	244,735,000	254,020,000
2003 ML&P Improvement and Refunding Revenue Bonds	4.000%–6.000%	2028	251,850,000	134,045,000	146,815,000
2002 ML&P Refunding Revenue Bonds	3.000%–4.500%	2014	87,735,000	17,590,000	28,265,000
2001 ML&P Improvements and Refunding Revenue Bonds	5.000%–5.500%	2026	503,700,000	106,830,000	443,980,000
2000 ML&P Revenue Bonds	4.500%–5.625%	2025	98,830,000	-	86,475,000
1998B ML&P Revenue Bonds	4.750%–5.000%	2024	90,000,000	-	72,590,000
1998A ML&P Refunding Revenue Bonds	4.500%–5.000%	2020	104,650,000	-	77,325,000
1997 ML&P Revenue Bonds	5.000%–5.125%	2022	30,000,000	-	22,565,000
Total prior lien bonds			<u>\$2,500,765,000</u>	<u>\$1,536,775,000</u>	<u>\$1,383,050,000</u>

The Department had the following activity in long-term debt during 2010 and 2009:

2010	Balance at 12/31/09	Additions	Reductions	Balance at 12/31/10	Current Portion
Prior Lien Bonds	\$ 1,383,050,000	\$ 791,770,000	\$ (638,045,000)	\$ 1,536,775,000	\$ 58,685,000
Total	<u>\$ 1,383,050,000</u>	<u>\$ 791,770,000</u>	<u>\$ (638,045,000)</u>	<u>\$ 1,536,775,000</u>	<u>\$ 58,685,000</u>
2009	Balance at 12/31/08	Additions	Reductions	Balance at 12/31/09	Current Portion
Prior Lien Bonds	\$ 1,457,400,000	\$ -	\$ (74,350,000)	\$ 1,383,050,000	\$ 80,735,000
Subordinate Lien Bonds	<u>71,975,000</u>	<u>-</u>	<u>(71,975,000)</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 1,529,375,000</u>	<u>\$ -</u>	<u>\$ (146,325,000)</u>	<u>\$ 1,383,050,000</u>	<u>\$ 80,735,000</u>

Prior Lien Bonds—In May 2010, the Department issued \$791.8 million of Municipal Light and Power (ML&P) Improvement Revenue and Refunding Revenue Bonds (2010 Bonds). The 2010 Bonds were comprised of \$181.6 million 2010A series taxable ML&P Build America Bonds, \$596.9 million 2010B series tax exempt ML&P Improvement and Refunding Revenue Bonds, and \$13.3 million 2010C series taxable ML&P Revenue Recovery Zone Economic Development Bonds. The taxable 2010A series bonds’ coupon interest rates ranged from 4.45% to 5.57% and mature serially from February 1, 2021 through 2027 with term bonds maturing February 1, 2040. The tax exempt 2010B series bonds mature serially from February 1, 2011 through 2026 with coupon interest rates ranging from 2.00% to 5.00%. The taxable 2010C series bonds mature on February 1, 2040 with a coupon interest rate of 5.59%. The arbitrage yield was 3.53%, 3.18%, and 3.08% for the 2010A series, 2010B series, and 2010C series bonds, respectively. 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 from the 2010 bonds are being used to finance certain capital improvement and conservation programs

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and also were used to advance refund a total of \$570.7 million of certain outstanding prior lien bonds including the 1997, 1998A, 1998B, 2000, and a significant portion of the 2001 series bonds.

The debt service on the 2010 bonds requires a cash flow over the life of the bonds of \$1.3 billion, including \$462.8 million in interest. The difference between the cash flows required to service the old and new debt and to complete the refunding totaled \$57.5 million, and the aggregate economic gain on refunding totaled \$51.8 million at net present value. The accounting loss on refunding was \$18.8 million and is being amortized using the effective interest method over the life of the refunded bonds. The unamortized balance of the loss on refunding for all bonds was \$33.4 million at December 31, 2010 and \$27.9 million at December 31, 2009, respectively.

The 2010A series and 2010C series bonds provide a refundable tax credit or federal subsidy paid to state or local governmental issuers by the United States Internal Revenue Service. The amount of the federal subsidies are equal to 35% of the total coupon interest payable to investors for the 2010A series bonds and 45% of the total coupon interest payable to investors for the 2010C series bonds. These federal subsidies ultimately result in a net decrease to debt service, although debt service payments are paid gross. The federal subsidies are recorded as non-operating revenues on the statements of revenues, expenses, and changes in equity.

Debt service requirements for prior lien bonds, excluding federal subsidies for the 2010 bonds, are as follows:

Years Ending December 31	Principal Redemptions	Interest Requirements	Total
2011	\$ 58,685,000	\$ 83,148,394	\$ 141,833,394
2012	83,865,000	73,257,371	157,122,371
2013	90,335,000	69,303,234	159,638,234
2014	91,565,000	65,011,034	156,576,034
2015	93,165,000	60,367,040	153,532,040
2016 – 2020	437,840,000	234,089,369	671,929,369
2021 – 2025	393,940,000	129,777,212	523,717,212
2026 – 2030	171,485,000	50,311,073	221,796,073
2031 – 2035	52,730,000	25,160,154	77,890,154
2036 – 2040	63,165,000	9,058,602	72,223,602
Total	<u>\$1,536,775,000</u>	<u>\$799,483,483</u>	<u>\$2,336,258,483</u>

The Department is required by Ordinance No. 123169 (the bond ordinance) to fund reserves for the 2010 Bonds and other Parity Bonds in the Municipal Light and Power Bond Reserve Fund (Reserve Fund) in an amount at any time equal to the lesser of (a) the maximum annual debt service on all Parity Bonds then outstanding; and (b) the maximum amount permitted by the Internal Revenue Code (IRC) as a reasonably required reserve or replacement fund (Reserve Requirement). The Reserve Requirement upon issuance of the 2010 Bonds was an amount equal to \$96.3 million (125% of average annual debt service). The maximum annual debt service on prior lien bonds is \$159.6 million due in 2013 and the average annual debt service was \$77.1 million at issuance of the 2010 Bonds. No proceeds of the 2010 Bonds were deposited in the Reserve Fund (an account within the books of the Department). Upon issuance of the 2010 Bonds, the Reserve Requirement was met by an existing surety bond purchased in

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2005 from Financial Security Assurance, Inc., which is now known as Assured Guarantee Municipal Corporation, in the amount of \$109.5 million. The surety bond will expire on August 1, 2029. Assured Guarantee Municipal Corporation is currently rated Aa3 and AAA by Moody's and Standard & Poor's, respectively. The bond ordinance does not require that the Reserve Requirement be funded with cash, a substitute surety bond, or letter of credit, if the provider of qualified insurance is downgraded. Under the bond ordinance, a surety bond qualifies as Qualified Insurance for purposes of satisfying the Reserve Requirement if the provider's ratings are in one of the top two rating categories at the time the policy is issued, even if the provider of such surety bond is subsequently downgraded.

