

New Issue
Book-Entry Only

Moody's Rating: Aaa (Underlying Aa3)
Standard & Poor's Rating: AAA (Underlying A)
(See "Other Bond Information—Bond Insurance" and "—Ratings.")

In the opinion of Bond Counsel, under existing federal law and assuming compliance with applicable requirements of the Internal Revenue Code of 1986, as amended, that must be satisfied subsequent to the issue date of the Bonds, interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals. However, while interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by corporations is taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by certain S corporations may be subject to tax, and interest on the Bonds received by foreign corporations with United States branches may be subject to a foreign branch profits tax. Receipt of interest on the Bonds may have other federal tax consequences for certain taxpayers. See "Tax Exemption" and "Certain Other Federal Tax Consequences" under "Legal and Tax Information" herein.

\$87,735,000

**THE CITY OF SEATTLE, WASHINGTON
MUNICIPAL LIGHT AND POWER REFUNDING REVENUE BONDS, 2002**

Dated: December 1, 2002

Due: December 1, as shown on inside cover

The Bonds will be issued as fully registered bonds under a book-entry only system, registered in the name of Cede and Co. as registered owner and nominee for DTC. DTC will act as initial securities depository for the Bonds. Individual purchases of the Bonds will be made in book-entry form, in the denomination of \$5,000 or any integral multiple thereof. Purchasers will not receive certificates representing their interests in the Bonds. Interest on the Bonds will be paid semiannually on each June 1 and December 1, beginning June 1, 2003. The principal of and interest on the Bonds are payable by the Bond Registrar (currently, The Bank of New York in New York, New York) to DTC, which in turn is obligated to remit such payments to its participants for subsequent disbursement to beneficial owners of the Bonds, as described in "Description of the Bonds—Book-Entry Transfer System" and in Appendix E.

MATURITY SCHEDULE LOCATED ON INSIDE COVER

The Bonds are being issued to refund all of the City's outstanding Municipal Light and Power Revenue Bonds, Series 1992B, and a portion of the City's outstanding Municipal Light and Power Revenue Bonds, 1993, and to pay the costs of issuance of the Bonds. See "Refunding Plan."

The Bonds are subject to optional redemption prior to maturity as described herein. See "Description of the Bonds—Redemption of the Bonds."

The Bonds are special limited obligations of the City payable from and secured solely by the Gross Revenues of the Light System and by money in the Parity Bond Fund and the Reserve Fund. The Bonds will be issued on a parity with \$1,327,971,000 of Outstanding Parity Bonds, of which \$86,560,000 will be refunded by the Bonds, and any Future Parity Bonds. The Gross Revenues are pledged to make the required payments into the Parity Bond Fund and the Reserve Fund; this pledge is superior to all other charges upon the Gross Revenues except for reasonable charges for maintenance and operation of the Light System. Maintenance and operation charges include the unconditional obligation of the City to make payments under certain power purchase contracts, as more fully described in "Power Resources—Purchased Power Arrangements." See "Security for the Bonds."

The Bonds do not constitute general obligations of the City, the State of Washington or any political subdivision of the State, or a charge upon any general fund or upon any money or other property of the City, the State or any political subdivision of the State not specifically pledged thereto by the Bond Ordinance. Neither the full faith and credit nor the taxing power of the City, nor any revenues of the City derived from sources other than the Light System, are pledged to the payment of the Bonds.

The scheduled payment of principal of and interest on the Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Bonds by FINANCIAL SECURITY ASSURANCE INC. See "Other Bond Information—Municipal Bond Insurance."



The Bonds are offered for delivery when, as and if issued, subject to the approving legal opinion of Foster Pepper & Shefelman PLLC, Seattle, Washington, Bond Counsel, and certain other conditions. The form of Bond Counsel's opinion is attached hereto as Appendix B. It is expected that the Bonds will be available for delivery at the facilities of DTC in New York, New York, or to the Bond Registrar on behalf of DTC by Fast Automated Securities Transfer on or about December 4, 2002.

This cover page contains certain information for quick reference only. It is not a summary of this issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

Dated: November 20, 2002

\$87,735,000

**THE CITY OF SEATTLE, WASHINGTON
MUNICIPAL LIGHT AND POWER REFUNDING REVENUE BONDS, 2002**

Due December 1	Amounts	Interest Rates	Yields	CUSIP Numbers
2003	\$ 2,460,000	3.000%	1.45%	8126426J0
2004	5,080,000	4.000	1.75	8126426K7
2005	12,450,000	4.000	2.18	8126426L5
2006	9,270,000	4.000	2.53	8126426M3
2007	9,255,000	4.000	2.84	8126426N1
2008	10,230,000	4.500	3.16	8126426P6
2009	10,725,000	4.375	3.38	8126426Q4
2010	10,675,000	4.500	3.63	8126426R2
2011	4,140,000	4.000	3.80	8126426S0
2012	4,310,000	4.000	3.90	8126426T8
2013	4,480,000	4.000	4.04	8126426U5
2014	4,660,000	4.125	4.20	8126426V3

(Plus accrued interest from the dated date.)

THE CITY OF SEATTLE

CITY OFFICIALS AND CONSULTANTS

MAYOR AND CITY COUNCIL

Greg Nickels	Mayor
Peter Steinbrueck	President, City Council
Jim Compton	Council Member
Richard Conlin	Council Member
Jan Drago	Council Member
Nick Licata	Council Member
Richard McIver	Council Member
Judy Nicastro	Council Member
Margaret Pageler	Council Member
Heidi Wills	Council Member

SEATTLE CITY LIGHT DEPARTMENT

Gary Zarker	Superintendent
Jesse A. Krail, P.E.	Deputy Superintendent, Distribution
Dana L. Backiel	Deputy Superintendent, Generation
James P. Ritch	Deputy Superintendent, Finance and Administration
Joan Walters	Deputy Superintendent, Customer Services
Mike Sinowitz	Deputy Superintendent, Power Management

CITY ADMINISTRATION

Dwight D. Dively	Director of Finance
Thomas A. Carr	City Attorney

BOND COUNSEL

Foster Pepper & Shefelman PLLC
Seattle, Washington

FINANCIAL ADVISOR

Seattle-Northwest Securities Corporation
Seattle, Washington

No dealer, broker, salesperson, or other person has been authorized by the City to give any information or to make any representations, other than as contained in this Official Statement, and if given or made, such other information or representations must not be relied upon as having been authorized by the City. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy the Bonds, nor shall there be any sale of the Bonds by any person in any jurisdiction in which it is unlawful for such persons to make such offer, solicitation or sale.

The information set forth herein has been furnished by the City, DTC and certain other sources that are believed to be reliable. The information and expressions of opinion contained herein are subject to change without notice. Any statements made in this Official Statement involving matters of opinion or estimates, whether or not so expressly stated, are set forth as such and not as representations of fact or representations that the estimates will be realized.

Neither the Department's independent auditors, nor any other independent accountants, have compiled, examined, or performed any procedures with respect to the projected financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability, and assume no responsibility for, and disclaim any association with, the prospective financial information.

Other than with respect to information concerning Financial Security Assurance Inc. ("Financial Security") contained under "Bond Insurance" and in Appendix F—Municipal Bond Insurance Policy Specimen herein, none of the information in this Official Statement has been supplied or verified by Financial Security and Financial Security makes no representation or warranty, express or implied, as to (i) the accuracy or completeness of such information; (ii) the validity of the Bonds; or (iii) the tax exempt status of the interest on the Bonds. Neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the City since the date hereof.

This Official Statement is not to be construed as a contract with the purchasers of the Bonds.

The Bonds have not been registered under the Securities Act of 1933, as amended, in reliance upon a specific exemption contained in such act, nor have they been registered under the securities laws of any state.

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OFFICIAL STATEMENT

\$87,735,000

THE CITY OF SEATTLE, WASHINGTON MUNICIPAL LIGHT AND POWER REFUNDING REVENUE BONDS, 2002

INTRODUCTION

The purpose of this Official Statement, which includes the cover page and the appendices, is to set forth certain information concerning The City of Seattle (the "City"), its City Light Department (the "Department" or "City Light"), municipal light and power plant and system (the "Light System"), and Municipal Light and Power Refunding Revenue Bonds, 2002 (the "Bonds"), in connection with the offering and sale of the Bonds. The Bonds are to be issued in accordance with Ordinance 120931 passed on September 23, 2002 (the "Bond Ordinance"), and Resolution 30549, adopted on November 20, 2002 (the "Bond Resolution").

The Bond Ordinance is attached hereto as Appendix A. Appendix B contains the form of legal opinion of Foster Pepper & Shefelman PLLC ("Bond Counsel"). Appendix C contains the Department's audited 2001 financial statements. Appendix D provides demographic and economic information about the City. Appendix E contains information on the book-entry transfer system supplied by DTC and the City. Appendix F is a municipal bond insurance policy specimen. Capitalized terms that are not defined herein have the meanings set forth in the Bond Ordinance and Bond Resolution.

The Bonds are being issued on a parity of lien with the City's first lien Municipal Light and Power Revenue Bonds, which include 12 series of bonds issued since 1992 (the "Outstanding Parity Bonds"). As of November 13, 2002, the City had \$1,327,971,000 principal amount of Outstanding Parity Bonds, of which \$86,560,000 will be refunded by the Bonds. See "Refunding Plan."

IN THE PREPARATION OF THE PROJECTIONS IN THIS OFFICIAL STATEMENT, THE CITY HAS MADE CERTAIN ASSUMPTIONS WITH RESPECT TO CONDITIONS THAT MAY OCCUR IN THE FUTURE. WHILE THE CITY BELIEVES THESE ASSUMPTIONS ARE REASONABLE FOR THE PURPOSE OF THE PROJECTIONS, THEY DEPEND UPON FUTURE EVENTS, AND ACTUAL CONDITIONS MAY DIFFER FROM THOSE ASSUMED. THE CITY DOES NOT REPRESENT OR GUARANTEE THAT ACTUAL RESULTS WILL REPLICATE THE ESTIMATES IN THE VARIOUS TABLES SET FORTH IN THIS OFFICIAL STATEMENT. THE ELECTRIC INDUSTRY HAS UNDERGONE SIGNIFICANT CHANGES, AS DISCUSSED UNDER "RECENT DEVELOPMENTS IN THE ELECTRIC UTILITY INDUSTRY" AND "THE WESTERN POWER CRISIS" AND ELSEWHERE IN THIS OFFICIAL STATEMENT. POTENTIAL PURCHASERS OF THE BONDS SHOULD NOT RELY ON THE PROJECTIONS IN THIS OFFICIAL STATEMENT AS STATEMENTS OF FACT. SUCH PROJECTIONS ARE SUBJECT TO CHANGE, AND WILL CHANGE, FROM TIME TO TIME. THE CITY HAS NOT COMMITTED ITSELF TO PROVIDE INVESTORS WITH UPDATED FORECASTS OR PROJECTIONS.

Recent Developments Affecting the Department

In 2000 and 2001, the Department's financial results were adversely impacted by the combination of poor hydro conditions and an extraordinary confluence of events which caused wholesale power prices in the Western United States to increase to unprecedented levels. As a result of the high prices and the Department's need to purchase large quantities of power to offset poor water conditions at its own facilities, the Department incurred \$524.4 million in costs for wholesale market purchases in 2001. This was more than ten times the amount assumed in the financial forecasts on which its retail rates were based. The City's response to this set of circumstances included the following actions:

- (i) four retail rate increases totaling 58 percent in 2001;
- (ii) acquisition of additional resources through multi-year contracts to reduce the Department's dependence on the wholesale market for power supply, even under critical water conditions;

- (iii) reduction of retail customer consumption through expansion of the Department's conservation programs and a public information campaign; and
- (iv) reduction of debt service costs through bond refinancings in 2001 and 2002.

To finance its cash flow requirements, the Department incurred \$282.2 million in short-term debt in 2001. The City Council by resolution has required that rates remain at their current levels until all of the short-term obligations have been repaid and the Department has accrued an operating cash balance of \$30 million. In the same resolution, the Council adopted new rate-setting policies for the Department. The new policies require that, once the short-term obligations have been repaid, rates will be set at levels that give greater recognition to the higher risks that the Department faces in the current utility environment.

In 2002, with retail rates at the levels to which they were raised in 2001 and with normal water conditions, the Department's financial results have improved. Through September 30, 2002, the Department has accrued net income of \$30.9 million, compared with a loss of \$363.3 million in the same period of 2001. The Department expects to repay all of its short-term obligations by the first quarter of 2004 and to set rates under the new rate-setting policies effective January 1, 2005.

For additional information, see "Historical and Projected Operating Results," "The Western Power Crisis," "The City's Response to the Western Power Crisis," and "Power Resources."

REFUNDING PLAN

The Bonds are being issued to refund all of the City's outstanding Municipal Light and Power Revenue Bonds, Series 1992B (the "Refunded 1992B Bonds") and a portion of the City's outstanding Municipal Light and Power Revenue Bonds, Series 1993 (the "Refunded 1993 Bonds" and together with the Refunded 1992B Bonds, the "Refunded Bonds") and to pay the costs of issuance of the Bonds.

Refunding Plan

The proceeds from the sale of the Bonds are expected to be used to refund the following Outstanding Parity Bonds of the City for the purpose of realizing debt service savings. The Refunded 1992B Bonds are currently callable and will be called 30 days after closing of the Bonds. The Refunded 1993 Bonds will be called on November 1, 2003.

REFUNDED BONDS

Series	Maturity	Amount (\$)	Interest Rate (%)	Call Price
Series 1992B Bonds	02/01/2003	335,000	5.400	102
Serials	08/01/2003	4,345,000	5.400	102
	02/01/2004	310,000	5.500	102
	08/01/2004	4,320,000	5.500	102
	02/01/2005	285,000	5.625	102
	08/01/2005	4,290,000	5.625	102
	02/01/2006	255,000	5.750	102
	08/01/2006	5,265,000	5.750	102
	02/01/2007	220,000	5.750	102
	08/01/2007	5,230,000	5.750	102
	08/01/2008	6,370,000	5.750	102
	08/01/2009	6,765,000	5.750	102
	08/01/2010	<u>6,635,000</u>	5.750	102
Subtotal		44,625,000		
Series 1993 Bonds	11/01/2005	8,115,000 *	5.100	102
Serials	11/01/2006	3,020,000	5.200	102
	11/01/2007	3,180,000	5.300	102
	11/01/2008	3,345,000	5.400	102
Term	11/01/2010	7,245,000 *	5.450	102
Term	11/01/2013	12,425,000	5.500	102
Term	11/01/2018	<u>4,605,000 *</u>	5.375	101
Subtotal		41,935,000		
Total		86,560,000		

* Partial maturities.