A portion of the proceeds from the 2010 revenue refunding bonds were placed in a separate irrevocable trust to provide for all future debt service payments on certain prior lien bonds advance refunded or defeased. There were balances outstanding in the irrevocable trust during 2010 for prior lien bonds advance refunded with the 2010 Bonds and no balances were outstanding for prior lien bonds advance refunded prior to 2010. Neither the assets of the trust account nor the liabilities for the defeased bonds are reflected in the Department's financial statements. These bonds had an outstanding principal balance of \$311.7 million as of December 31, 2010 with no balance outstanding as of December 31, 2009. Funds held in the 2010 trust account as of December 31, 2010 were sufficient to service and redeem the defeased bonds. \$259.0 million of bonds defeased in 2010 were called and repaid in full during 2010 and \$311.7 million of the 2001 bond series were called on March 1, 2011.

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 claims 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 \$70.0 million or 15% of the aggregate principal amount of prior lien bonds then outstanding. All subordinate lien bonds totaling \$72.0 million were repaid in full in February 2009 and no subordinate bonds were outstanding as of December 31, 2010.

Revenue Pledged—All revenue bonds are special limited obligations payable from and secured solely by the gross revenues of the Department, less charges for maintenance and operations, and by money in the debt service account and Reserve Fund. Principal and interest paid for 2010 and 2009 was \$118.4 million and \$144.9 million, respectively. Total revenue available for debt service as defined for the same periods was \$210.4 million and \$199.7 million. Annual interest and principal payments are expected to require 67.4% of revenues available for debt service for 2010 and required 75.5 % in 2009.

Federal Arbitrage Regulations—All revenue bonds are subject to federal arbitrage regulations and the Department has complied with these regulations. There was no federal arbitrage rebate due in 2010 or 2009.

Other—There were no liens on property or revenue pertaining to parity bonds and all bond covenants were in compliance for the Department's prior lien bonds as of December 31, 2010 and 2009, respectively.

Fair Value—Fair values at December 31, 2010 and 2009 were provided by the Department's financial advisor, Seattle Northwest Securities, and were based on observable inputs consisting of subscription service indices that reflect the current yields of municipal debt; yields were adjusted for the differential in credit for the Department's bonds. The fair value for the Department's bonds are estimated based on the quoted market prices for the same or similar issues or on the current rates offered to the Department

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for debt of the same remaining maturities. Carrying amounts (net of premiums and discounts) and fair values at December 31, 2010 and 2009, are as follows:

	2010		2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt:				
Prior lien bonds	\$ 1,607,921,444	\$ 1,623,269,589	\$ 1,408,006,718	\$ 1,453,781,594
Total	\$ 1,607,921,444	\$ 1,623,269,589	\$ 1,408,006,718	\$ 1,453,781,594

Amortization—Bond issue costs, including the surety bond, 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 effective interest methods over the terms of the issues to which they pertain. Deferred refunding costs amortized to interest expense totaled \$5.1 million in 2010 and \$4.6 million in 2009. Deferred refunding costs in the amount of \$33.4 million and \$27.9 million are reported as a component of long-term debt in the 2010 and 2009 balance sheets, respectively.

Noncurrent Liabilities—The Department had the following activities during 2010 and 2009:

2010	Balance at 12/31/09	Additions	Reductions	Balance at 12/31/10	Current Portion
Compensated absences	\$ 14,789,136	\$ 19,105,587	\$ (18,354,241)	\$ 15,540,482	\$ 1,560,966
Other	3,448,056	1,118,340	(11,841)	4,554,555	-
Deferred revenue - rate stabilization account	-	54,265,627	-	54,265,627	-
Other deferred credits	28,726,364	192,596,141	(197,772,572)	23,549,933	-
Total	\$ 46,963,556	\$ 267,085,695	\$ (216,138,654)	\$ 97,910,597	\$ 1,560,966

2009	Balance at 12/31/08	Additions	Reductions	Balance at 12/31/09	Current Portion
Compensated absences	\$ 13,662,932	\$ 19,258,166	\$ (18,131,962)	\$ 14,789,136	\$ 1,330,512
Other	2,387,451	1,085,125	(24,520)	3,448,056	-
Deferred revenue - rate stabilization account	-	-	-	-	-
Other deferred credits	30,736,545	239,924,303	(241,934,484)	28,726,364	-
Total	\$ 46,786,928	\$ 260,267,594	\$ (260,090,966)	\$ 46,963,556	\$ 1,330,512

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**NOTES TO FINANCIAL STATEMENTS
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8. ACCOUNTS PAYABLE

Accounts Payable and Other Current Liabilities—The composition of accounts payable and other current liabilities at December 31, 2010 and 2009, is as follows:

	2010	2009
Vouchers payable	\$ 19,219,869	\$ 18,363,583
Power accounts payable	18,320,724	22,310,215
Taxes payable	9,932,180	10,065,814
Claims payable	10,926,243	7,895,892
Guarantee deposit and contract retainer	632,082	795,352
Other accounts payable	<u>1,055,971</u>	<u>880,012</u>
 Total	 <u>\$ 60,087,069</u>	 <u>\$ 60,310,868</u>

9. SEATTLE CITY EMPLOYEES’ RETIREMENT SYSTEM AND OTHER POSTEMPLOYMENT BENEFITS

Pension Benefits—The Seattle City Employees’ Retirement System (SCERS) is a single-employer defined benefit public employee retirement system, covering employees of the City 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 pension trust fund of the City.

All employees of the City 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. Employees of the King County Departments of Transportation and Public Health who established membership in SCERS when these organizations were City departments were allowed to continue their SCERS membership. As of December 31, 2010, there were 5,440 retirees and beneficiaries receiving benefits and 10,638 active members of SCERS. In addition, 1,998 vested terminated employees were entitled to future benefits.

SCERS provides retirement, death, and disability benefits. Retirement benefits vest after 5 years of credited service, while death and disability benefits vest after 10 years of service. Retirement benefits are calculated 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. Future increases in the cost-of-living adjustments are available to current and future retired members only if SCERS attains at least a 95% funding level. SCERS does not provide termination benefits.

The contribution requirements of plan members and the City are established and may be amended by the City Council. Plan members are required to contribute 8.03% of their annual covered salary. The City is required to contribute at an actuarially determined rate, equal to at least that of the members’ contribution rate. The City’s contribution rates during 2010 and 2009 were 8.03% of annual covered payroll. Actuarially recommended contribution rates both for members and for the employer were 8.03% of covered payroll during 2010 and 2009.

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The City's contracts with all labor unions that represent members of SCERS describe how contribution rates would be changed in the event higher contributions are needed to improve the financial status of the Employee's Retirement Fund. On November 22, 2010, the Seattle City Council adopted Council Bill No. 117018, Ordinance No. 123482, amending Seattle Municipal Code Section 4.36.110 to provide for contribution rate increases for members of the City's Retirement System. Effective for the first full pay period in January 2011 and January 2012, the rate of employee and employer contributions will be 9.03% and 10.03%, respectively. The increase in contribution rates, as noted in the actuary's January 1, 2010 valuation report, is necessary to acknowledge the financial and economic recession of 2007/2008 which adversely impacted the Retirement System's assets. Also, plan demographics show active members in the Retirement System retire later in life and live longer, placing a heavier liability on the Retirement System assets. Changes to the contribution rates are necessary to ensure continued financial support to the retired employees of the City of Seattle.