From the proceeds of the Bonds and other available money, the City will purchase certain United States Treasury Certificates of Indebtedness, Notes and Bonds—State and Local Government Series and other direct, noncallable obligations of the United States (the “Acquired Obligations”). These Acquired Obligations will be deposited in the custody of U.S. Bank, N.A. or a duly appointed successor (the “Refunding Trustee”). The Acquired Obligations, interest earned thereon and any necessary beginning cash balance will be used to provide for the payment of the Refunded Bonds, pursuant to a refunding trust agreement to be executed by the City and the Refunding Trustee.

The mathematical accuracy of (i) the computations of the adequacy of the maturing principal amounts of and interest on the Acquired Obligations to be held by the Refunding Trustee to pay principal and interest and the redemption premium, if any, on the Refunded Bonds as described above, and (ii) the computations supporting the conclusion of Bond Counsel that the Bonds are not “arbitrage bonds” under Section 148 of the Internal Revenue Code of 1986, as amended, will be verified by Grant Thornton LLP, independent certified public accountants.

Sources and Uses of Funds

The proceeds of the Bonds (excluding accrued interest) are expected to be applied as follows:

Sources of Funds

Par Amount of the Bonds	\$ 87,735,000
Net Original Issue Premium	<u>4,014,386</u>
Total Sources of Funds	<u>\$ 91,749,386</u>

Uses of Funds

Escrow Deposit	\$ 90,953,291
Costs of Issuance*	<u>796,095</u>
Total Uses of Funds	<u>\$ 91,749,386</u>

- * Includes legal fees, financial advisory fees, rating agency and printing costs, underwriter's discount, bond insurance premium, and certain miscellaneous expenses.

SECURITY FOR THE BONDS

Pledge of Revenues

The Bonds are special limited obligations of the City. The principal of and interest on the Bonds are payable out of the Seattle Municipal Light Revenue Parity Bond Fund (the "Parity Bond Fund"). The City has agreed to pay into the Parity Bond Fund on or prior to the respective dates on which principal of and premium, if any, and interest on Parity Bonds will be payable, certain amounts from the Gross Revenues of the Light System sufficient to pay such principal and interest as the same become due. The Gross Revenues of the Light System are pledged to make such payments, which pledge constitutes a lien and charge upon such revenues prior and superior to all other charges whatsoever except reasonable charges for maintenance and operation of the Light System. See Appendix A—Bond Ordinance—Sections 16 and 17(a). Gross Revenues include the proceeds received by the City directly or indirectly from the sale, lease or other disposition of any of the properties, rights or facilities of the Light System, but do not include Bond proceeds and certain insurance proceeds. See Appendix A—Bond Ordinance—Section 1. Maintenance and operation charges do not include any taxes paid to the City (see "The Department—Taxation and Intergovernmental Payments"), but do include the unconditional obligation to make payments under certain power purchase contracts. See "Contingent Obligations" below.

Payment of the principal of and premium, if any, and interest on Parity Bonds constitutes a first and prior lien upon Gross Revenues of the Light System, after payment of reasonable maintenance and operation costs, superior to payments of principal of and premium, if any, and interest on the outstanding 2001 Notes and 2002 Notes and the Subordinate Lien Bonds, all described below, unless and until such Subordinate Lien Bonds are converted to fixed rate Parity Bonds in compliance with the requirements for the issuance of additional Parity Bonds.

The Bonds do not constitute general obligations of the City, the State of Washington (the "State") or any political subdivision of the State, or a charge upon any general fund or upon any money or other property of the City, the State or any political subdivision of the State not specifically pledged thereto by the Bond Ordinance. Neither the full faith and credit nor the taxing power of the City, nor any revenues of the City derived from sources other than the Light System, are pledged to the payment of the Bonds.

Outstanding Parity Bonds

The Bonds are being issued on a parity of lien with the Outstanding Parity Bonds, which include 12 series of bonds issued since 1992. As of November 13, 2002, the City had \$1,327,971,000 principal amount of Outstanding Parity Bonds, of which \$86,560,000 will be refunded by the Bonds. See "Refunding Plan."

Rate Covenant

In the Bond Ordinance the City has covenanted, among other things, to establish and maintain rates sufficient to provide for payment of debt service on the Outstanding Parity Bonds and any additional bonds issued on a parity of lien with the Outstanding Parity Bonds (together, the “Parity Bonds”) and all other obligations for which revenues have been pledged or to provide for such payment from other sources, to pay all costs of maintenance and operation and to maintain the Light System in good order and repair. The Bond Ordinance does not include a requirement that the City set rates to achieve a specific level of debt service coverage on Parity Bonds. See “The Department—Financial Policies” and Appendix A—Bond Ordinance—Section 17(c).

Reserve Fund

The City has created and is required to maintain the Municipal Light and Power Bond Reserve Fund (the “Reserve Fund”). The City has covenanted and agreed that it will pay into the Reserve Fund, out of Gross Revenues, within five years from the date of issuance of the Bonds, such sums as will, together with money presently in the Reserve Fund, provide for the Reserve Fund Requirement, which is defined as an amount equal to the lesser of:

- (i) the maximum Annual Debt Service on all Parity Bonds then outstanding, and
- (ii) the maximum amount permitted by the Internal Revenue Code of 1986, as amended, as “a reasonably required reserve or replacement fund.”

On the New Covenant Date, as defined in the Bond Ordinance, “Reserve Fund Requirement” will mean, for any issue of Future Parity Bonds, the Reserve Fund Requirement specified for that issue, and the Reserve Fund Requirement for all series of Future Parity Bonds will be the sum of the Reserve Fund Requirements for all such Future Parity Bonds.

If payments from the Reserve Fund are required to pay interest on or principal of any Outstanding Parity Bonds, the City will deposit money into that fund out of any money legally available therefor until the Reserve Fund has been replenished to the Reserve Fund Requirement. The balance in the Reserve Fund as of September 30, 2002, was \$76,778,461, which amount was sufficient to meet the Reserve Fund Requirement on that date. Additional amounts will be deposited over the next five years to satisfy the Reserve Fund Requirement for the Parity Bonds. The Department’s financial forecast assumes that funds will be added to the Reserve Fund in each year through 2007 to meet the Reserve Fund Requirement on Outstanding Parity Bonds and the Bonds.

In lieu of cash deposits to the Reserve Fund, the City may provide Qualified Insurance or a Qualified Letter of Credit in an amount equal to the Reserve Fund Requirement or any portion thereof. See Appendix A—Bond Ordinance—Section 17(b)(i). The Department has not acquired and does not assume the use of such insurance or letter of credit in its financial forecast.

Future Parity Bonds

The Bond Ordinance authorizes the issuance of additional Parity Bonds subsequent to the issuance of the Bonds (the “Future Parity Bonds”) if:

- (i) there is no deficiency in the Parity Bond Fund or in any of the accounts therein and provision has been made to meet the Reserve Fund Requirement for all Parity Bonds then outstanding plus the proposed Future Parity Bonds, and
- (ii) either:
 - (a) the Finance Director certifies that Gross Revenues (with certain adjustments), less the expenses of operation, maintenance and repair of the Light System (the “Net Revenue”), in any 12 consecutive months out of the most recent 24 months preceding the issuance of the Future Parity Bonds (the “Base Period”) was not less than 125 percent of maximum Annual Debt Service in any future calendar year on all Parity Bonds then outstanding and the Future Parity Bonds proposed to be issued, or

- (b) the City has on file a certificate of a Professional Utility Consultant stating that the Adjusted Net Revenue for the Base Period, calculated as described in the Bond Ordinance, was not less than 125 percent of maximum Annual Debt Service in any future calendar year on all Parity Bonds then outstanding and the Future Parity Bonds proposed to be issued. The Bond Ordinance permits the Professional Utility Consultant to adjust Net Revenue based on certain conditions. See Appendix A—Bond Ordinance—Section 17(f).

On the New Covenant Date, “Net Revenue” will mean, for the purpose of these requirements for the issuance of Parity Bonds, that amount determined by deducting from Gross Revenues the expenses of operation, maintenance and repair of the Light System and further deducting any deposits into the Rate Stabilization Account and by adding to Gross Revenues any withdrawals from the Rate Stabilization Account.

The Bond Ordinance authorizes the issuance of Refunding Parity Bonds without the requirement of meeting the above provisions. See Appendix A—Bond Ordinance—Section 17(g) and 17(h).

Payment Agreements

With the defeasance of all of the Refunded 1992B Bonds, which will occur upon the closing of the Bonds, the City will be permitted to enter into Parity Payment Agreements that constitute a charge and lien on Net Revenue equal to that of the Parity Bonds. See Appendix A—Bond Ordinance—Section 1—Definitions—Annual Debt Service. The prerequisites described above for the issuance of Future Parity Bonds will apply to the City’s incurrence of obligations under any Parity Payment Agreements.

No Acceleration of the Bonds

The Bonds are not subject to acceleration upon the occurrence of a default. The City, therefore, would be liable only for principal and interest payments as they become due. In the event of multiple defaults in payment of principal or interest on the Parity Bonds, the registered owners would be required to bring a separate action for each such payment not made. This could give rise to a difference in interests between registered owners of earlier and later maturing Parity Bonds.

Subordinate Lien Bonds

The City had \$100,040,000 principal amount of outstanding Subordinate Lien Bonds as of November 1, 2002, all in variable rate mode. The ordinances authorizing the issuance of the Subordinate Lien Bonds allow for the conversion of those bonds to Parity Bonds upon compliance with the requirements relating to the issuance of additional Parity Bonds at the time of conversion. Under the authorizing ordinances, the aggregate principal amount of outstanding Subordinate Lien Bonds at the time of issuance is limited to the greater of \$70,000,000 or 15 percent of the aggregate principal amount of Parity Bonds then outstanding.

The City’s repayment obligations under the reimbursement agreements between the City and J.P. Morgan Chase & Co. (the “Bank”), the provider of the letters of credit for the Subordinate Lien Bonds, are subject to acceleration, at the option of the Bank, if the City is in default under those reimbursement agreements. If the Bank were to exercise its right to accelerate, the Department could be obligated to pay from Gross Revenues the total amount then owed to the Bank. That amount could be as much as the entire outstanding principal amount of the Subordinate Lien Bonds plus accrued interest thereon and any applicable Bank fees or charges.

Notes

Also outstanding on November 1, 2002, was \$182,210,000 principal amount of Municipal Light and Power Revenue Anticipation Notes, 2001 (the “2001 Notes”), which mature on March 28, 2003. As of October 1, 2002, there was on deposit in the Municipal Light and Power Revenue Anticipation Note Account, 2001 (the “Note Account”) the amount of \$91,105,000 for payment of one-half of the principal amount of the 2001 Notes due on March 28, 2003.

On November 21, 2002, the Department expects to issue up to \$125,000,000 principal amount of Municipal Light and Power Revenue Anticipation Notes, 2002 (the “2002 Notes” and together with the 2001 Notes, the “Notes”) maturing on November 21, 2003, to fund its operating cash flow requirements over the period

through November 2003. The proposed 2002 Notes will be issued on a parity with the 2001 Notes and will mature subsequent to the 2001 Notes. Additional notes or other obligations may be issued on a parity with or subordinate to the 2001 Notes and the proposed 2002 Notes.

Contingent Obligations

The Department has in the past and may in the future enter into various agreements, such as energy purchase agreements, under which the Department may be obligated to make payments or post collateral contingent upon certain future events within or beyond the Department's control. Such contingent payment obligations may be treated as operation and maintenance charges payable from Gross Revenues prior to the payment of principal of and interest on the Parity Lien Bonds, the Subordinate Lien Bonds and the Notes. See "Power Resources—Purchased Power Arrangements."

DESCRIPTION OF THE BONDS

The Bonds will be dated December 1, 2002. Interest on the Bonds is payable semiannually on each June 1 and December 1, beginning June 1, 2003, at the rates set forth on the inside cover of this Official Statement. Principal is payable on each December 1, beginning December 1, 2003, in the amounts set forth on the inside cover of this Official Statement. Interest on the Bonds is to be computed on the basis of a 360-day year consisting of twelve 30-day months. The Bonds will be issued in \$5,000 denominations and integral multiples thereof. The principal of and interest on the Bonds is payable by the Bond Registrar, currently the fiscal agent of the State of Washington (the "Bond Registrar") (currently, The Bank of New York in New York, New York). For so long as the Bonds remain in a "book-entry only" transfer system, the Bond Registrar will make payments of principal and interest only to DTC, which in turn will remit such payments to its participants for subsequent disbursement to beneficial owners of the Bonds, as further described in Appendix E hereto.

Redemption of the Bonds

Optional Redemption. The Bonds maturing before December 1, 2013, are not subject to redemption prior to maturity. The Bonds maturing on or after December 1, 2013, are subject to redemption prior to maturity at the option of the City on and after December 1, 2012, in whole or in part at any time (maturities to be selected by the City and within a maturity by lot in such manner as the Bond Registrar may determine and, so long as the Bonds are in book-entry form, in accordance with the procedures established by the securities depository) at the price of par plus accrued interest.

Notice of Redemption. Notice of any intended redemption will be given not less than 30 nor more than 60 days prior to the redemption date by first-class mail, postage prepaid, to the registered owner of any Bond to be redeemed at the address appearing on the Bond Register at the time the Bond Registrar prepares the notice. The requirements of this section will be deemed to have been fulfilled when the notice is mailed, whether or not it actually is received by the registered owner of any Bond. As long as the Bonds are held in book-entry form, notices will follow procedures established by the securities depository. See "Description of the Bonds—Book-Entry Transfer System."

Open Market Purchase

The City reserves the right and option to purchase any or all of the Bonds in the open market at any time at any price acceptable to the City plus accrued interest to the date of purchase.

Book-Entry Transfer System

Book-Entry Bonds. DTC will act as initial securities depository for the Bonds. The ownership of one fully registered Bond for each maturity, as set forth on the inside cover of this Official Statement, each in the aggregate principal amount of such maturity, will be registered in the name of Cede and Co., as nominee for DTC. For so long as the Bonds remain in a "book-entry only" transfer system, the Bond Registrar will make payments of principal and interest only to DTC, which in turn will remit such payments to its participants for subsequent disbursement to beneficial owners of the Bonds. See Appendix E for additional information. As

indicated therein, certain information in Appendix E has been provided by DTC. The City makes no representation as to the accuracy or completeness of the information in Appendix E provided by DTC. Purchasers of the Bonds should confirm this information with DTC or its participants.