Under the authority of the state and City, SCERS operates a securities lending program, and there were transactions during 2010 and 2009. In 2010 and 2009, SCERS did not incur a loss as a result of borrower default. SCERS did not have negative credit exposure at December 31, 2010 or 2009. In 2008, SCERS experienced a loss resulting from a default by an issuer. This loss from default is proceeding through the bankruptcy process and as of December 31, 2010 and 2009, the securities lending program's exposure was limited to less than \$75.0 million.

SCERS issues a stand-alone financial report that may be obtained by writing to the Seattle City Employees' Retirement System, 720 Third Avenue, Suite 900, Seattle, WA 98104; by telephone at (206) 386-1293; or by accessing the web site http://www.seattle.gov/retirement/annual_report.htm.

Employer contributions for the City were \$45.2 million and \$46.7 million in 2010 and 2009. Employer contributions for the Department were \$10.2 million and \$10.4 million in 2010 and 2009. The annual required contributions were made in full.

Actuarial Data

Valuation date	January 1, 2010
Actuarial cost method	Entry age
Amortization method	Level percent
Remaining amortization period	Does not amortize**
Amortization period	Maximum of 30 years
Asset valuation method	Fair Value

Actuarial Assumptions*

Investment rate of return	7.75%
Projected general wage increases	4.00%
Postretirement benefit increases	1.50%
Cost-of-living year-end bonus dividend	0.00%

* Includes price inflation at 3.5% and 0.5% of payroll growth.

** The contribution rates currently in effect do not amortize the UAAL over any period of time.

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**NOTES TO FINANCIAL STATEMENTS
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Annual Pension Cost and Net Pension Obligation

For Fiscal Year Ending December 31, 2009

Based on January 1, 2008 Valuation

		Fiscal Year Ended December 31	
		2009	2008
1a	Total normal cost rate	13.32 %	13.32 %
1b	Employee contribution rate	<u>8.03 %</u>	<u>8.03 %</u>
1c	Employer normal cost rate (1a-1b)	5.29 %	5.29 %
2a	Total employer contribution rate	8.03 %	8.03 %
2b	Amortization payment rate (2a-1c)	2.74 %	2.74 %
2c	Amortization period*	16.20	16.20
2d	GASB 27 amortization rate	2.74 %	2.74 %
3	Total annual required contribution (ARC) rate (1c+2d)	8.03 %	8.03 %
4	Covered employee payroll**	\$ 580,948,555	\$ 572,366,625
5a	ARC (3x4)	\$ 46,650,169	\$ 45,961,040
5b	Interest on net pension obligation (NPO)	(6,056,564)	(6,078,596)
5c	ARC adjustment	<u>6,339,817</u>	<u>6,362,880</u>
5d	Annual pension cost (APC) (5a+5b+5c)	\$ 46,933,422	\$ 46,245,324
6	Employer contribution	\$ 46,650,169	\$ 45,961,040
7a	Change in NPO (5d-6)	\$ 283,253	\$ 284,284
7b	NPO at beginning of year	<u>(78,149,216)</u>	<u>(78,433,500)</u>
7c	NPO at end of year (7a+7b)	\$ (77,865,963)	\$ (78,149,216)

* If the amortization period determined by the actual contribution rate exceeds the maximum amortization period required by GASB Statement No. 27, the ARC is determined using an amortization of the UAAL over 30 years.

** Covered payroll includes compensation paid to all active employees on which contributions were made in the year preceding the valuation date.

The schedules of funding progress (\$ in millions) for SCERS are as follows:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liabilities (AAL) ⁽¹⁾ (b)	Unfunded AAL (UAAL) ⁽²⁾ (b-a)	Funding Ratio (a/b)	Covered Payroll ⁽³⁾ (c)	UAAL (or Excess) as a Percentage of Covered Payroll ((b-a)/c)
January 1, 2006	\$ 1,791.8	\$ 2,017.5	\$ 225.8	88.8 %	\$ 447.0	50.5 %
2008	2,119.4	2,294.6	175.2	92.4	501.9	34.9
2010	1,645.3	2,653.8	1,008.5	62.0	580.9	173.6

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- (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 were made in the year preceding the valuation date.

Other Postemployment Benefits (OPEB)—Health care plans for active and retired employees are administered by the City of Seattle as single-employer defined benefit public employee health care plans.

Eligible retirees may contribute to the medical and any additional health care programs contemplated or amended by ordinance of the Seattle City Council and as provided in Seattle Municipal Code 4.50.020.

The Seattle City Council authorizes the obligations of the plan members and the City as employer by passing ordinances and amendments regarding contributions to the plans. Eligible retirees up to age 65 self-pay 100% of the premium based on blended rates which were established by including the experience of retirees with the experience of active employees for underwriting purposes. The plan is financed on a pay-as-you-go basis, and the City's expected contribution for employer-paid benefits was \$3.2 million in 2010 and \$3.0 million in 2009. The Department's portion of the expected contribution was \$0.5 million in 2010 and \$0.4 million in 2009. The City recorded an expense and liability for OPEB of \$7.2 million in 2010 and \$6.4 million in 2009. The Department recorded an expense and liability for OPEB of \$1.1 million in 2010 and \$1.1 million in 2009.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and plan members in the future. Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. Based on the latest biennial actuarial valuation date the significant methods and assumptions are as follows:

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Actuarial data and assumptions

Valuation date	January 1, 2010
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Initial amortization period	30 years, open
Discount rate	4.39%
Health care cost trend rates—medical:	Aetna plans: 10.0%, decreasing by 0.5% each year for 10 years to an ultimate rate of 5.0%. Group Health plans: 9.5%, decreasing by 0.5% each year for 9 years to an ultimate rate of 5.0%
Participation	40% of Active Employees who retire participate
Mortality	General Service Actives and Retirees based on the Group Annuity Mortality (GAM) 1994 Static Table (Final) with ages set forward one year for male and female actives; set forward one year for male retirees and no age adjustment for female retirees.
Marital status	60% of members electing coverage: married or have a registered domestic partner. Male spouses two years older than their female spouses.
Morbidity factors	Morbidity rate ranges for ages 50 through 64: Aetna Traditional 104.3% to 172.5% for male retirees, 76.8% to 127.1% for female retirees, 138.9% to 229.8% for male spouses, and 102.3% to 169.3% for female spouses. Aetna Preventive 112.6% to 186.4% for male retirees, 83.0% to 137.3% for female retirees, 138.6% to 229.4% for male spouses, and 102.1% to 169.0% for female spouses. For the Aetna plans, because the retirees' spouses pay a lower premium for health care coverage than retirees, the net cost to the City for the spouse coverage is greater than for a retiree of the same age and gender. The morbidity factors were adjusted to reflect this discrepancy.
Group Health Standard and Deductible Plans	123.0% to 203.6% for males, and 90.6% to 150.0% for females.
Other considerations	Active employees with current spouse and/or dependent coverage elect same plan and coverage. After retirement, it is assumed that children will have aged off of coverage and will have \$0 liability.