Termination of Book-Entry Transfer System. If DTC resigns as the securities depository and the City is unable to retain a qualified successor to DTC, or if the City determines that a continuation of the book-entry transfer system is not in the best interests of the City, the City will deliver at no cost to the beneficial owners of the Bonds or their nominees Bonds in registered certificate form, in the denomination of \$5,000 or any integral multiple thereof within a maturity. Thereafter, the principal of the Bonds will be payable upon due presentment and surrender thereof at the principal office of the Bond Registrar. Interest on the Bonds will be payable by check or draft mailed or by wire transfer (wire transfer will be made only if so requested in writing and if the registered owner owns at least \$1,000,000 par value of the Bonds), to the persons in whose names such Bonds are registered, at the address appearing upon the registration books on the 15th day of the month preceding an interest payment date, and the Bonds will be transferable as provided in the Bond Ordinance.

THE DEPARTMENT

Introduction

The Department is a municipally-owned electric utility. In 1905, the City began providing its residents with electricity generated by the Cedar Falls Hydroelectric Plant, which was the first municipally-owned hydroelectric facility in the nation. By 1910, operational responsibility for the City's electric system had been assigned to a separate lighting department, referred to herein as the "Department." In 1951, the Department purchased from Puget Sound Power and Light Company certain generation, transmission and distribution facilities serving the City's residents. The Department has operated without competition in its service area since the 1951 purchase. See "Customers, Energy Sales and Requirements and Peak Loads—Service Area" for a description of the Department's service area.

The Light System currently consists of seven hydroelectric generating plants (with an aggregate one-hour peak capability of approximately 1,800 MW), approximately 656 miles of transmission lines (through which electricity is wheeled to and between the Department's various substations), over 2,400 miles of distribution lines (through which electricity is delivered from such substations to customers), 14 major substations, and two service centers. See "City Light System" and "Power Resources" for a discussion of the Department's existing facilities and "Capital Improvement and Conservation Implementation Programs" for a discussion of the Department's proposed capital projects. The Light System is interconnected with transmission lines owned by the Bonneville Power Administration ("Bonneville"). See "Power Resources—Transmission" for a discussion of Bonneville's transmission system.

Management

The Department is a department of the City and is subject to ordinances and resolutions adopted by the City Council and approved by the Mayor. The Mayor and City Council approve the Department's budget, set rates and approve financing and bond issuance, along with other functions outlined in the City Charter. The Department is under the direction of a superintendent, who is appointed by the Mayor and confirmed by the City Council.

In May 2002, the Mayor appointed a six-member panel to examine the Department's practices and strategies in the areas of power management, resource acquisition, risk management, and financing, and to recommend any changes in the Department's governance that the panel considered appropriate. In October 2002, the panel submitted a set of recommendations to the Mayor that included a proposal to establish an advisory committee consisting of five to seven individuals with expertise in the areas of concern. The panel also recommended that the City Council and Mayor's office increase the level of resources devoted to oversight of the Department and establish clear policies for power management and risk management. The Mayor has indicated support for the panel's recommendations. See "The City's Response to the Western Power Crisis—External Reviews of the Department."

The Department is organized into four main operating branches (Generation, Distribution, Power Management, and Customer Services) which are headed by Deputy Superintendents who report directly to the Superintendent. A Deputy Superintendent for Finance and Administration, also reporting to the Superintendent, has responsibility for the Department's major administrative functions, including Finance, Information Technology and Facilities. Division Directors responsible for the Human Resources Division, Environment and Safety Division, Strategic Planning Office, External Affairs Office, and Account Executives Office also report directly to the Superintendent.

Brief descriptions of the backgrounds of certain key officials of the Department are provided below:

Gary Zarker, Superintendent, was appointed Superintendent in 1994. Prior to his appointment, Mr. Zarker served in several positions within the City, including Director of Engineering and Director of the Office of Management and Budget. Mr. Zarker serves on the board of directors for Energy Northwest, the Western Systems Coordinating Council and the Northwest Public Power Association and on the Steering Committee for the Large Public Power Council, and is actively involved in the Public Generating Pool. Mr. Zarker graduated from Grinnell College, Iowa, with a Bachelor of Arts degree.

Jesse A. Krail, P.E., Deputy Superintendent, Distribution, was appointed to his current position in 1996. Mr. Krail is responsible for management of the Distribution Branch, which delivers power and electrical services, including transmission, substations, feeders, and meters, to customers. Mr. Krail has extensive experience in public works and a broad management, engineering and customer service background with large public agencies, including the King County Department of Public Works/Transportation and the Seattle Engineering Department. Mr. Krail holds a Bachelor of Science degree in electrical engineering from Union College, New York. He is a Licensed Civil Engineer in the State of Washington.

Dana L. Backiel, Deputy Superintendent, Generation, was appointed to her current position in 1998. From her appointment to Chief Engineer in 1996 until her present appointment, Ms. Backiel managed all in-house engineering service functions. Previously, Ms. Backiel held the position of Power Stations Director and served as Acting North Electric Services Director. Ms. Backiel obtained her bachelor's degree in electrical engineering from Case Institute of Technology (Case/Western Reserve University) in Cleveland, Ohio.

James P. Ritch, Deputy Superintendent, Finance and Administration, was appointed to his current position of chief financial officer for the Department in 1995. Mr. Ritch has held various positions in City government, including Director of the Office of Management and Budget and Director of the Department of Administrative Services. Mr. Ritch also was the Vice President of Human Resources for Egghead Software. Mr. Ritch received Bachelor of Arts and Master of Arts degrees in economics from the University of Washington.

Joan Walters, Deputy Superintendent, Customer Services, was appointed to her current position in January 2002. Immediately prior to her appointment, Ms. Walters served as Budget Director for the City. During the 1990s, Ms. Walters held a number of positions with the State of Illinois, including Director of the Bureau of the Budget and Director of the Department of Public Aid. Ms. Walters holds a Bachelor of Arts degree in science from Governors State University in Illinois.

Mike Sinowitz, Deputy Superintendent, Power Management, served as Director of the City Light Power Control Center from June 1999 until his appointment to his current position in February 2002. Mr. Sinowitz joined the Department in 1987 as Manager of Generation, Transmission and Scheduling Dispatch at the System Control Center. He has over 30 years of experience in the utility industry, including positions with Pacific Gas & Electric, San Diego Gas & Electric and the Arabian-American Oil Company. Mr. Sinowitz holds a Bachelor of Science degree in electrical engineering from the University of California at San Diego.

Employee Relations

As of September 30, 2002, the Department had 1,600 full-time equivalent employees, almost all of whom are members of the City's Employee Retirement System. The Retirement System requires the Department, like all other City departments, to make contributions equal to an actuarially determined percentage of covered payrolls. See "The City of Seattle—Pension System."

State law requires municipal agencies to bargain collectively with formally recognized collective bargaining units. Currently, 14 union locals represent approximately 80 percent of the Department's regular full-time employees. The collective bargaining agreements between each of these unions and the Department will expire either on December 31, 2004, or on January 22, 2005. There have been no strikes during the past 20 years, and the Department considers its employee relations to be satisfactory. See "The City of Seattle—Labor Relations."

Outstanding Debt and Debt Service Requirements

As of September 30, 2002, there were outstanding \$1,327,971,000 in senior lien City of Seattle Municipal Light and Power Revenue Bonds (the "Parity Bonds"), \$100,040,000 in junior lien City of Seattle Municipal Light and Power Adjustable Rate Revenue Bonds (the "Subordinate Lien Bonds") and \$182,210,000 in 2001 Notes, due March 28, 2003, which are subordinate to the Parity Bonds and the Subordinate Lien Bonds. In addition, the City Council by ordinance in December 2001 authorized the Department to borrow up to \$110,000,000 from the City's Consolidated (Residual) Cash Pool (the "Cash Pool"), of which

\$78,300,000 was outstanding as of September 30, 2002. The Department plans to refinance its borrowing from the Cash Pool by issuing, on November 21, 2002, its 2002 Notes in an amount up to \$125,000,000 on a parity with the 2001 Notes.

Principal of and interest on the Parity Bonds, Subordinate Lien Bonds, Cash Pool loan, and Notes are payable from the gross revenues of the Light System, after payment of reasonable charges for maintenance and operation of the Light System. Maintenance and operation charges include the unconditional obligation to make payments under certain power purchase contracts.

Principal and interest payments due on the Department's outstanding Senior and Subordinate Lien Bonds are shown in the following table, which has not been adjusted to show the effects of the Refunding Plan. In addition to the amounts shown in the table, in 2003 the Department will pay \$182,210,000 in principal and \$4,199,362 in interest on the 2001 Notes and \$125,000,000 in principal on the proposed 2002 Notes, plus interest.

DEBT SERVICE REQUIREMENTS*

Year	Parity Bonds			Subordinate Lien Bonds			All Bonds
	Principal	Interest	Total	Principal	Interest	Total	Total Debt Service
2002	\$ 38,291,500	\$ 72,403,329	\$ 110,694,829	\$ 3,360,000	\$ 1,736,805	\$ 5,096,805	\$ 115,791,634
2003	39,250,000	70,472,017	109,722,017	3,585,000	1,973,142	5,558,142	115,280,159
2004	47,650,000	68,296,087	115,946,087	4,115,000	3,218,138	7,333,138	123,279,225
2005	50,176,000	65,766,732	115,942,732	4,445,000	3,850,608	8,295,608	124,238,340
2006	52,750,000	63,192,604	115,942,604	4,775,000	3,703,927	8,478,927	124,421,531
2007	55,520,000	60,421,428	115,941,428	5,305,000	3,572,170	8,877,170	124,818,598
2008	58,340,000	57,608,370	115,948,370	5,840,000	3,342,551	9,182,551	125,130,921
2009	61,610,000	54,339,561	115,949,561	6,270,000	3,075,680	9,345,680	125,295,241
2010	65,090,000	50,858,966	115,948,966	6,705,000	2,771,929	9,476,929	125,425,895
2011	60,090,000	47,728,626	107,818,626	7,345,000	2,722,544	10,067,544	117,886,170
2012	60,245,000	44,395,501	104,640,501	7,785,000	2,604,703	10,389,703	115,030,204
2013	62,885,000	40,959,425	103,844,425	8,425,000	2,262,284	10,687,284	114,531,709
2014	63,225,000	37,457,400	100,682,400	8,865,000	1,799,802	10,664,802	111,347,202
2015	63,690,000	33,952,938	97,642,938	9,410,000	1,331,760	10,741,760	108,384,698
2016	64,180,000	30,432,913	94,612,913	7,755,000	786,304	8,541,304	103,154,217
2017	64,050,000	26,903,138	90,953,138	2,600,000	518,751	3,118,751	94,071,889
2018	62,915,000	23,748,163	86,663,163	2,750,000	369,051	3,119,051	89,782,214
2019	59,415,000	20,357,038	79,772,038	1,300,000	207,744	1,507,744	81,279,782
2020	57,090,000	17,144,993	74,234,993	1,355,000	128,858	1,483,858	75,718,851
2021	54,550,000	14,126,413	68,676,413	1,410,000	43,590	1,453,590	70,130,003
2022	53,100,000	11,155,566	64,255,566				64,255,566
2023	52,505,000	8,264,274	60,769,274				60,769,274
2024	53,085,000	5,402,781	58,487,781				58,487,781
2025	36,430,000	2,699,148	39,129,148				39,129,148
2026	30,130,000	772,081	30,902,081				30,902,081
	<u>\$ 1,366,262,500</u>	<u>\$ 928,859,490</u>	<u>\$ 2,295,121,990</u>	<u>\$ 105,800,000</u>	<u>\$ 49,985,232</u>	<u>\$ 155,785,232</u>	<u>\$ 2,450,907,222</u>

* Does not reflect the effect of issuance of the Bonds on debt service.

City Light System

Power Resources. The Department owns and operates three major hydroelectric generating plants on the Skagit River, approximately 80 miles northeast of Seattle, and the Boundary Hydroelectric Plant (the “Boundary Project”) on the Pend Oreille River, approximately 250 miles east of Seattle. In addition, the Department owns three smaller hydroelectric plants in western Washington. The Department sold its eight percent share of the coal-fired Centralia Steam Plant to TransAlta Corporation in May 2000.

In addition to these resources, the Department’s power is supplied through contracts with Bonneville, two public utility districts and three Columbia Basin irrigation districts. Additional contracts are in place with King County, the Province of British Columbia, the City of Klamath Falls, Oregon, three Idaho irrigation districts, and one Oregon irrigation district. A long-term contract for the purchase of power from a wind-powered generation project in the Northwest region has been signed with PacifiCorp Power Marketing, Inc. (“PPM”), the developer of the project.

More detailed information on the Department’s power resources is provided under “Power Resources” below.

Transmission Facilities. The Department operates a system of 656 miles of transmission facilities that follow several routes. Power from the Skagit River plants is transmitted over lines owned by the Department. The Department also uses the facilities of other agencies, principally Bonneville, to transmit power from other generating plants from which the Department receives power, including the Boundary Project. The Department’s transmission facilities are connected to Bonneville’s transmission grid. The Department also has acquired ownership rights to 160 MW of capacity over the AC Intertie, which connects the Pacific Northwest power grid with the Southwest region. See “Power Resources—Transmission.”

Distribution Facilities. There are 14 major substations in the Light System. Those of recent construction have been designed with an emphasis on aesthetics and have received national attention and architectural awards. Service in the City’s downtown business area and other areas of high load density is provided through underground network systems.

General Plant. The Department’s general plant facilities include two service centers that serve as headquarters for construction and maintenance activities, the System Control Center, communication facilities, transportation equipment, and office equipment, including data processing equipment. The System Control Center, completed in 1995, houses an advanced energy management system. The Department’s central administrative offices are located in Key Tower, a downtown Seattle office building owned by the City.

Taxation and Intergovernmental Payments

The Department pays a utility tax to the City equal to six percent of Gross Revenues from sales within the State and five percent of Gross Revenues from retail sales outside the State, less certain adjustments. The proceeds of this tax are deposited into the City’s General Fund. The City Charter does not permit the Department to pay taxes to the City’s General Fund “until ample provision has been made for the servicing of the debts and obligations of the utility and for necessary betterments and replacements for the current year.” A State public utility tax is paid at a rate of 3.873 percent of Gross Revenues from sales within the State, less certain adjustments.

Certain contractual payments are made to Pend Oreille and Whatcom Counties, Washington, for services rendered. Under the terms of franchise agreements signed in 1998 and 1999, the Department makes payments to the cities of Shoreline, Burien, Lake Forest Park, and SeaTac in amounts equal to six percent of the revenue derived from customers residing within those cities that is attributable to the energy component of their rates.

Retail Rates

Rate Setting. The City Council has exclusive jurisdiction with respect to establishing and revising the Department’s retail rates. State law requires that rates must be fair, nondiscriminatory and fixed to produce revenue that is adequate to pay operation and maintenance expenses of the Department and to meet all debt

service requirements payable from such revenue. In its retail rate-setting capacity, the City Council is not subject to control by the Washington Utilities and Transportation Commission, but it is subject to certain rate-making provisions of the Public Utility Regulatory Policies Act of 1978. The Department never has been cited for failing to comply with such act, and believes that it is operating in compliance with the requirements of such act.

Since 1980 the City Council has conducted comprehensive reviews of the Department’s rate levels and rate structure at intervals of two or three years. In the course of its rate reviews, the City Council holds public meetings to consider the Department’s proposed budget, construction plan, load forecast, and resource plans. Based on these planning documents, as approved by the City Council, the Department’s staff estimates the Department’s revenue requirements and develops a rate proposal that will produce the required amount of revenue and allocate the revenue requirement among the various rate classes in accordance with City policy. The City Council holds public meetings to introduce and explain the proposals to the public and to accept public input. The Council makes final decisions through passage of a rate ordinance.

Rate Changes: 1990-1999. From 1990 through 1999, the City’s periodic rate reviews resulted in the following changes in average rates for the system as a whole:

SUMMARY OF RATE CHANGES 1990-1999

<u>Effective Date</u>	<u>Percentage Change</u>
January 1, 1990	(2.4)%
May 1, 1993	12.6
March 1, 1995	5.7
March 1, 1996	5.3
March 6, 1997	(0.4)
March 1, 1998	(0.6)
December 24, 1999	3.2

In addition to these changes, the City Council imposed three temporary surcharges ranging from 4.1 percent to 10.0 percent between 1992 and 1995 to offset the impact of poor water conditions on power costs.

The most recent comprehensive rate review took place in 1999 and culminated in the passage of an ordinance in November 1999 that provided for an average increase of 3.2 percent, effective December 24, 1999. Pursuant to City policy, rates for low-income residential customers were set at levels 50 percent below rates in the standard residential classes. The ordinance provided for a further increase averaging 3.0 percent, effective March 1, 2002.

Rate Changes: 2000-2002. In 2000 and the first nine months of 2001, the Department was required to purchase large amounts of power in the wholesale market as a result of its 1996 decision to limit purchases of power from Bonneville (see “Power Resources—Purchased Power Arrangements”), the sale of the Centralia Steam Plant in May 2000 and unusually poor water conditions in the water year beginning October 1, 2000. Beginning in May 2000, largely as a result of supply constraints and the repercussions of restructuring efforts in California, wholesale market prices increased to unprecedented levels. As a result, the Department incurred power expenses in 2000 and 2001 that in total exceeded its budgeted estimates by almost \$600 million. See “The Western Power Crisis,” “The City’s Response to the Western Power Crisis” and “Historical and Projected Operating Results.” In response to these developments, the City increased rates four times in 2001:

- (i) Effective January 1, 2001, all energy charges were increased by 0.4 cents per kWh, with the exception of rates for low-income customers, which were increased by 0.2 cents per kWh. On the average, rates increased by 9.8 percent.
- (ii) Effective March 1, 2001, winter energy charges for all classes except the low-income classes were increased by 0.4 cents per kWh and the distinction between summer rates and winter rates was eliminated. Rates for low-income customers remained unchanged. With rates for non-low-income

customers set at the higher winter levels in all months of the year, average rates increased by 18.0 percent.

- (iii) Effective July 1, 2001, energy charges for all classes except the low-income classes were increased by 0.49 cents per kWh, which represented an increase of 9.3 percent in average rates. Average rates for low-income customers were not increased, but the distinction between summer and winter rates for low-income customers was eliminated, and rates were set at the average of winter and summer rates.
- (iv) Effective October 1, 2001, all energy charges were increased by 0.6 cents per kWh, or 10.3 percent, with the exception of the low-income rate classes, which received an increase of 0.3 cents per kWh. This increase passed through to customers the financial effect of increases in rates charged by Bonneville for transmission services and power purchases. Pass-through of the transmission and power rate increases had been mandated by the ordinances implementing the December 24, 1999, rate increases and the July 1, 2001, power cost adjustment, respectively. See “Power Resources—Purchased Power Arrangements.”

The last of the rate ordinances in 2001 also required that the effect of future increases or decreases in Bonneville rates be passed through to customer classes through adjustments to their energy charges. Pursuant to this provision, energy charges for all rate classes were reduced by 0.07 cents per kWh, effective April 1, 2002, except for low-income rates, which were reduced by 0.03 cents per kWh. This resulted in an average decrease of 1.1 percent.

In addition to the four power cost adjustments enacted in 2001, rates for Medium and Large General Service customers in the downtown network were increased by 4.1 percent and 3.8 percent respectively, effective March 1, 2002, as provided for in the November 1999 rate ordinances. Fees for rental of streetlights, poles, ducts, and vaults also increased on that date. These increases resulted in an average increase of 0.5 percent for the system as a whole. The ordinance enacting the power cost adjustment effective July 1, 2001, eliminated the increases for the other rate classes that were to have taken effect on March 1, 2002, under the terms of the November 1999 ordinance.

SUMMARY OF RATE CHANGES SINCE JANUARY 1, 2000

<u>Effective Date</u>	<u>Percentage Change</u>
January 1, 2001	9.8%
March 1, 2001	18.0
July 1, 2001	9.3
October 1, 2001	10.3
March 1, 2002	0.5
April 1, 2002	(1.1)

The net effect of the four power cost adjustments in 2001, the March 1, 2002, increase in network rates and the pass-through of the Bonneville rate decrease on April 1, 2002, has been to increase average rates for the system as a whole by 55 percent. Because low-income rates were exempted from the power cost adjustments effective March 1, 2001, and July 1, 2001, rates for low-income customers increased by 19 percent.

Under the terms of the financial policies adopted by the City Council for the Department in December 2001, current rates will remain in effect until the Department repays all short-term debt obligations, including the Notes and the amounts borrowed from the Cash Pool, and accumulates an operating account cash balance of \$30 million, unless rates are increased by City Council action or adjusted to pass through further changes in Bonneville power rates. These conditions are expected to be met in mid-2004. At that point rates can be set in accordance with the rate-setting guidelines in the Council-adopted financial policies, which give greater recognition to the higher risks that the Department faces in the current utility environment. The Department’s financial forecast assumes that new rates will take effect on January 1, 2005. Financial policies adopted by the City Council are subject to change by the City Council. See “The Department—Financial Policies.”

In 2001, the Department's average rate for residential service was 6.15 cents per kWh. The Department's commercial and industrial rates averaged 5.38 cents and 5.10 cents per kWh, respectively. See the table titled "Unit Revenue and Monthly Bills." With the Department's recent power cost adjustments taken into account, the Department's current average rates are below the national average. See the table titled "Annual Bill Comparisons with Other Puget Sound Utilities."

Market-Indexed Rates for High Demand Customers. Since 1996, the Department has offered a market-indexed rate schedule ("Market-Indexed Schedule") to the seven customers in its High Demand General Service class. Currently no customers are served under the Market-Indexed Schedule.

Special Rates for New Large Loads. In 2000, the Department received a number of requests from customers for the connection of facilities serving the high-technology, Internet-related sector. The estimated energy consumption of these facilities was very high. In order to meet the Department's obligation to serve, the City Council passed an ordinance in October 2000 that created a new customer class for New Large Loads. A New Large Load is defined in the ordinance as any service fed from an expanded or a new installation equal to or greater than 12.5 megavolt-amperes ("MVA") of energized capacity installed within any consecutive five-year period after August 31, 2000. The ordinance provides that New Large Load customers will be charged for service either under the Department's Market-Indexed Schedule (see "The Department—Retail Rates—Market-Indexed Rates for High Demand Customers") or on the basis of a negotiated, customized delivery and payment package which would include one of a number of options for acquiring and paying for energy. New Large Loads will also pay a retail service charge to the Department for delivery of power to the customer's premises. Under either payment option, each New Large Load customer is responsible for installation costs and a fixed charge per MW of capacity to cover the cost of providing feeder and substation capacity.

Interruptible Rates for High Demand Customers. In December 2001, the City Council passed an ordinance creating a new rate class for customers in the High Demand General Service class who sign contracts with the Department for interruptible service. Under the terms of such contracts, the Department has the right to interrupt service to such customers when the wholesale market price of energy exceeds a "trigger price," which has been set at \$55 per MWh through the end of 2003 and may be adjusted by the Department after that date. Through December 31, 2001, rates for High Demand customers choosing to be served on this basis are set at a level which approximates what the rates for the High Demand class would be without the power cost adjustments effective January 1, March 1 and July 1, 2001, but including the pass-through of Bonneville rate changes. Effective January 1, 2004, rates for this class will be the standard rates for customers in the High Demand class, plus 0.725 cents per kWh. The additional charge of 0.725 cents per kWh is intended to recover over a five-year period the revenue that would have been received in 2002 and 2003 if the interruptible customer had paid the standard High Demand rates, including the power cost adjustments. These rates will remain in effect until the customer has consumed five times the amount of energy actually consumed in calendar year 2000. One customer has signed a contract with the Department for interruptible service.

Voluntary Green Power Program. In 2000 the State Legislature passed a law requiring all utilities in the State to provide retail electricity customers a voluntary option to purchase electricity derived from alternative energy resources, effective January 1, 2002. Pursuant to this requirement, the Department now provides residential customers the option of paying additional monthly amounts of \$3, \$7 or \$10 to fund renewable resources. Non-residential customers also can elect to make voluntary payments in amounts ranging from \$8 to \$150 per month. The proceeds of these voluntary payments will be used by the Department to fund the acquisition of energy from renewable resources, such as solar, wind, fuel cells, and landfill gas. See "Power Resources—Purchased Power Arrangements—Other Renewable Resources." As of June 2002, more than 2,700 customers had elected to participate in the program.

UNIT REVENUE AND MONTHLY BILLS ⁽¹⁾

	Average Revenue (Cents per kWh)		Average Monthly Bill (\$)	
	Summer	Winter	Summer	Winter
Residential: City				
500 kWh per month	6.6	5.0	33	25
1,000 kWh per month	7.6	6.8	76	68
2,000 kWh per month	8.1	7.7	162	154
Residential: Suburban				
500 kWh per month	6.7	5.1	33	26
1,000 kWh per month	7.7	6.9	77	69
2,000 kWh per month	8.2	7.8	164	156
Small General Service: City				
10,000 kWh per month (40kW)	6.1	6.1	605	605
Small General Service: Suburban				
10,000 kWh per month (40kW)	6.2	6.2	616	616
Medium General Service: City Non-network				
20,000 kWh per month (60kW)	6.2	6.2	1,234	1,234
200,000 kWh per month (500kW)	6.1	6.1	12,235	12,235
Medium General Service: City Network				
20,000 kWh per month (60kW)	6.8	6.8	1,365	1,365
200,000 kWh per month (500kW)	6.7	6.7	13,495	13,495
Medium General Service: Suburban				
20,000 kWh per month (60kW)	6.3	6.3	1,256	1,256
200,000 kWh per month (500kW)	6.2	6.2	12,455	12,455
Large General Service: City Non-network				
400,000 kWh per month (1,000kW)	5.7	5.7	22,955	22,928
1,800,000 kWh per month (5,000kW)	5.7	5.7	103,495	103,375
Large General Service: City Network				
400,000 kWh per month (1,000kW)	6.2	6.2	24,813	24,765
1,800,000 kWh per month (5,000kW)	6.2	6.2	112,075	111,859
Large General Service: Suburban				
400,000 kWh per month (1,000kW)	5.8	5.8	23,312	23,287
1,800,000 kWh per month (5,000kW)	5.8	5.8	105,102	104,991
High Demand General Service				
6,000,000 kWh per month (20,000kW)	5.5	5.5	330,907	330,660
18,000,000 kWh per month (60,000kW)	5.5	5.5	992,722	991,981

(1) Based on rates in effect October 1, 2002.

**ANNUAL BILL COMPARISONS WITH OTHER PUGET SOUND UTILITIES
(BASED ON RATES IN EFFECT ON OCTOBER 1, 2002)**

Monthly Use		Seattle City Light			Puget Sound Energy ^{(3) (4)}	Snohomish County PUD ⁽⁴⁾	Tacoma Power
kWh	kW	City ⁽¹⁾	City Network	Suburban			
RESIDENTIAL							
100		\$86		\$87	\$126	\$155	\$131
500		\$347	(2)	\$353	\$364	\$471	\$393
1,000		\$862		\$874	\$662	\$943	\$721
2,000		\$1,892		\$1,916	\$1,534	\$1,886	\$1,376
Annual Bill at 2001 SCL							
Average Residential Usage		\$631		\$661	\$565	\$733	\$574
SMALL GENERAL SERVICE							
300	1	\$218		\$222	\$408	\$361	\$316
3,000	10	\$2,178	(2)	\$2,218	\$2,610	\$2,669	\$2,186
10,000	40	\$7,260		\$7,392	\$8,319	\$8,654	\$7,034
MEDIUM GENERAL SERVICE							
20,000	60	\$14,806		\$15,070	\$17,167	\$17,204	\$11,565
200,000	500	\$146,820		\$149,460	\$162,325	\$171,104	\$104,959
360,000	900	\$264,276		\$269,028	\$291,946	\$307,904	\$188,485
LARGE GENERAL SERVICE							
400,000	1,000	\$275,297		\$279,591	\$269,166	\$269,400	\$209,366
1,800,000	5,000	\$1,241,220		\$1,343,605	\$1,235,310	\$1,228,920	\$968,837
2,500,000	7,500	\$1,726,568		\$1,871,689	\$1,749,522	\$1,725,300	\$1,377,192
HIGH DEMAND GENERAL SERVICE							
6,000,000	20,000	\$3,969,408			\$3,491,568	\$4,207,200	\$3,418,968
18,000,000	60,000	\$11,908,223	(2)	(2)	\$10,474,704	\$12,621,600	\$10,255,800
24,000,000	60,000	\$15,784,966			\$13,296,672	\$16,164,000	\$12,529,416
Last Rate Change		6/14/2002	6/14/2002	6/14/2002	9/5/2002	4/1/2002	10/1/2001

- (1) Annual bills are those charges that would be incurred by a customer of this size if rates in effect October 1, 2002, were in effect for an entire 12-month period. Some of the utilities listed above may have special contractual arrangements with customers that are not reflected in the table.
- (2) There are no Network Residential and Small General Service Rates and no High Demand General Service Network and Suburban Rates.
- (3) For Puget Sound Energy, Large General Service is Primary General Service and High Demand General Service is High Voltage General Service.
- (4) Does not include local taxes.