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Based on the actuarial valuation date of January 1, 2010, the City's annual cost for fiscal years ended December 31, 2010 and 2009, the amount of expected contribution to the plan, and changes in net obligation are as follows:

	2010	2009
Annual required contribution	\$ 10,709,000	\$ 9,269,000
Interest on net OPEB obligation	898,000	693,000
Adjustment to annual required contribution	<u>(1,239,000)</u>	<u>(915,000)</u>
Annual OPEB cost (expense)	10,368,000	9,047,000
Expected contribution (employer-paid benefits)	<u>(3,202,000)</u>	<u>(2,954,000)</u>
Increase in net OPEB obligation	7,166,000	6,093,000
Net OPEB Obligation - beginning of the year	<u>20,446,000</u>	<u>14,352,775</u>
Net OPEB obligation - end of year	<u>\$ 27,612,000</u>	<u>\$ 20,445,775</u>

The schedules of funding progress (\$ in millions) are as follows:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liabilities (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funding Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
January 1, 2006	\$ -	\$ 84.3	\$ 84.3	- %	\$ 734.5	11.5 %
2008	-	78.8	78.8	-	837.1	9.4
2010	-	93.5	93.5	-	869.1	10.8

The Health Care Subfund of the General Fund is reported in The City of Seattle's Comprehensive Annual Financial Report.

10. LONG-TERM PURCHASED POWER, EXCHANGES, AND TRANSMISSION

Bonneville Power Administration—The Department purchases electric energy from the U.S. Department of Energy, Bonneville Power Administration (Bonneville) under the Block and Slice Power Sales Agreement, a 10-year contract that expires September 30, 2011. The agreement provides power equal to the Department's annual net requirement, defined as the difference between projected load and firm resources declared to serve that load. The Block product provides fixed amounts of power per month.

In 2006, the Department and Bonneville amended the Block agreement to enable the Department to participate in the Bonneville Flexible Priority Firm (PF) Program. Under the provisions of this program, which expired in 2009, the Block product was subject to a Flexible PF Charge on a power bill increasing the amount payable by the Department for power service in a given month followed by reductions in the amount payable for power service in subsequent months until the charge was recovered. Participation in the program provided the Department with a monthly discount on its Block bill whether or not the Flexible PF Charge was applied. In order to participate, the Department was required to enter into an irrevocable standby letter of credit for \$16.5 million issued by the Bank of America with a term from

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October 1, 2006 through September 30, 2009; the letter of credit was not renewed. The Flexible PF Charge was not applied in 2010 or 2009.

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 cost of Slice power is based on the Department's same percentage (4.6676%) of the expected costs of the system and is subject to true-up adjustments based on actual costs with specified exceptions. Subsequent amendments to the contract provide that Bonneville will pay the Department for qualified energy savings realized through specified programs and decrement Block purchases accordingly.

Bonneville's Residential Exchange Program (REP) was established as a mechanism to distribute financial benefits of the Federal Columbia River Power System to residential customers of the region's investor owned utilities (IOUs). In May 2007, the Ninth Circuit Court rulings found the 2000 REP Settlement Agreements with IOUs inconsistent with the Northwest Power Act. The Department received \$6.0 million and \$10.9 million in 2010 and 2009 respectively in payments and billing credits related to both the Block and Slice agreements.

In December of 2008 the Department entered into a new contract to purchase both Block and Slice energy from Bonneville for the period October 1, 2011 through September 30, 2028. Block quantities, Slice percentage, and Bonneville rates are expected to be recalculated periodically during the contract. The Block quantities, Slice percentage, and Bonneville rates were not finalized as of the end of 2010. Accordingly, certain estimates and assumptions were used in the calculations in the estimated future payments table below.

Lucky Peak—In 1984, the Department entered into a purchase power agreement with four irrigation districts to acquire 100% of the net surplus output of a hydroelectric facility that began commercial operation 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, and the FERC license expires in 2030. 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.

British Columbia—High Ross Agreement—In 1984, an agreement was reached between the Province of British Columbia and the City under which British Columbia will provide the Department with energy equivalent to that which would have resulted from an addition to the height of Ross Dam. Delivery of this energy began in 1986 and is to be received for 80 years. In addition to the direct costs of energy under the agreement, the Department incurred costs of approximately \$8.0 million in prior years related to the proposed addition and was obligated to help fund the Skagit Environmental Endowment Commission through four annual \$1.0 million payments. These other costs were included in utility plant-in-service as an intangible asset as defined in Statement No. 51, and are being amortized to purchase power expense over 35 years through 2035 (see Note 2).

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Energy received and expenses incurred under these and other long-term purchased power agreements at December 31, 2010 and 2009 are as follows:

	2010 Expense	2009 Expense	2010 Average Megawatts	2009
Bonneville Block	\$ 59,197,099	\$ 54,701,786	237.3	237.6
Bonneville Slice	104,140,385	98,983,673	361.1	379.4
	<u>163,337,484</u>	<u>153,685,459</u>	598.4	617.0
Lucky Peak	5,560,270	5,654,794	32.6	36.9
British Columbia - High Ross Agreement	13,411,346	13,405,324	35.1	35.7
Grant County Public Utility District	9,396,155	1,788,917	19.2	3.8
Grand Coulee Project Hydro Authority	5,263,342	5,010,391	27.5	29.7
Bonneville South Fork Tolt billing credit	(3,382,401)	(3,429,444)	-	-
British Columbia - Boundary Encroachment	-	-	1.8	1.7
Renewable energy - State Line Wind	18,979,230	19,015,418	39.8	40.2
Renewable energy - Other	4,921,501	989,721	9.7	1.8
Exchanges and loss returns energy at fair value	10,204,731	10,168,478	17.0	14.0
Long-term purchased power booked out	<u>(4,101,148)</u>	<u>(4,285,996)</u>	<u>(16.9)</u>	<u>(16.9)</u>
	<u>\$ 223,590,510</u>	<u>\$ 202,003,062</u>	<u>764.2</u>	<u>763.9</u>

Payments under these long-term power contracts totaled \$222.4 million and \$200.7 million in 2010 and 2009, respectively. Payments under transmission contracts totaled \$38.0 million and \$37.9 million in 2010 and 2009, respectively.

Energy Exchange—Northern California Power Agency (NCPA) and the Department executed a long-term Capacity and Energy Exchange Agreement in March 1993. The Department delivers energy to NCPA from June through October 15. NCPA returns energy under conditions specified in the contract at a 1.2:1 ratio of exchange power, from November through April. The agreement, which includes a financial settlement option, may be terminated effective May 31, 2014 or any May 31 thereafter with seven year's advance written notice by either party.

Renewable Energy Purchase and/or Exchanges—The Energy Independence Act, Chapter 19.285 Revised Code of Washington, requires all qualifying utilities in Washington State to meet certain annual targets of eligible new renewable resources and/or equivalent renewable energy credits as a percentage of total energy delivered to retail customers. The annual targets are: at least 3% by 2012, at least 9% by 2016, and at least 15% by 2020. The Department's resource portfolio for 2010 met the 3% 2012 target. Long-term renewable purchase or exchange agreements were executed with the Sacramento Municipal Utility District in 2007, Waste Management Renewable Energy, LLC in 2009, and the existing Stateline Wind Project contract, assigned to JP Morgan in 2010.