Billing and Collection Processes

The Department currently bills its residential customers bi-monthly and all other customers monthly. Such bills are due within 15 days of receipt. The Department has established various payment programs for its customers, including a leveled monthly payment program and an electronic funds transfer program. Accounts receivable write-offs by the Department in 2000 and 2001 were less than one percent of energy sales revenue. The Department's collection policy provides for disconnection of power for nonpayment of amounts due the Department, subject to statutory prohibitions against disconnecting customers in winter months.

Financial Policies

The rate covenants in the Department's Parity Bond ordinances do not require the Department to set rates that achieve a specific level of debt service coverage on Parity Bonds. However, the City Council has adopted by resolution financial policies to be used by the Department in setting rates. From 1990 through December 2001, these policies required that rates be set at levels that would be expected to provide debt service coverage of 1.80 times debt service on Parity Bonds. In December 2001 the Council adopted by resolution new financial policies which require that rates be set at levels that will provide 95 percent confidence that net revenue available to fund capital requirements will be greater than zero, after payment of all operating and maintenance expenses, debt service, City taxes, deposits to the Parity Bond Reserve Fund, and other current obligations. Coverage is expected to exceed 2.0 times debt service on Parity Bonds under the new rate-setting policies. The new policies additionally require that, in the first two years in which they are in effect, rates be set at levels which will allow the accumulation of a \$25 million contingency reserve account. The new rate-setting policies will take effect after the Department has retired all short-term debt obligations, including the Notes and the amounts borrowed from the Cash Pool, and has accumulated an operating cash balance of \$30 million. Rates will remain at current levels until the new policies take effect, unless increased by the City Council or otherwise changed to pass through increases or decreases in Bonneville rates. See "Power Resources—Purchased Power Arrangements." The Department expects that the conditions which will allow the new financial policies to take effect will be met in mid-2004. See "Historical and Projected Operating Results." The Department's financial policies are subject to change by the City Council.

CUSTOMERS, ENERGY SALES AND REQUIREMENTS AND PEAK LOADS

Service Area

The Department's 131 square-mile service area consists of the City plus areas extending three to four miles north and south of the city limits. Because of these geographic limitations, the growth of the Department's electric load has resulted exclusively from development within the service area.

Sales to customers located outside the City's boundaries but within the service area represent approximately one-sixth of retail energy sales and revenues. The Department has franchise agreements with King County and the City of Tukwila that extend until 2007 and 2008, respectively. The Department also has franchise agreements with the cities of Shoreline, Burien, Lake Forest Park, and SeaTac that expire in 2015 and 2016. These six jurisdictions represented over 99 percent of the Department's retail energy sales outside the City in 2001. The Department's service area also includes portions of the cities of Normandy Park and Renton.

The terms of the franchises granted by the cities of Shoreline, Lake Forest Park, SeaTac, and Burien require the Department to make payments to these cities in amounts equal to six percent of the unbundled power portion of rate revenue derived from customers in these jurisdictions. Payments can be increased to six percent of total rate revenue at the request of the city granting the franchise. The franchises allow the cities to request levels of service in such areas as streetlighting and undergrounding that exceed standards generally applicable throughout the service area but provide that incremental costs related to such higher service levels will be recovered from customers in the requesting city. The franchises also limit the amount by which the average rates charged to customers in the cities, exclusive of any additional charges related to higher service levels, can exceed the average rates charged to customers in the City to eight percent of the unbundled power portion of such rates.

Largest Customers

The Department's ten largest customers in 2000, in order of their maximum kW demand, were Birmingham Steel Company (recently acquired by Nucor Corporation), the Boeing Company, the University of Washington, the United States Government, the Jorgensen Forge Corporation, the City of Seattle, Saint Gobain Containers, Unico Properties/Union Square Ltd., Sabey Corporation, and King County. These customers accounted for approximately 15.3 percent of retail energy sales and 13.0 percent of retail energy revenues in 2000. The load factors of these customers ranged from 9.4 percent to 82.6 percent, with an average load factor of 43.6 percent.

Historical Sales

Energy sales in the Department's service area can be affected by variations in weather conditions. In winter months, colder than normal weather patterns can result in higher loads, due to the extensive use of electricity for heating. However, warmer than normal conditions in summer months do not lead to significant increases in load because of the limited use of residential air conditioning. Temperatures in the service area were near normal in 1999, 2000 and 2001. From February through May 2002, temperatures were below normal.

From 1991 through 2000, retail energy sales within the Department's service area increased at an average rate of 0.8 percent per year. In 2001 energy sales were 5.1 percent below the 2000 level. The amount of energy consumed by retail customers in 2001 was influenced by the Department's public appeal for reduced consumption, the price response to a series of substantial rate increases, the local effects of the general economic downturn, and the events of September 11, 2001.

Total sales of energy to residential customers, which constituted 34.0 percent of the Department's energy sales in 2001, have been relatively stable over the 1991-2000 period, despite a 1.1 percent average annual increase in the number of customers during this period. The declining level of consumption per customer reflects smaller household size, fuel-switching, the effect of domestic conservation efforts, and enhanced energy efficiency elements of building codes. In 2001, the combined effect of the factors mentioned in the preceding paragraph was a reduction of 6.6 percent in residential consumption.

Commercial and governmental customers accounted for 52.2 percent of total sales in 2001. Sales growth in these customer classes has averaged 1.6 percent annually from 1990 to 2000. Consumption by commercial and governmental customers fell by 3.2 percent in 2001.

The industrial customers served by the Department represented 13.8 percent of retail sales in 2001. Sales to this sector have exhibited a slight downward trend over the period 1991-2000, declining at an average annual rate of 0.3 percent. In 2001, sales to industrial customers were 8.5 percent below the 2000 level. The local economic recession and the increase in energy prices were major factors in this decline. Two of the utility's largest industrial customers agreed to "compensated interruption" during the period from December 2000 through September 2001 at times when the utility faced high market prices. These customers were compensated for 39,914 MWh of interrupted service over this period.

A record peak load of 2,059,566 kW was recorded in December 1990 due to unusually cold weather. The 2001 peak load was 1,661,842 kW and occurred in February.

New Large Loads

During 2000, several new and existing non-residential customers requested service from the Department for facilities providing services to high-technology sectors of the economy. The density of the loads, measured in terms of kilowatts per square-foot, was several times greater than that of ordinary office space. The power requirements of these customers is on the scale of industrial processes, but unlike typical industrial loads that fluctuate through time, these new loads are relatively constant. The City Council has created a new customer class for such loads and has established guidelines for setting rates for such customers that are intended to recover the full cost of providing service. See "The Department—Retail Rates."

Due to the recession in the high-technology sector of the local economy, the anticipated increase in demand from New Large Loads has not yet materialized. No customers are being served as New Large Loads.

Load Forecast (2002-2007)

The Department's ongoing planning activities include the annual preparation of a forecast of firm system load, derived from a forecasting model that assumes average weather conditions and includes other independent demographic and economic variables developed from an historical service area database. The most recent load forecast presented in the table "Retail Customers, Energy Sales, Peak Demand, and Energy Requirements" incorporates the estimated impact on load of adopted and projected rate changes, the Department's conservation programs and the residual effects of the Department's efforts to reduce electricity consumption during 2001. See "The Department—Retail Rates."

The forecast of system load for the 2002-2007 period is based on actual experience through September 30, 2002. The decline in load that began in late 2000 ended in the second quarter of 2002. Weather-adjusted load for the March-June 2002 quarter was at the same level as in the same quarter of 2001. Weather-adjusted load in the third quarter of 2002 was 1.9 percent higher than in the same period in 2001. Average load in 2002 is expected to be 0.5 percent higher than in 2001. From 2002 through 2007, load is expected to increase at an average annual rate of 1.2 percent.

Sales to residential customers are expected to increase at an average annual rate of 0.5 percent from 2003 through 2007. The projected increase of 1.0 percent per year in the number of residential customers is expected to be partially offset by a reduction in average consumption per customer. Sales to commercial and governmental customers are projected to increase at an average rate of 1.8 percent per year over the same period. As the region emerges from the economic slowdown of 2001-2002, sales to the industrial sector are expected to return to the 1999 level by 2007, implying an annual growth rate of 2.0 percent over the 2003-2007 period. The table below provides a summary of historical and projected customers and energy sales and requirements.

RETAIL CUSTOMERS, ENERGY SALES, PEAK DEMAND, AND ENERGY REQUIREMENTS

	Actual			Projected					
	1999	2000	2001	2002	2003	2004	2005	2006	2007
Average Number of Customers ⁽¹⁾									
Residential	312,849	316,758	322,707	325,523	328,384	331,380	334,543	337,788	341,171
Commercial	30,568	30,838	30,934	30,934	30,934	30,934	30,934	30,934	30,934
Governmental ⁽²⁾	1,817	1,686	1,776	1,776	1,776	1,776	1,776	1,776	1,776
Industrial	279	276	259	259	259	259	259	259	259
Total Customers	345,234	349,282	355,676	358,492	361,353	364,349	367,512	370,757	374,140
Energy Sales (MWh)									
Residential	3,340,768	3,267,710	3,050,899	3,127,631	3,054,593	3,070,572	3,086,634	3,102,781	3,119,012
Commercial	3,714,041	3,932,043	3,829,358	3,775,800	3,812,813	3,859,313	3,906,379	3,954,019	4,002,241
Governmental	987,768	908,283	858,451	846,955	876,729	911,820	948,315	986,270	1,025,744
Industrial	1,355,316	1,352,457	1,237,083	1,222,795	1,273,741	1,299,572	1,325,927	1,352,817	1,380,252
Total Energy Sales ⁽³⁾	9,397,893	9,460,493	8,975,791	8,973,181	9,017,876	9,141,277	9,267,255	9,395,887	9,527,249
Peak Demand (MW) ⁽⁴⁾	1,730	1,769	1,662	2,027	2,031	2,094	2,163	2,198	2,198
Energy Requirements (MWh)									
Total Energy Sales	9,397,893	9,460,493	8,975,791	8,973,181	9,017,876	9,141,277	9,267,255	9,395,887	9,527,249
Energy used in Operation	36,207	35,294	32,144	30,660	30,660	30,744	30,660	30,660	30,660
Energy for Public Lighting ⁽²⁾	0	78,436	78,741	80,513	81,513	82,771	83,514	84,514	85,514
System Losses ⁽⁵⁾	573,170	460,472	392,240	437,357	437,222	472,557	454,296	461,491	467,862
Total Energy Requirements ⁽⁶⁾	10,007,270	10,034,695	9,478,916	9,521,711	9,567,271	9,727,349	9,835,725	9,972,552	10,111,285

- (1) The Department's forecast projects an increase in the number of residential customers but no change in the number of customers in other classes.
- (2) In 1999, energy delivered to governmental customers included energy for streetlighting in the City, which was paid for by the City from general revenues. In 2000 the cost of streetlighting was allocated to all retail customers in the City and was recovered through the rates charged to those customers. Beginning in 2000, energy for streetlighting in the City is shown separately on this table as "Energy for Public Lighting."
- (3) Energy sales in the Department's service area only.
- (4) Actual data reflect one-hour peak load. Projections reflect the 16-hour peak load under extremely cold weather conditions.
- (5) Includes transmission and distribution losses.
- (6) Firm energy required in the Department's service area.

RECENT DEVELOPMENTS IN THE ELECTRIC UTILITY INDUSTRY

The electric utility industry in the United States has been in a period of change, resulting from actions taken by legislative and regulatory bodies at the national, regional and state levels. The National Energy Policy Act of 1992 (the “Energy Act”) and subsequent orders issued by the Federal Energy Regulatory Commission (“FERC”) require utilities under FERC’s jurisdiction to provide wholesale power suppliers with non-discriminatory, open access to transmission facilities. The result has been greater competition in the wholesale electricity market. Although the Energy Act explicitly prohibited FERC from requiring open access to power suppliers at the retail level (“retail wheeling”), many states have passed legislation or implemented regulations providing for varying degrees of retail wheeling. However, turbulence in the wholesale power market in the Western United States in 2000 and 2001 reduced the pressures for legislation related to deregulation. In Washington State, legislation to restructure the electric utility industry has not received serious consideration since 1997.

Regional Transmission

In 1999, FERC issued its Order 2000, which set forth certain guidelines and incentives for the formation of Regional Transmission Organizations (“RTOs”). In compliance with FERC Order 2000, Bonneville and nine investor-owned utilities in the Northwest have made various filings with FERC regarding the formation of a regional RTO (“RTO West”) that would assume operational responsibility for transmission facilities in the Pacific Northwest under standardized tariffs. The Department depends on contractual arrangements with transmission owners, principally Bonneville, for the transmission of power from Boundary and other generating facilities and for the Department’s wholesale market transactions. The Department therefore would be affected by the establishment of RTO West. The Department has joined other regional utilities in opposing the establishment of RTO West as currently proposed. The Department cannot predict whether efforts to form an RTO will ultimately be successful, and if successful, what the impact will be on the Department’s access to regional transmission facilities and the cost of such access. See “Power Resources—Transmission.

Standard Market Design

In July 2002, FERC issued a Notice of Proposed Rule-Making (“NOPR”) setting forth standards for the provision of transmission services and the operation of wholesale energy markets in the United States. Under the Standard Market Design (“SMD”) described in the NOPR, transmission services in each region would be provided by an independent transmission provider. Transmission providers would offer a single form of transmission service, Network Access Service, based on an open access tariff. Transmission users would pay an access charge which would be sized to recover the embedded transmission costs of the transmission owners. Parties with existing contracts for transmission services would have the option of converting their contracts to Network Access Service or retaining their rights under the existing contracts. The independent transmission providers would operate both day-ahead and real-time energy markets to manage congestion. Prices would be established at each node of the transmission grid to reflect the cost of congestion. Load-serving entities would be required to demonstrate that they have access to power resources that are sufficient to meet future peak demand. The SMD also includes provisions for market monitoring and oversight and for governance of the independent transmission providers.