Fair Value of Exchange Energy—Exchange energy receivable and the related deferred gains at December 31, 2010 and 2009, were based on a market valuation technique that utilized Platts M2M Power Curves, Dow Jones U.S. Daily Electricity Price Indices for settled deliveries, and an income valuation technique that uses interest rate forecasts from HIS Global Insight that are used to calculate discount rates. Risk was evaluated internally resulting in no valuation adjustments (see Notes 12 and 15).

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Estimated Future Payments Under Purchased Power and Transmission Contracts—The Department’s estimated payments under its contracts with Bonneville, various public utility districts and irrigation districts, Lucky Peak Project, British Columbia—High Ross Agreement, JP Morgan (assigned from Iberdrola Renewables, Inc. in 2010) and PacifiCorp for wind energy and net integration and exchange services, and others, and for transmission with Bonneville, and others for the period from 2011 through 2065, undiscounted, are as follows:

Years Ending December 31	Estimated Payments ⁽¹⁾
2011	\$ 261,681,866
2012	254,385,397
2013	258,100,563
2014	262,752,899
2015	267,785,946
2016–2020	1,473,394,955
2021–2025 ⁽²⁾	1,427,045,903
2026–2030 ⁽³⁾	755,254,619
2031–2035	51,967,350
2036–2040 ⁽⁴⁾	32,528,944
2041–2045	3,231,324
2046–2065	<u>17,242,335</u>
Total	<u>\$5,065,372,101</u>

(1) 2011 to 2015 includes estimated REP recoveries from Bonneville.

(2) Bonneville transmission contract expires July 31, 2025.

(3) Bonneville new Block and Slice contract expires September 30, 2028.

(4) Lucky Peak contract expires September 30, 2038.

11. OTHER ASSETS

Seattle City Council passed resolutions authorizing the debt financing and/or deferral of certain costs in accordance with ASC 980-10-05, *Effect of Regulatory Accounting*. Programmatic conservation costs incurred by the Department and not funded by third parties and Endangered Species Act costs are deferred in accordance with ASC 980-10-05 and amortized over 20 years. Endangered Species Act costs are amortized over the remaining license period (see Note 16).

Other deferred assets, which are not covered under ASC 980-10-05, consist of:

- Suburban infrastructure long-term receivables are underground electrical infrastructure costs for suburban jurisdictions, which will be recovered through rates from customers within the respective jurisdictions for a period of approximately 25 years, as approved by the Seattle City Council.
- In 2010, the Department issued an interfund conservation loan to enhance lighting in the Seattle Municipal Tower where the Department’s administrative offices are located. The initial principal amount was \$1.7 million with a 10-year term. The total amount outstanding at December 31, 2010,

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was \$1.6 million, \$0.1 million of which is the amount due within one year and is included in Accounts receivable.

- Puget Sound Energy interconnection and substation, Studies, surveys, and investigations, and Unamortized debt expense are being amortized to expense over 4 to 36 years.
- The remaining components of other assets, Real estate and conservation loans receivable and General work-in-progress to be billed, are not amortized.

Regulatory deferred charges and other assets net at December 31, 2010 and 2009, consisted of the following:

	2010	2009
Regulatory deferred charges:		
Deferred conservation costs—net	\$ 178,436,794	\$ 162,136,725
Endangered Species Act—net	<u>2,626,689</u>	<u>2,418,434</u>
	<u>181,063,483</u>	<u>164,555,159</u>
Other deferred charges and assets—net:		
Suburban infrastructure long-term receivables	25,851,106	26,176,002
Puget Sound Energy interconnection and substation	992,859	1,092,145
Studies, surveys, and investigations	515,263	406,545
Real estate and conservation loans receivable	16,145	30,756
Unamortized debt expense	9,767,638	8,217,401
General work-in-process to be billed	1,073,782	1,908,467
Interfund note receivable—long-term portion	1,452,226	-
Other	<u>752,950</u>	<u>214,197</u>
	<u>40,421,969</u>	<u>38,045,513</u>
Total Other Assets	<u>\$ 221,485,452</u>	<u>\$ 202,600,672</u>

12. DEFERRED CREDITS

Seattle City Council passed resolutions authorizing deferral of certain credits in accordance with ASC 980-10-05, *Effect of Regulatory Accounting*. Retail electric revenues from the Rate Stabilization Account surcharge were deferred in 2010 (see Note 3). Payments received from Bonneville for qualified conservation augmentation programs are amortized to revenues over the life of the 10-year contract that expires September 30, 2011. Bonneville Slice contract true-up credits are deferred in the year invoiced and recognized as revenue in the following year (see Note 10). Seattle City Council affirmed the Department's practice of deferring recognition of the effects of reporting the fair value of exchange contracts for rate making purposes and maintaining regulatory accounts to defer the accounting impact of these accounting adjustments, in Resolution No. 30942 adopted January 16, 2007 (see Note 10).

The remaining components of deferred credits are amortized to revenues as earned, except unrealized or deferred gains from fair valuations that expire at contract completion and deposits that are returned to customers.

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Regulatory deferred credits and other credits at December 31, 2010 and 2009, consisted of the following:

	2010	2009
Regulatory deferred credits:		
Deferred revenue—rate stabilization account	\$ 54,265,627	\$ -
Bonneville conservation augmentation	4,699,529	10,433,379
Deferred Bonneville Slice true-up credit	7,101,497	1,979,551
Exchange energy: regulatory deferred gain	288,801	1,087,450
	<u>66,355,454</u>	<u>13,500,380</u>
Other credits:		
Deferred capital fees	5,009,039	7,392,604
Deferred revenues in lieu of rent for in-kind capital	510,004	523,062
Customer deposits—sundry sales	2,399,679	2,413,789
Deferred operations and maintenance revenues	1,058,803	821,759
Deferred exchange premiums	1,089,789	3,263,222
Deferred service revenue exchange fair value	510,419	626,052
Deferred revenues—other	882,373	185,496
	<u>11,460,106</u>	<u>15,225,984</u>
Total	<u>\$ 77,815,560</u>	<u>\$ 28,726,364</u>

13. PROVISION FOR INJURIES AND DAMAGES

The Department establishes liabilities for claims based on estimates of the ultimate projected cost of claims. Environmental related expenses are discussed in Note 14. 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 economic and social factors. For 2010 and 2009, liabilities for lawsuits, claims, and workers' compensation were discounted over a period of 16 to 19 years at the City's average annual rate of return on investments, which was 1.027% and 1.650%, respectively.

To address the risk for certain losses arising from personal and property damage claims by third parties and for job-related illnesses and injuries to employees, the Department as part of the City of Seattle, has been self-insured for most of its general liability risks prior to January 1, 1999, for workers' compensation since 1972, and for employees' health care benefits starting in 2000. Through 2006, the City had general liability insurance coverage for losses over a \$5.0 million per occurrence self-insured retention, with a \$25.0 million limit per occurrence and in the aggregate. In June 2007, the limit was increased to \$30.0 million over a \$5.0 million self-insured retention. In June 2009, the City's general liability self-insured risk retention was increased from \$5.0 million to \$6.5 million.

The City also purchased an all risk comprehensive property insurance policy that provides \$500.0 million in limits subject to various deductible levels depending on the type of asset and value of the building. This includes \$100.0 million in earthquake and flood limits. Hydroelectric projects are not

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covered. The City also purchased insurance for excess worker’s compensation, fiduciary and crime liability, inland marine transportation, volunteers, and an assortment of commercial general liability, medical, accidental death and dismemberment, and miscellaneous policies. Bonds are purchased for public officials, public notaries, pension exposures, and specific projects and activities as necessary.

The changes in the provision for injuries and damages at December 31, 2010 and 2009, are as follows:

	2010	2009
Beginning unpaid claims liability	\$ 11,590,611	\$ 12,709,494
Payments	(1,823,302)	(5,184,896)
Incurred claims	<u>2,312,149</u>	<u>4,066,013</u>
Ending unpaid claims liability	<u>\$ 12,079,458</u>	<u>\$ 11,590,611</u>

The provision for injuries and damages included in current and noncurrent liabilities at December 31, 2010 and 2009 is as follows:

	2010	2009
Noncurrent liabilities	\$ 8,440,749	\$ 7,851,929
Accounts payable and other current liabilities	<u>3,638,709</u>	<u>3,738,682</u>
Total liability	<u>\$ 12,079,458</u>	<u>\$ 11,590,611</u>

14. ENVIRONMENTAL LIABILITIES

Environmental liabilities were \$35.3 million and \$29.1 million, at December 31, 2010, and 2009, respectively.

The following is a brief description of the significant Superfund sites:

The Harbor Island Superfund Site—In 1983, the U.S. Environmental Protection Agency (EPA) designated this site as a federal Superfund site. The Department and other entities are sharing costs of investigating contamination in the East Waterway alongside Harbor Island. The Department’s involvement stems from its sale of transformers to a company on Harbor Island. The City of Seattle is one of four parties who are conducting a remedial investigation and feasibility study that will delineate cleanup actions. The Department’s ultimate liability is indeterminate.

The Lower Duwamish Waterway Superfund Site—In 2001, the EPA designated this site as a federal Superfund site for contaminated sediments. The Department’s involvement is attributable to its land ownership or use of property along the river. The City of Seattle is one of four parties who signed an Administrative Order on Consent with the EPA and Washington State Department of Ecology to conduct a remedial investigation/feasibility study to prepare a site remedy. The City filed a suit in King County Superior Court against The Boeing Company to require Boeing to pay its fair share of costs. The case settled in 2010 with Boeing paying part of the City’s past costs and agreeing to pay a specific percentage of future costs related to the cleanup.

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North Boeing Field/Georgetown Steam Plant—The City, King County, and Boeing have signed an Administrative Order by the Washington State Department of Ecology (Ecology) requiring them to pay for Ecology’s investigation and possible removal of contamination in an area that encompasses North Boeing Field, the Department’s Georgetown Steam Plant, and the King County Airport. The three potentially liable parties have agreed to share costs equally on an interim basis for the current investigative phase. During or after the investigative phase, contaminated areas will be cleaned up. With respect to North Boeing Field, Boeing agreed to pay a specific percentage of Ecology’s costs and all costs for work on the property it uses. With respect to the Georgetown Steam Plant site, the Department has agreed to pay all of the costs of the cleanup.

The Department has included in its estimated liability those portions of the environmental remediation work that are currently deemed to be reasonably estimable. Cost estimates were developed using the expected cash flow technique in accordance with GASB 49. Estimated outlays were based on current cost and no adjustments were made for discounting or inflation. Cost scenarios were developed that defined a particular solution for a given site. Scenarios considered relevant potential requirements and alternatives for remediation of a site. Costs were calculated on a weighted average that was based on the probabilities of each scenario being selected and reflected cost-sharing agreements in effect. In addition, certain estimates were derived from independent engineers and consultants. The estimates were made with the latest information available; as new information becomes available, estimates may vary significantly due to price increases or reductions, technology, or applicable laws or regulations.

The Department is aggressively pursuing other third parties that may have contributed to the contamination of superfund sites for appropriate cost sharing. The Department’s estimate for not yet realized recoveries from other parties for their share of remediation work that partially offset the Department’s estimated environmental liabilities were \$1.7 million and \$2.4 million at December 31, 2010 and 2009, respectively.

The changes in the provision for environmental liabilities at December 31, 2010 and 2009 are as follows:

	2010	2009
Beginning environmental liability, net of recoveries	\$29,076,469	\$ 18,656,955
Payments	(3,742,179)	(5,143,355)
Incurred environmental liability	<u>10,012,680</u>	<u>15,562,869</u>
Ending environmental liability, net of recoveries	<u>\$ 35,346,970</u>	<u>\$ 29,076,469</u>

The provision for environmental liabilities included in current and noncurrent liabilities at December 31, 2010 and 2009, is as follows:

	2010	2009
Noncurrent liabilities	\$28,059,436	\$24,919,259
Accounts payable and other current liabilities	<u>7,287,534</u>	<u>4,157,210</u>
Ending liability	<u>\$ 35,346,970</u>	<u>\$ 29,076,469</u>

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15. FAIR VALUE MEASUREMENTS

ASC 820, *Fair Value Measurements and Disclosures*, establishes a hierarchy for inputs used in measuring fair value of certain assets and liabilities that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the Department. Unobservable inputs are inputs that reflect the Department's assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Department has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for the asset or liability. Valuation adjustments such as for nonperformance risk or inactive markets could cause an instrument to be classified as Level 3 that would otherwise be classified as Level 1 or Level 2.

Following are the valuation techniques provided by ASC 820: The "market approach" uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. The "income approach" uses valuation techniques to convert expected future amounts to a single present value. The "cost approach" is based on the amount that would be required to replace the service capacity of an asset. The Department uses the market approach for the valuation of settled exchanges and other nonmonetary transactions, and a combination of the market and income approaches for the valuation of the undelivered forward portion of exchanges and other nonmonetary transactions.

The Department obtained the lowest level of input that was significant to the fair value measurement in its entirety from subscription services or other independent parties under contract and considers its inputs to be observable either directly or indirectly and used applicable valuation approaches. The observable inputs for the settled portion of the exchange contracts are Dow Jones price indices. The observable inputs for the undelivered forward portion of exchanges and other non-monetary transactions are Platts forward curves and present value factors based on the interest rate for Treasury constant maturities, bond-equivalent yields.

The forward portions of the exchange contract transactions are valued as follows using Platts forward curves for the time and place corresponding to the transactions, and in some cases the average daily prices from the Dow Jones U.S. Daily Electricity Price Indices. These prices are applied to the number of megawatt hours to be transacted. The result is then discounted for present value based on the interest rate for Treasury constant maturities, bond-equivalent yields by the future month of the transactions.