Strong opposition to the proposed SMD has been expressed by state elected officials and regulatory agencies in the Northwest and the Southeast United States. The Department has also stated its opposition to the SMD because, in the opinion of the Department, the uniform standards proposed by FERC do not take into account the unique features of the Northwest power system, with its heavy dependence on hydroelectric generation. The Department cannot predict the outcome of the deliberations regarding the SMD or the effects on the Department if the SMD is adopted.

THE WESTERN POWER CRISIS

In 2000 and 2001, electric utilities in the Western United States, including the Department, were subject to a number of unprecedented developments that had severe negative effects on their financial results. Key factors in the events of the past two years were: (i) restructuring of the electric utility industry in the State of California, (ii) price volatility in wholesale markets for electricity and natural gas, and (iii) water conditions in the 2000-01 water year that were among the lowest ever recorded in the Northwest region.

Utility Industry Restructuring in California

As required under a 1996 law, the State of California restructured its electric utility industry in ways which were expected to improve the efficiency of the wholesale electricity market in California. These expectations were not realized. Growth in demand outstripped available supply, which was depressed by an unusually high level of plant outages in the spring of 2000. Defects in the design of California's deregulation efforts created the potential for manipulation of market prices by entities with market power. Power emergencies and rolling blackouts occurred frequently during the period from May 2000 through April 2001. With rates frozen, investor-owned utilities were unable to recover their costs and experienced severe cash flow pressures.

Price Volatility in Wholesale Energy Markets

From May 2000 to April 2001, prices in California wholesale markets increased to unprecedented levels. The sharp rise in wholesale prices spread from California throughout the western region. Increases in the price of natural gas, the major fuel for thermal generation of electricity in the western region, exacerbated the pressures on price emanating from the California market. Wholesale market prices, as measured by the Dow-Jones Mid-Columbia Index for peak period transactions, rose by a factor of ten, from an average of \$27 per MWh in the first quarter of 2000 to \$272 per MWh in the first quarter of 2001. FERC initially declined to intervene in the western power market to control prices, but with major power shortages and continued high prices predicted for the summer of 2001, FERC instituted a price mitigation and monitoring plan on June 19, 2001, that set upper limits on prices in the western region. By that time reductions in the demand for power and the appearance of new power supplies in the market had already caused prices to decline from their peak levels. Prices continued to fall through the remainder of 2001 and into the first quarter of 2002. From January through May 2002, spot market prices were at levels more consistent with experience prior to 2000. In June and July improved water conditions together with a delayed spring runoff resulted in an increase in the amount of surplus energy available in the Northwest. As a result, spot prices fell to the \$9-10 per MWh range in June and July. Prices returned to more normal levels in August and September.

Adverse Water Conditions in the Northwest

Water conditions in the hydroelectric operating year beginning October 1, 2000, were among the lowest ever recorded in the Pacific Northwest, which relies on hydroelectric generation for about 70 percent of its power resources. Under normal water conditions, the Department's hydroelectric resources generate 813 average MW of power. In calendar year 2001, the Department's hydroelectric output was 450 average MW, or 55 percent of normal. Having just completed its rate case in May 2000 with a Record of Decision ("ROD") that provided for moderate increases in rates for the next five years, Bonneville was forced to announce that it would have to raise its rates sharply in response to the low water conditions and high market prices.

The Effect on the Department

The Department's reliance on the wholesale power market was greater than normal in 2000 and the first nine months of 2001 because of decisions made by the Department in 1996 to limit its purchases of power from Bonneville through October 31, 2001, and in 2000 to sell its eight percent share of the Centralia Steam Plant. Each of these decisions had the effect of requiring the Department to purchase more energy in the wholesale market to meet load. The amount of the purchase requirement increased as water conditions worsened in the water year beginning October 1, 2000. The combination of high market prices and poor water conditions had a severe impact on the Department's financial status in 2000 and 2001. In 2000 and 2001, the Department incurred net costs of \$558.4 million for its wholesale market purchases and sales, an amount which exceeded estimates made in 1999 for rate-setting purposes by \$538.8 million.

THE CITY'S RESPONSE TO THE WESTERN POWER CRISIS

Actions Taken by the Department

The Department took action in 2001 and 2002 in a number of areas to deal with the impact of its unexpectedly high power costs.

- (i) The Department requested, and the City Council granted, four separate rate increases in 2001, on January 1, March 1, July 1, and October 1. The cumulative effect of these actions was an increase of 58 percent in average system rates. See "The Department—Retail Rates."
- (ii) In adopting the March 1, 2001, and July 1, 2001, rate increases, the City Council by ordinance required the Department to pass through to customers the effects of increases or decreases in power rates charged by Bonneville. The October 1, 2001, increase passed through the effect of the 46 percent increase in Bonneville rates that took effect on that date. On April 1, 2002, the Department lowered average rates by 1.1 percent to pass through a reduction in Bonneville's rates. Future changes in Bonneville's application of the Cost Recovery Adjustment Clause ("CRAC") will be passed through to the Department's customers without further authorization by the City Council. See "Power Resources—Purchased Power Arrangements—Bonneville Power Administration."
- (iii) The Department increased its target for conservation savings and carried out an intensive public information campaign to encourage customers to reduce their use of electricity. As a result of these efforts, and in response to the increase in rates, consumption of electricity by retail customers in the Department's service area fell by 5.1 percent from 2000 to 2001, thereby reducing the need to buy power in the wholesale market.
- (iv) The Department obtained additional sources of power by signing a new contract with Bonneville effective October 1, 2001, and by contracting to purchase power from the Klamath Falls Cogeneration Project and the State Line Wind Project. Firm and nonfirm power available under the new Bonneville contract was estimated to be almost 600 average MW, more than three times the amount available under the prior contract with Bonneville. The contract with the City of Klamath Falls provides 100 MW of power from a combustion turbine through June 30, 2006. The State Line Wind Project will provide 17.8 average MW of energy in 2002 and 33.7 average MW in 2003. Energy from wind generation is expected to increase to 56.4 average MW beginning in 2004. With the additional power from these resources, the Department expects to have surplus power available even under critical water conditions for the next several years.
- (v) In March 2001, the Department issued \$503.7 million in long-term bonds to finance its capital requirements, to refinance and restructure certain outstanding bonds and to reimburse the Department's operating account in the amount of \$110.0 million for capital expenditures previously funded from operating revenues.
- (vi) In April 2001, the Department issued \$182.2 million of its 2001 Notes to fund the anticipated operating cash flow deficit in 2001.
- (vii) In December 2001, the City Council passed an ordinance authorizing a loan of up to \$110.0 million to the Department from the City's Cash Pool to cover a cash flow deficit that exceeded the projections on which the sale of the 2001 Notes was based. As of December 31, 2001, the Department's borrowing from the Cash Pool amounted to \$100,000,000. By October 31, 2002, the amount outstanding had fallen to \$78.3 million.
- (viii) In December 2001, the City Council approved a resolution establishing new financial policies to be used by the Department in setting rates. In the near term the new policies require that current rates remain unchanged, unless increased by the City Council or changed to pass through changes in Bonneville rates, until all short-term borrowing has been repaid and the balance in the Department's operating account has reached a level of \$30 million. At that time new rate-setting guidelines will take effect that will require rates to be set at higher levels than the former policies in order to provide greater protection against unfavorable developments in wholesale power markets. See "The Department—Financial Policies."

- (ix) In June 2002, bonds issued by irrigation districts in Idaho to finance the construction of the Lucky Peak Project were refinanced, with present value savings of \$5.4 million. The Department is responsible for paying debt service on the bonds under a power purchase contract. Savings from the refunding will improve the Department's cash position in 2002 and 2003.
- (x) The Department plans to use the proceeds of the 2002 Notes to repay the outstanding balance on its loan from the City's Cash Pool and to finance future cash flow deficits, thereby reducing interest costs by \$1.0 million to \$1.5 million.
- (xi) The Department plans to use the proceeds of the Bonds to refinance all of its outstanding 1992B Bonds and a portion of its outstanding 1993 Bonds in November 2002, generating additional savings in debt service costs.

Largely as a result of the actions listed above and the return of normal water conditions to the Northwest, the Department's financial performance in 2002 has been favorable. Cash flow from operations has been positive in 2002. Through October 31, 2002, the Department generated \$109.1 million in operating cash flow, of which \$91.1 million was deposited to the Note Account to fund the repayment of one-half of the principal amount of the 2001 Notes due on March 28, 2003, and \$18.0 million was used to reduce the amount owed to the Cash Pool. Two additional deposits to the Note Account for payment of the principal on the 2001 Notes, each in the amount of \$45.5 million, are required to be made on January 1 and March 28, 2003. Assuming normal water conditions, the Department expects to pay all of its short-term debt obligations, including the Notes, by the end of the second quarter of 2004.

Pending Litigation Before FERC

In two cases currently before FERC, the City is seeking refunds of amounts paid for electricity. Both cases arose from FERC's investigation of the extremely high prices experienced in the California energy markets beginning in May 2000 and continuing into the summer of 2001, which led FERC to issue an order on July 25, 2001 (the "Order").

The Order required a hearing to determine refunds in the California markets operated by the California Independent System Operator and the California Power Exchange. Hearings have been completed and post-hearings briefs submitted. The Order also required a preliminary hearing to determine whether refunds should be ordered for transactions in the Pacific Northwest markets. The first stage of that hearing has been completed. In September 2001, the administrative law judge issued proposed findings and preliminary recommendations stating that prices were not unreasonable or unjust and refunds should not be ordered. The City has filed a brief urging FERC to reject the recommendations and to recognize that the unreasonable prices in California directly affected prices in the Pacific Northwest. However, FERC has yet to act on either the administrative law judge's recommendations or on any other party's response to those recommendations. Supplemental briefs were filed by the City and other parties in the wake of Enron's revelation of market manipulation strategies in California.

The City also is involved in other legal actions relating to the failure of the California Independent System Operator to pay the Department for power deliveries in the fall of 2000 and the bankruptcy filings of the California Power Exchange, Pacific Gas and Electric Company and Enron. Finally, the City has filed a request to intervene in a FERC investigation of companies that may have cooperated with Enron in transactions designed to adversely affect the California and West Coast markets.

None of these actions is expected to materially adversely affect the financial condition of the Department.

External Reviews of the Department

In May 2002, the Mayor appointed a six-member panel to examine the Department's practices and strategies in the areas of power management, resource acquisition, risk management, and financing, and to recommend any changes in the Department's governance that the panel considered appropriate. In October 2002, the panel submitted a report which included a number of recommendations concerning governance and oversight of the Department. The recommendations included a proposal to establish an advisory committee consisting of five to seven individuals with expertise in the electric utility industry. The responsibilities of the committee

would be purely advisory; governance of the Department would remain the responsibility of the Mayor and the City Council. The panel also recommended that the City Council and Mayor's office increase the level of resources devoted to oversight of the Department and establish clear policies for power management and risk management. The Mayor has indicated support for the panel's recommendations regarding the establishment of an advisory committee and has established a new staff position in his office to deal with the Department's issues.

In March 2002, the City Council directed the City Auditor to retain the services of a consultant to review the Department's policies and performance in the areas of financial management, risk management and governance. The consultant's report, submitted to the Council on October 31, 2002, criticized the Department's financial and risk management practices. The report took note of the increase in the level of the Department's debt over the past decade and recommended financial policies that would reduce reliance on debt to finance capital requirements. In addition, the report recommended various approaches to strengthen the Department's risk management function, including the establishment of mechanisms to limit the Department's exposure to price variability in the wholesale market and the use of risk analysis in strategic planning and other decision-making functions. The report did not propose any changes to the basic governance structure of the Department, but recommended the establishment of a utility review board to strengthen oversight. The Department's Superintendent has accepted the report's recommendations and submitted a work plan to address the major findings.

POWER RESOURCES

Overview of Resources

The Department typically meets the majority of its energy requirements from its own power resources. These include four large and three small hydroelectric facilities which generate 7,117,981 MWh of energy, about 49 percent of the energy available to the Department from its owned and contracted resources, under average water conditions. In 2001, these hydroelectric facilities supplied only 3,941,388 MWh of energy, or 37 percent of the energy available to the Department in that year because water conditions were the second driest on record. In 2000 and 2001, the Department contracted for over 400 average MW of additional firm power from Bonneville, the Klamath Falls Cogeneration Project, and the State Line Wind Project. With the additional power from these resources, the Department expects to have surplus power available even under critical water conditions for the next several years.

Purchases of energy from Bonneville provided 22 percent of available energy in 2001, reflecting a substantial increase in purchases from Bonneville when the new power sales contract with Bonneville took effect on October 1, 2001. The remaining 41 percent of energy used by the Department in 2001 was provided through long-term contracts with other power sources (18 percent) and through short-term purchases in the wholesale power market (23 percent). The average cost of energy available to the Department in 2001 from all sources was \$62.26 per MWh, excluding transmission and depreciation. The average cost of power in 2001 was unusually high because the Department was required to buy additional amounts of energy in the wholesale power market in the first three quarters of the year at extraordinarily high prices to compensate for the shortfall in hydroelectric production resulting from subnormal water conditions. Water conditions and market prices returned to normal levels in the 2001-2002 water year (October 1, 2001, through September 30, 2002). The average cost of power in calendar year 2002 is projected to be \$14.28 per MWh.

Under the Pacific Northwest Coordination Agreement (the "Coordination Agreement"), the Department and 15 other public and investor-owned utilities in the Northwest have agreed to coordinate the operation of their power generation systems to maximize the firm capability and reliability of the coordinated system. The Coordination Agreement went into effect in 1965 and will terminate on September 24, 2024. Under the terms of the Coordination Agreement, the firm capability of the generating resources of the parties to the agreement is calculated with reference to a critical period, which is defined as the multi-month period of adverse streamflows of historical record during which the amount of firm load that could be served by the firm resources of the parties to the Coordination Agreement (the "Critical Period") was at a minimum. Water conditions would be expected to be better than those of the Critical Period about 95 percent of the time.