The following fair value hierarchy table presents information about the Department's assets and liabilities reported at fair value on a recurring basis or disclosed at fair value as of December 31, 2010 and 2009:

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2010	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at 12/31/10
ASSETS				
Current assets:				
Exchange energy receivable	\$ -	\$ 2,794,440	\$ -	\$ 2,794,440
Total at fair value	\$ -	\$ 2,794,440	\$ -	\$ 2,794,440
LIABILITIES				
Deferred credits:				
Exchange energy deferred revenue	\$ -	\$ 799,220	\$ -	\$ 799,220
Total at fair value	\$ -	\$ 799,220	\$ -	\$ 799,220

2009	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at 12/31/09
ASSETS				
Current assets:				
Exchange energy receivable	\$ -	\$ 3,777,444	\$ -	\$ 3,777,444
Total at fair value	\$ -	\$ 3,777,444	\$ -	\$ 3,777,444
LIABILITIES				
Deferred credits:				
Exchange energy deferred revenue	\$ -	\$ 1,713,502	\$ -	\$ 1,713,502
Total at fair value	\$ -	\$ 1,713,502	\$ -	\$ 1,713,502

16. COMMITMENTS AND CONTINGENCIES

Operating Leases—While the Department owns several buildings including those at the Skagit and Boundary hydroelectric projects, service centers, and the System Control Center, the Department leases some administrative office space from the City. Such lease payments to the City are made through a central cost allocation process, similar to all other payments for tenancy of City property. These payments are not included in the operating leases table below. The Department also leases certain office equipment and smaller facilities for various purposes through long-term operating lease agreements. Expenses under all leases totaled \$1.1 million and \$0.6 million in 2010 and 2009, respectively.

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Minimum payments under the operating leases are:

Year Ending December 31	Minimum Payments
2011	\$ 1,115,687
2012	1,136,063
2013	1,145,353
2014	1,044,826
2015	1,072,542
Thereafter	<u>1,754,192</u>
Total	<u>\$ 7,268,663</u>

2011 Capital Program—The estimated financial requirement for the Department’s 2011 program for capital improvement, conservation, and deferred operations and maintenance including required expenditures on assets owned by others is \$280.5 million. The Department has substantial contractual commitments relating thereto.

Federal Energy Regulatory Commission Fees—Estimated Federal land use and administrative fees related to hydroelectric licenses total \$229.3 million through 2061; these estimates are subject to change. The estimated portion of fees attributed to the Skagit and Tolt licenses are excluded after 2025, at which time their current FERC licenses expire. The estimated portion of Boundary fees is included through 2061, although the new license has not yet been approved by FERC. Boundary FERC application process and related issues are discussed below.

Application Process for New Boundary License—The Department’s FERC license for the Boundary Project expires on September 30, 2011. The Department filed an application for a new license with FERC on September 29, 2009, and a proposed settlement agreement and revised exhibit addenda with FERC on March 28, 2010. The proposed settlement and revised exhibit addenda seek to preserve the Department’s operational flexibility at Boundary Dam while providing for natural resource protection, mitigation and enhancement measures. While the Department was preparing its initial license application, the Department was also negotiating the proposed settlement with external parties such as owners of other hydroelectric projects, Indian tribes, conservation groups and other government agencies. When the Department and the external parties agreed to the settlement, the Department requested FERC to allow the settlement agreement and revised exhibit addenda to replace the initial September 2009 application as the Department’s application; FERC agreed to this request. Implementation of the settlement will depend upon FERC’s approval of the settlement terms as part of the new license. If the new FERC license is significantly different than the settlement terms, the settlement may be terminated. If FERC does not issue a new license before the expiration of the current license, FERC will issue a license annually that continues the conditions of the current license. If necessary, FERC will issue annual licenses until it issues the new long-term license.

Total application process costs are estimated at \$40.1 million, of which \$38.5 million had been expended and deferred as of December 31, 2010. A new license will require additional mitigation efforts for endangered species, including water quality standards. The cost projections for such mitigation, included in the Department’s license application, are estimated to be \$415.8 million over the 50-year life of the license.

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Skagit and South Fork Tolt Licensing Mitigation and Compliance—In 1995, the FERC issued a license for operation of the Skagit hydroelectric facilities through April 30, 2025. On July 20, 1989, the FERC license for operation of the South Fork Tolt hydroelectric facilities through July 19, 2029, became effective. As a condition for both of these licenses, the Department has taken and will continue to take required mitigating and compliance measures.

Total Skagit license mitigation costs from the effective date until expiration of the federal operating license were estimated at December 31, 2010, to be \$116.1 million, of which \$97.5 million had been expended. Total South Fork Tolt license mitigation costs were estimated at \$1.3 million, of which \$0.8 million were expended through 2010. In addition to the costs listed for South Fork Tolt mitigation, the license and associated settlement agreements required certain other actions related to wildlife studies and wetland mitigation for which no set dollar amount was listed. Requirements for these actions have been met, and no further expenditures need to be incurred for these items.

Capital improvement, other deferred costs, and operations and maintenance costs are included in the estimates related to the settlement agreements for both licenses. Amounts estimated are adjusted to 2010 dollars. Department labor and other overhead costs associated with the activities required by the settlement agreements for the licenses are not included in the estimates.

Hydroelectric projects must satisfy the requirements of the Endangered Species Act (ESA) and the Clean Water Act in order to obtain a FERC license. ESA and related issues are discussed below.

Endangered Species—Several 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 threatened or endangered. Although the species were listed after FERC licenses were issued for all of the Department's hydroelectric projects, the ESA listings still affect operations of City Light's Boundary, Skagit, Tolt, and Cedar Falls hydroelectric projects.

Federal Regulations in response to the listing of species affect flow in the entire Columbia River system. As a result of these regulations, the Department's power generation at its Boundary Project is reduced in the fall and winter when the region experiences its highest sustained energy demand. The Boundary Project's firm capability is also reduced.

The Department, with the support of City Council, elected to take a proactive approach to address issues identified within the ESA. The Department is carrying out an ESA Early Action program in cooperation with agencies, tribes, local governments, and watershed groups for bull trout, Chinook salmon, and steelhead in the South Fork Tolt and Skagit Watersheds. The ESA Early Action program is authorized by City Council, but is separate from any current FERC license requirements. The program includes habitat acquisition, management and restoration. The ESA Early Action has been successful in protecting listed species. Total costs for the Department's share of the Early Action program from inception in 1999 through December 31, 2010 are estimated to be approximately \$5.0 million, and approximately \$0.8 million has been allocated for the program in the 2011 budget.

Project Impact Payments—Effective August 2010, the Department committed to pay a total of \$19.0 million over 10 years ending in 2019 to Pend Oreille County for impacts on county governments from the operations of the Department's hydroelectric projects. This updated agreement superseded an expired agreement with Pend Oreille County. Effective February 2009, the Department renewed its contract with Whatcom County committing to pay a total of \$15.8 million over 15 years ending in 2023.

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The payments compensate the counties, and certain school districts and towns located in these counties, for loss of revenues and additional financial burdens associated with the projects. The Boundary Project, located on the Pend Oreille River, affects Pend Oreille County, and Skagit River hydroelectric projects affect Whatcom County. The combined impact compensation and retroactive payments totaled \$1.4 million and \$1.4 million to Pend Oreille County, and \$0.9 million and \$0.9 million to Whatcom County in 2010 and 2009, respectively.