The table below provides an overview of the Department’s power resources.

OWNED AND CONTRACTED POWER RESOURCES IN 2003

	One-Hour Peak Capability (MW)	Energy Available Under Critical Water Conditions (MWh) ⁽¹⁾	Energy Available under Average Water Conditions (MWh) ⁽²⁾	Year FERC License Expires
Department-Owned Resources				
Boundary	1,055	2,985,408	4,293,017	2011
Gorge	177	864,612	985,324	2025
Diablo	159	733,212	844,395	2025
Ross	360	657,000	848,343	2025
Newhalem	2	13,613	13,613	2027
Cedar Falls ⁽³⁾	30	47,304	81,512	N/A
South Fork Tolt	17	51,777	51,777	2028
Contract Resources				
Bonneville	1,161 ⁽⁴⁾	4,185,022	4,991,295	N/A
Box Canyon	12	78,840	78,840	2005
Priest Rapids	68	302,424	369,370	2005
CSPE	21	26,350	26,350	N/A
GCPHA	64 ⁽⁵⁾	236,863	236,863	2030/2031
High Ross	298 ⁽⁶⁾	310,246	310,246	N/A
Lucky Peak	113	249,082	337,233	2030
Metro Cogeneration	1	10,512	10,512	N/A
Klamath Falls	100	744,600	744,600	N/A
State Line Wind Project	50	282,294	28,294	N/A

- (1) Critical water conditions represent the lowest sequence of streamflows experienced in the Northwest region over a historical period of record (1929-1978). The firm energy capability of hydroelectric resources is the amount of energy that would be produced under critical water conditions. Actual water conditions would be expected to be better than critical water conditions about 95 percent of the time.
- (2) Figures in this column represent the average amount of energy that would be produced over all of the water conditions in the period of record (1929-1978).
- (3) The Cedar Falls Hydroelectric Plant is not subject to FERC licensing requirements.
- (4) Approximate. Through purchase of the Slice product, the Department is entitled to 4.6676 percent of the actual output of the Federal System. The Department is also entitled to purchase 155 average MW of Block power (as defined below under “Purchased Power Arrangements—Bonneville Power Administration”) from Bonneville in 2003.
- (5) The Department’s 50 percent share of installed capacity.
- (6) The Department’s contract with the Province of British Columbia provides capacity from November through March in an amount equal to 532 MW minus the actual capacity of the Ross Powerhouse.

Resource Acquisitions

In 1996 the Department completed a Strategic Resources Assessment (“SRA”) in which it recommended a strategy of reliance on purchases of power in the wholesale market to fill the gap between loads and resources in the near term. In the first half of 2000 the Department published an update to the SRA which recommended that the Department pursue a number of alternative power sources and demand-side management options to meet its load requirements beyond 2000. Specifically, the SRA update recommended that the Department maximize its purchases of Bonneville power under a new power sales contract that was to take effect on October 1, 2001; purchase as much Bonneville power as possible in the form of the Slice-of-the-

System product (the “Slice”) (see “Purchased Power Arrangements—The Bonneville Power Administration”); pursue a power sales contract of 100 MW from the Klamath Falls Cogeneration Project to replace power previously supplied by the Centralia Steam Plant (see “Purchased Power Arrangements—Klamath Falls Cogeneration Project”); increase the level of conservation savings to be acquired through 2010 (see “Conservation”); and acquire an estimated 100 average MW of new non-hydro renewable resources (see “Purchased Power Arrangements—Wind Generation” and “—Other Renewable Resources”). The City Council approved the recommendations of the 2000 SRA update, and the Department has acquired the recommended resources.

Resource Capabilities and Costs

The following tables show the actual and projected availability and projected cost of resources that are in the Department’s current plan to meet its net energy requirements through 2007. Projections for 2002 take into account actual water conditions through September 2002, which have been about average. Output projected for the years beyond 2002 represent the average output that would be realized over all water conditions experienced in the 1929-1978 period, the period generally used for purposes of regional power planning. The tables contain projections that are based on assumptions about future events. Actual conditions may differ from those assumed, resulting in actual results that vary from those projected.

ENERGY RESOURCES

	Actual			Projected ⁽¹⁾					
	1999	2000	2001	2002	2003	2004	2005	2006	2007
Department-Owned Generation									
Boundary	4,465,874	3,809,267	2,339,590	4,053,928	4,293,017	4,301,738	4,290,778	4,282,263	4,291,122
Gorge	1,186,500	959,800	616,754	1,103,003	985,324	989,167	986,045	985,197	985,236
Diablo	1,022,509	814,712	477,635	966,925	844,395	848,083	845,102	844,453	844,531
Ross	962,487	741,637	392,922	922,889	848,343	852,947	848,744	846,074	848,590
Cedar Falls/Newhalem	71,019	53,780	74,430	108,700	95,125	95,446	95,125	95,125	95,125
Centralia ⁽²⁾	689,802	277,103	0	0	0	0	0	0	0
South Fork Tolt	70,495	44,090	40,057	75,520	51,777	51,912	51,777	51,777	51,777
Subtotal	8,468,686	6,700,389	3,941,388	7,230,965	7,117,981	7,139,293	7,117,571	7,104,889	7,116,381
Energy Purchases									
Bonneville ⁽³⁾	1,582,163	1,701,674	2,384,896	4,574,169	4,991,295	5,007,243	4,990,270	5,282,400	5,994,273
Box Canyon	70,759	57,746	42,663	78,840	78,840	79,056	45,656	0	0
Priest Rapids	412,482	363,740	262,188	328,626	369,370	371,070	309,397	45,960	46,000
CSPE	141,117	106,603	102,037	99,358	26,350	0	0	0	0
GCPHA	250,663	238,987	271,009	252,658	236,863	236,863	236,863	236,863	236,863
High Ross	308,353	296,828	307,738	302,531	310,246	312,773	311,020	309,726	311,474
Lucky Peak	426,152	340,825	188,403	288,147	337,233	337,322	337,233	337,233	337,233
Metro Cogeneration	7,553	7,419	11,915	13,478	10,512	10,541	10,512	10,512	8,760
Klamath Falls	--	--	326,104	697,948	533,708	545,025	380,573	106,938	--
Wind Resources	--	--	--	148,655	282,294	460,185	494,014	494,014	494,014
Seasonal Exchange Received	183,968	287,066	395,146	208,538	145,946	109,417	108,604	107,926	108,499
Wholesale Market Purchases ⁽⁴⁾	1,393,718	2,571,228	2,417,907	752,454	61,317	60,579	154,286	118,921	62,719
Subtotal	4,776,928	5,972,116	6,710,006	7,745,402	7,383,974	7,530,074	7,378,428	7,050,493	7,599,835
Total Department Resources	13,245,614	12,672,505	10,651,394	14,976,367	14,501,955	14,669,367	14,495,999	14,155,382	14,716,216
Minus Offsetting Energy Sales:									
Firm Energy Sales and Marketing Losses ⁽⁵⁾	219,793	249,321	255,505	446,782	470,863	444,445	508,197	555,848	558,300
Out of System Sales	89,907	96,399	15,956	0	0	0	0	0	0
Seasonal Exchange Delivered	255,102	269,030	376,950	231,650	127,830	90,846	90,623	90,623	90,329
Wholesale Market Sales	2,673,542	2,023,060	524,067	4,776,224	4,335,991	4,406,727	4,061,454	3,536,359	3,956,302
Total Net Energy Resources ⁽⁶⁾	10,007,270	10,034,695	9,478,916	9,521,711	9,567,271	9,727,349	9,835,725	9,972,552	10,111,285

Footnotes to Table:

- (1) Projections for 2002 are based on actual precipitation through September 2002. Projections for the final quarter of 2002 and for the 2003-2007 period assume average water conditions.
- (2) The Centralia Steam Plant was sold in May 2000.
- (3) From 1999 through September 30, 2001, the amount of power purchased under the Bonneville contract was limited to 195 average MW. Energy from Bonneville over the 2002-2007 period is based on the new Block and Slice Power Sales contract which took effect on October 1, 2001. See “Power Resources—Purchased Power Arrangements—Bonneville Power Administration.”
- (4) Purchases to compensate for low water conditions and to make up the difference between loads and resources. In 2000 and 2001, the Department’s purchases of power in the wholesale market were unusually large, due to poor water conditions.
- (5) Energy provided to Public Utility District No. 1 of Pend Oreille County under Article 49 of the Boundary Project’s FERC license and to compensate the PUD for the Boundary Project’s encroachment on Box Canyon. From 2002 through 2007, figures on this line also include incremental losses due to expanded activity in the wholesale market.
- (6) Firm energy required in the Department’s service area.

COST OF POWER SUPPLY
(\$000)

	Actual			Projected					
	1999	2000	2001	2002	2003	2004	2005	2006	2007
Wholesale Market Purchases ⁽¹⁾	\$ 34,296	\$ 212,402	\$ 524,422	\$ 13,637	\$ 1,989	\$ 1,620	\$ 4,137	\$ 3,017	\$ 1,946
Other Power Purchases:									
Bonneville ⁽²⁾	\$ 33,089	\$ 34,443	\$ 66,824	\$ 134,779	\$ 154,805	\$ 150,465	\$ 154,790	\$ 157,966	\$ 152,354
Box Canyon	1,467	998	1,267	991	1,042	1,068	633	0	0
Priest Rapids	2,268	2,136	2,303	2,319	2,551	2,618	2,520	1,734	1,712
GCPHA	8,422	8,406	8,465	5,085	4,206	4,845	2,171	2,225	2,281
CSPE	--	--	--	--	--	--	--	--	--
High Ross	22,440	13,342	13,353	13,362	13,366	13,374	13,385	13,392	13,399
Lucky Peak	17,361	16,985	15,978	12,216	12,661	17,670	17,658	17,712	10,788
Metro Cogeneration	242	238	381	753	390	390	400	409	419
Klamath Falls	0	0	18,460	38,604	29,164	30,828	28,084	11,538	0
State Line Wind Project	0	0	0	8,011	10,787	18,215	19,631	19,631	19,631
Int and Ex of Wind Resources	0	0	0	2,253	5,245	5,346	5,429	5,516	5,604
Overdraft and Load Factoring	343	0	0	0	15	15	15	15	16
Seasonal Exchange Received	(102)	6,287	27,895	4,837	4,598	3,546	3,607	3,672	3,778
Interchange Received	0	0	0	0	0	0	0	0	0
BPA Billing Credits ⁽³⁾	(3,845)	(3,531)	(3,713)	(3,054)	(3,740)	(3,705)	(3,668)	(3,520)	(3,479)
Subtotal	\$ 81,684	\$ 79,305	\$ 151,213	\$ 220,156	\$ 235,091	\$ 244,675	\$ 244,653	\$ 230,289	\$ 206,503
Production:									
Centralia ⁽⁴⁾	\$ 14,098	\$ 7,274	\$ --	\$ --	\$ --	\$ --	\$ --	\$ --	\$ --
Hydro Projects ⁽⁵⁾	17,336	18,611	17,012	19,692	21,246	22,931	23,598	24,637	25,339
Control and Dispatch	4,146	5,285	6,065	6,174	6,322	6,493	6,653	6,813	6,976
Subtotal	\$ 35,580	\$ 31,170	\$ 23,077	\$ 25,866	\$ 27,568	\$ 29,424	\$ 30,251	\$ 31,450	\$ 32,315
Total Power Supply Expense	\$ 151,560	\$ 322,878	\$ 698,712	\$ 259,659	\$ 264,647	\$ 275,719	\$ 279,040	\$ 264,756	\$ 240,764
Minus Offsetting Power Revenue:									
Wholesale Power Sales	\$ 51,466	\$ 103,082	\$ 75,333	\$ 113,242	\$ 126,502	\$ 138,524	\$ 128,576	\$ 111,622	\$ 130,346
Other Power Sales ⁽⁶⁾	3,395	5,050	33,191	10,432	10,476	9,453	10,535	15,074	15,872
Net Cost of Power	\$ 96,699	\$ 214,746	\$ 590,188	\$ 135,985	\$ 127,669	\$ 127,741	\$ 139,929	\$ 138,059	\$ 94,547
Total Energy Requirement (MWh)	10,007,270	10,034,695	9,478,916	9,521,711	9,567,271	9,727,349	9,835,725	9,972,552	10,111,285
Average Unit Cost (Dollars/MWh) ⁽⁷⁾	\$ 9.66	\$ 21.40	\$ 62.26	\$ 14.28	\$ 13.34	\$ 13.13	\$ 14.23	\$ 13.84	\$ 9.35

Footnotes to Table:

- (1) Purchases to compensate for low water conditions and to make up the difference between loads and resources. Excludes wheeling costs. In 2000 and 2001, the Department purchased unusually large amounts of power in the wholesale market at high prices due to poor water conditions.
- (2) From 1999 through September 30, 2001, the amount of power purchased under the Bonneville contract was limited to 195 average MW. The cost of power from Bonneville over the 2002-2007 period is based on the new Block and Slice Power Sales contract which took effect on October 1, 2001. From 2003 through 2006, the forecast assumes the CRAC adjustments projected by Bonneville. The CRAC adjustments are assumed to be removed effective October 1, 2006.
- (3) Billing credits received from Bonneville for the South Fork Tolt Project.
- (4) The sale of the Centralia Steam Plant was completed in May 2000.
- (5) Includes operation and maintenance costs only.
- (6) Includes sales to Public Utility District No. 1 of Pend Oreille County under Article 49 of the Boundary Project license, seasonal exchange delivered and other energy credits.
- (7) Average cost of power supplied to service area customers after recognizing the net revenue or cost associated with wholesale power sales and purchases.

The Department's Resources

Boundary Hydroelectric Plant. The Boundary Project is located on the Pend Oreille River in northeastern Washington near the Canadian and Idaho borders, approximately 250 miles from Seattle. The plant was placed in service in 1967. It has a one-hour peak capability of 1,055 MW, and is expected to generate 4,053,928 MWh of energy in 2002, 94 percent of its expected annual output. The Boundary Project is operated under a Federal Energy Regulatory Commission ("FERC") license which expires on October 1, 2011. The Department plans to apply for renewal of its Boundary license.

The Boundary Project's FERC license requires that up to 48 MW of the Boundary Project's capacity be assigned, at cost, to Public Utility District No. 1 of Pend Oreille County ("Pend Oreille PUD"). Due to Pend Oreille PUD's increasing loads and other contractual requirements, the amount of Boundary Project power assigned to Pend Oreille PUD is expected to increase from its present 32 MW to the maximum allowable amount of 48 MW in August 2005.