Energy Crisis Refund Litigation—The City is involved in various legal proceedings relating to the enormous spikes in energy prices in California and the rest of the West Coast in 2000 and 2001.

- ***California Refund Case, Appeals and Related Litigation***—In the proceeding before the Federal Energy Regulatory Commission (FERC), various public and private California entities (the California Parties) sought refunds in markets that had been created by the State of California. The Department had sold energy in one of these markets. The City faced potential contractual liability of approximately \$6.5 million, with any judgment subject to interest dating back to 2001. In 2001, FERC ordered refunds to the extent that actual energy prices exceeded rates that FERC determined to be “just and reasonable.” On appeal, the Court of Appeals for the Ninth Circuit held that FERC has no authority to order governmental entities such as the City to pay refunds. Following this ruling, the three major California investor-owned utilities sought refunds from the Department and other governmental entities in federal district court on a breach of contract theory. In March 2007, the federal court dismissed all claims. In April 2007, the three major California investor-owned utilities refiled their claims in state court. In December 2007, the trial court denied a request to dismiss the case. In February 2011, the City agreed to a proposed settlement, pending final approval by the trial court and FERC. Under the proposed settlement, the City would resolve this matter for \$9.0 million, none of which would need to be immediately paid by the Department. If the settlement is approved by the trial court and FERC, the Department would assign its current accounts receivable from the California Independent Systems Operator to the California Parties, which is currently valued at approximately \$1.4 million. The balance of over \$7.6 million would be contingent upon the Department recovering monies in the Pacific Northwest Refund Case, discussed below.
- ***Pacific Northwest Refund Case and Appeal***—In the proceeding before FERC, various buyers of energy, including the City, sought refunds on energy transactions in the Pacific Northwest between May 2000 and June 2001. The Department’s claims currently are in excess of \$100.0 million. In 2003, FERC declined to grant refunds, on the grounds that there was no equitable way to do so. The City and other parties appealed to the Ninth Circuit. In August 2007, the Ninth Circuit held that FERC had abused its discretion in denying all refund relief in the Pacific Northwest, and remanded the case to FERC for further proceedings. In December 2007, various buyers of energy filed petitions for rehearing in the Ninth Circuit. On April 9, 2009, the Ninth Circuit denied those petitions for rehearing. On April 16, 2009, the Ninth Circuit issued the mandate remanding the case to FERC. On September 4, 2009, the sellers filed a Petition for a Writ of Certiorari in the United States Supreme Court. That petition was denied on January 11, 2010. FERC has yet to take any action on remand.

Other Contingencies—In addition to those noted above, in the normal course of business, the Department has various other legal claims and contingent matters outstanding. The Department believes

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that any ultimate liability arising from these actions will not have a material adverse impact on the Department's financial position, operations, or cash flows.

17. SUBSEQUENT EVENTS

Fair Value of Pooled and Dedicated Investments—The Federal Open Market Committee (FOMC) of the Federal Reserve Board last met on March 15, 2011. The FOMC left its target range for Federal Funds unchanged at 0% to 0.25%. The range has not changed since it was first established December 16, 2008, during the financial crisis. Interest rates have risen slightly along the yield curve since the end of 2010. However, changes in the fair value of the Department's dedicated investments over the first quarter 2011 has been insignificant due to the short-term duration of the investments and mitigated by the investments being held to maturity.

Fair value of the City's pooled investments fluctuates with changes in interest rates and is most sensitive to changes in the 1-2 year area of the yield curve. Since interest rates have risen slightly during the first quarter, fair value of some of the City's pooled investments have declined. Many of the pooled investments held at the end of 2010 were initially purchased when interest rates were higher, so these investments have increased in market value offsetting the decline in fair value of more recently purchased pooled investments held at December 31, 2010. Therefore, the net change in fair value of the City's pooled investments, and thus the Department's share in the pooled investments, was generally insignificant during the first quarter of 2011.

Rate Stabilization Account and Retail Electric Rates Adjustment—On January 1, 2011, the Department transferred \$21.0 million from the operating cash account to the RSA. The balance in the RSA reached the initial funding level of \$100.0 million specified in Ordinance No. 123260. Accordingly, the 4.5% rate surcharge implemented in May 2010 was terminated.

Also on January 1, 2011, the Department implemented a 4.3% across the board electric retail rate increase in accordance with Ordinance No. 123479. Rates will also increase 3.2% at the beginning of 2012. The rate increases were approved by the Seattle City Council to meet financial policies, protect the Department's financial stability, and fund improvements to the aging infrastructure.

2011 Bond Issue—On February 8, 2011, the Department issued \$296.3 million of Municipal Light and Power Improvement and Refunding Revenue Bonds, Series 2011A, and \$10.0 million of Municipal Light and Power Improvement Revenue Bonds, Series 2011B. The Series 2011A bonds were issued at a premium while the Series 2011B bonds were issued at a slight discount. \$96.3 million of the Series 2011A bonds along with the premium were used to advance refund \$101.3 million of prior lien bonds, Series 2001. Economic savings on the advance refunding totaled \$9.8 million at net present value. The balance of the Series 2011A bonds will be used to finance certain capital improvements and conservation programs.

The Series 2011A bonds are tax exempt and the Series 2011B bonds are taxable Clean Renewable Energy Bonds (CREBS) that will be used for capacity and efficiency improvements at the Boundary Hydroelectric Project. True interest cost for the Series 2011A bonds was 4.54% and 1.96% for the Series 2011B bonds, respectively. Arbitrage yield was 4.43% and 1.94% for the Series 2011A and Series 2011B bonds, respectively.

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REQUIRED SUPPLEMENTARY INFORMATION (UNAUDITED)

Schedules of Funding Progress

SCERS. The schedule of funding progress for SCERS is presented below for the most recent actuarial valuation and the two preceding valuations for which the Department has available data (dollar amounts in millions):

Actuarial Valuation Date January 1,	Actuarial Value of Assets (a)	Actuarial Accrued Liabilities (AAL) ⁽¹⁾ (b)	Unfunded AAL (UAAL) ⁽²⁾ (b-a)	Funding Ratio (a/b)	Covered Payroll ⁽³⁾ (c)	UAAL (or Excess) as a Percentage of Covered Payroll ((b-a)/c)
2006	\$ 1,791.8	\$ 2,017.5	\$ 225.8	88.8 %	\$ 447.0	50.5 %
2008	2,119.4	2,294.6	175.2	92.4	501.9	34.9
2010	1,645.3	2,653.8	1,008.5	62.0	580.9	173.6

- (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 were made in the year preceding the valuation date.

OPEB. The schedule of funding progress for the other post-employment benefit healthcare plans is presented below for the most recent actuarial valuation and the two preceding valuations for which the Department has available data (dollar amounts in millions):

Actuarial Valuation Date January 1,	Actuarial Value of Assets (a)	Actuarial Accrued Liabilities (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funding Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2006	\$ -	\$ 84.3	\$ 84.3	- %	\$ 734.5	11.5 %
2008	-	78.8	78.8	-	837.1	9.4
2010	-	93.5	93.5	-	869.1	10.8