For a discussion of the impacts of fisheries issues on this facility, see "Environmental Matters—Endangered Species Act Issues." Encroachment of British Columbia Hydro and Power Authority's ("B.C. Hydro") Seven Mile Project on the Boundary Project is discussed below under "Ross, Diablo and Gorge Hydroelectric Plants."

Ross, Diablo and Gorge Hydroelectric Plants. The Ross, Diablo and Gorge hydroelectric plants are located on a ten-mile stretch of the Skagit River above Newhalem, Washington, approximately 80 miles northeast of Seattle. Power is delivered to the Department's service area via two double-circuit Department-owned transmission lines. The Ross Plant, located upstream of the other two projects, has a reservoir with usable storage capacity of 1,052,000 acre-feet. Because the Diablo Plant, with usable storage capacity of 50,000 acre-feet, and the Gorge Plant, with usable storage capacity of 6,600 acre-feet, are located downstream from the Ross Dam, their operation is coordinated with water releases from the Ross Reservoir and the three plants are operated as a single system. The combined one-hour peak capability of the three plants is 696 MW. Energy output in 2002 is expected to be 2,992,817 MWh. Expected annual output from these three plants is 2,678,062 MWh, based on water conditions in the 1929-1978 period.

These plants form the Skagit Hydroelectric Project and are licensed as a unit by FERC. FERC-required independent inspections of the Skagit Project in 1992 revealed no deficiencies. In 1995, FERC issued a new 30-year license for operation of the Skagit Project. As a condition of the new license, the Department has taken and will continue to take various mitigating actions relating to fisheries, wildlife, erosion control, archeology, historic preservation, recreation, and visual quality issues.

Although the original plans for the Skagit Project had included raising the height of Ross Dam by 122.5 feet to maximize the hydroelectric potential of the plant, the Canadian province of British Columbia (the "Province") protested on environmental grounds. After a protracted period of litigation and negotiation, an agreement (the "High Ross Agreement") was reached under which the Province provides the Department with power equivalent to the planned increase in the output of the Ross Plant in lieu of the Department's construction of the addition, for 80 years commencing in 1986. The agreement is subject to review by the parties every ten years. The most recent review, concluded in 1998, did not result in any changes to the agreement.

The Department's annual payments to the Province include a fixed charge of \$21.8 million annually through 2020, which represents the estimated debt service costs that would have been incurred had the addition been constructed and financed with bonds. In 2000, the Department began amortizing the annual \$21.8 million payments over the period through 2035. Equivalent maintenance and operation payments and certain other charges began in 1986 and will continue for 80 years. The energy to be purchased under this agreement is 310,246 MWh annually. One-hour peak capability is 150 MW from April through October; from November through March, one-hour peak capability is equal to 532 MW minus the actual peak capability of the Ross Plant, given actual reservoir elevations behind Ross Dam.

If the Province discontinues power deliveries, the High Ross Agreement provides full authority to the Department to proceed with the originally proposed construction and obligates the Province to return to the Department sufficient funds to permit the Department to increase the height of Ross Dam and make other improvements as originally proposed. This obligation has been guaranteed by the Government of Canada.

As authorized in the High Ross Agreement, B.C. Hydro increased the reservoir elevation of its Seven Mile Project on the Pend Oreille River in the spring of 1988, thereby extending its reservoir across the international border to the tail-race of the Boundary Project. An 80-year contract between the City and B.C. Hydro was signed in 1989 to provide compensation to the Department for the encroachment of Seven Mile Reservoir on the Boundary Project.

Cedar Falls Hydroelectric Plant. The Cedar Falls Hydroelectric Plant (“Cedar Falls”), built in 1905, is located on the Cedar River, approximately 30 miles southeast of Seattle. Cedar Falls was constructed before the adoption of the Federal Water Power Act of 1920 and is not subject to licensing by FERC. Cedar Falls power is delivered through an interconnection with Puget Sound Energy. The one-hour peak capability of the plant is 30 MW. Energy generation in 2002 is expected to be 96,819 MWh.

Newhalem Hydroelectric Plant. The Newhalem Hydroelectric Plant (“Newhalem”), located on Newhalem Creek, a tributary of the Skagit River, was built in 1921 to supply power for the construction of the Skagit Project. The plant was rebuilt and modernized in 1970. It is operated under a FERC license which expires January 31, 2027. The plant’s power is delivered over Department-owned transmission lines. The one-hour peak capability of the plant is 0.5 MW. Energy generation in 2002 is expected to be 11,881 MWh.

South Fork Tolt River Hydroelectric Plant. The South Fork Tolt River Hydroelectric Plant (the “Tolt Project”) was placed in commercial operation in 1995. The Tolt Project operates under a 40-year FERC license which expires in 2028. The one-hour peak capability of the installed unit is 16.8 MW. Energy production from the Tolt Project in 2002 is expected to be 75,520 MWh. To reduce its cost of power from the Tolt Project, the Department entered into a Billing Credits Generation Agreement with Bonneville in 1993, under which Bonneville makes payments to the Department that have the effect of making the cost of power from the Tolt Project approximately equal to the cost of equivalent power from Bonneville. Payments to the Department under the agreement commenced in 1996.

Purchased Power Arrangements

In 2002, the Department expects to purchase approximately 47 percent of its total available system energy from other utilities in the region, including Bonneville, under long-term purchase contracts. Some of these agreements with other utilities provide that the Department is obligated to pay its share of the costs of the generating facilities providing the power, including debt service on bonds issued to finance construction, whether or not it receives any power. The Department has covenanted to treat payment of such costs as part of its purchased power expense and includes such costs in its operating and maintenance expenses.

The Department has in the past and may in the future purchase power under the Western Systems Power Pool Agreement and the Block and Slice Power Sales Agreement described immediately below. Those agreements include an obligation on the part of the Department to post collateral contingent upon the occurrence or nonoccurrence of certain future events within the control of the Department, such as future credit ratings or payment defaults. The Department also has entered, and may in the future enter, into agreements that include an obligation on the part of the Department to make payments or post collateral contingent upon the occurrence or nonoccurrence of certain future events that are beyond the control of the Department, such as future changes in gas prices. See discussion of the swap agreement under “Klamath Falls Cogeneration Project” in this section. Such obligations may be characterized as maintenance and operation charges, and thus would be payable from Gross Revenues of the Light System prior to the payment of debt service on the Notes.

The Bonneville Power Administration. Bonneville markets power from 30 federal hydroelectric projects, from several non-federally-owned hydroelectric and thermal projects in the Pacific Northwest and from various contractual rights with installed peak generating capacity of 24,080 MW and a firm energy capability of

approximately 8,500 average MW (the “Federal System”). These projects are built and operated by the United States Bureau of Reclamation (the “Bureau”) and the United States Army Corps of Engineers (the “Corps”) and are located primarily in the Columbia River basin. The Federal System currently produces approximately 45 percent of the region’s energy requirements. Bonneville’s transmission system includes over 15,000 circuit miles of transmission lines, provides about 75 percent of the Pacific Northwest’s high-voltage bulk transmission capacity and serves as the main power grid for the Pacific Northwest. Its service area covers over 300,000 square miles and has a population of about ten million. Bonneville sells electric power at cost-based wholesale rates to more than 130 utility, industrial and governmental customers in the Pacific Northwest. Bonneville also sells power directly to eight industrial customers in the region. Legally, Bonneville is required to give preference to government-owned utilities and to customers in the Northwest region in its wholesale power sales.

A 1982 contract with Bonneville entitled the Department to purchase power from Bonneville in amounts equal to the difference between the Department’s load and the firm generating capability of its owned and contracted resources. Effective August 1, 1996, this contract was amended to limit the amount of power purchased from Bonneville to 195 average MW in each operating year through September 30, 2001. This lower level of purchases from Bonneville was considerably less than the difference between the Department’s load and firm resources. For the remaining term of the contract, the Department filled this gap with purchases of power in the wholesale market.

A Block and Slice Power Sales Agreement with Bonneville covers purchases of power for the ten-year period beginning October 1, 2001. Under the contract, power is delivered in two forms: a shaped block (the “Block”) and a Slice. Through the Block product, power is delivered to the Department in monthly amounts shaped to the Department’s monthly net requirement, defined as the difference between the Department’s projected monthly load and the resources available to serve that load under critical water conditions. The original contract provided for delivery of 163.8 average MW annually as a Block for the period from October 1, 2001, through September 30, 2006, and 278.2 average MW from October 1, 2006, through September 30, 2011. Under the Slice product, the Department receives a fixed 4.6676 percent of the actual output of the Federal System and pays the same percentage of the actual costs of the system. Payments for the Slice product are subject to annual true-up adjustment to reflect actual costs. True-up payments are made in three equal monthly amounts in January, February and March of the year following the federal fiscal year to which the payments apply. Power available under the Slice product varies with water conditions, federal generating capabilities and fish and wildlife restoration requirements. Under the most recent estimates of the capability of the Federal System, energy available to the Department through the Slice product is expected to average 426 average MW over all water conditions. Under critical water conditions, the Slice product would provide 334 average MW of energy.

Subsequent to the signing of the original contract, the amount of energy to be delivered to the Department by Bonneville has undergone two modifications. In response to Bonneville’s request that its customers temporarily reduce their purchases of power from Bonneville, in May 2001 the Department agreed to a reduction of about 24 average MW in the Slice product for the period from October 1, 2001, through March 31, 2002, and a reduction of about 74 average MW for the period from April 1, 2002, through September 30, 2002. In February 2002 Bonneville agreed to purchase from the Department conservation savings expected to be achieved over the period from October 1, 2001, through September 30, 2003. Conservation savings were estimated at 9.8 average MW for the twelve-month period beginning October 1, 2001, and an additional 9.3 average MW for the subsequent twelve-month period. Bonneville agreed to pay the Department \$27 million for these savings. The amount of energy to be delivered to the Department as a Block was reduced by 9.8 average MW for the period from October 1, 2001, through September 30, 2002, and by 19.1 average MW for the period from October 1, 2002, through September 30, 2011, to recognize the cumulative effect of the conservation savings on the Department’s load. As a result of these changes in the amounts of energy to be delivered under the contract, the total amount of power available through the contract under critical water conditions is estimated to be 438.7 average MW for the period from October 1, 2001, through September 30, 2002; 478.7 average MW from October 1, 2002, through September 30, 2006; and 593.1 average MW from October 1, 2006, through September 30, 2011. Under average water conditions, an additional 92 average MW of energy would be available through the Slice product.

In May 2000 Bonneville issued a Record of Decision establishing fees and charges effective October 1, 2001, at levels that were slightly higher than Bonneville's then current rates. The ROD included a Cost Recovery Adjustment Clause which authorized Bonneville to impose a surcharge on its power rates in order to deal with a number of contingencies that might affect adversely its financial condition. In the process of negotiating new power sales agreements with Bonneville for the period beginning October 1, 2001, many of Bonneville's public preference customers informed Bonneville that they intended to increase their purchases of power from Bonneville in the contract period beginning October 1, 2001, above the levels previously expected by Bonneville. Because the resources of the Federal System were not sufficient to serve this increase in demand, Bonneville anticipated that it would be required to purchase additional power in the wholesale market at prices considerably higher than the cost of power from the Federal System, thus substantially increasing its revenue requirements. In December 2000, Bonneville therefore issued an Amended Power Rate Proposal which addressed the increased level of uncertainty resulting from the increase in customer demand and the volatility of market prices and specified the terms under which the CRAC would be applied. A supplemental proposal in February 2001 incorporated a partial settlement agreement with the parties to the rate case. In June 2001 Bonneville issued a ROD on the Supplemental Proposal. FERC approved Bonneville's rates and the amended CRAC in September 2001.

Under the terms of the final rate proposal, Bonneville is authorized to apply a three-tiered CRAC to deal with various contingencies affecting its financial condition. The first tier, the Load-Based CRAC, is intended to cover the additional cost of purchasing power in the wholesale market to serve the increment in load that could not be accommodated by the Federal System. The second tier, the Financial-Based CRAC, will be invoked if higher than expected market prices cause Bonneville's accumulated net revenues to fall below a threshold level. The third tier, the Safety Net CRAC, will increase the Financial-Based CRAC in any year in which Bonneville projects that there is a greater than 50 percent probability that it will not be able to pay all of its financial obligations, including its debt service payments to the U.S. Treasury. The Load-Based CRAC applies to both the Block and the Slice products; the Financial-Based CRAC and the Safety Net CRAC apply only to Block purchases.

The final rate provisions include a mechanism for periodically reviewing Bonneville's financial status to determine the need for CRAC adjustments. Approximately 90 days before the beginning of each six-month segment of the rate period beginning October 1, 2001, Bonneville will conduct a public process through which it will determine the amount of revenue to be raised through the Load-Based CRAC in the next six-month period, based on the amount of augmentation energy estimated to be purchased in that period and the projected purchase price. Bonneville's rates will be adjusted to reflect the Load-Based CRAC. Approximately 90 days following the end of each six-month period, a true-up adjustment will be applied to the amounts paid by Bonneville customers, based on actual augmentation purchases made by Bonneville during the six-month period in question.

In the January 2001 ordinance that enacted the power cost adjustment to the Department's rates effective March 1, 2001, the City Council provided for an automatic adjustment on October 1, 2001, to pass through to the Department customers the effect on the Department's revenue requirements of the anticipated increase in the cost of power under the Bonneville contract resulting from Bonneville's use of its authority under the CRAC. This pass-through requirement was modified by ordinance in May 2001 to require that any future increase or decrease in Bonneville rates resulting from Bonneville's application of the CRAC be passed through to Department customers through an adjustment to energy charges. See "The Department—Retail Rates." No further action by the City Council is required to pass through future Bonneville CRAC adjustments.

In June 2001 Bonneville announced a Load-Based CRAC adjustment increasing power rates by approximately 46 percent, effective October 1, 2001. The effect of this increase was passed through to the Department's customers through an automatic increase of \$0.0055 per kWh in the energy charges of all rate classes, except the low-income rate classes. Energy charges were increased by \$0.0028 per kWh for the low-income rate classes. The effect of this pass-through, when combined with the pass-through of Bonneville's October 1, 2001, transmission rate increase authorized by the City Council in the November 1999 rate ordinance, was to increase average rates by 10.3 percent. In February 2002, Bonneville announced a reduction in the Load-Based CRAC from 46 percent to 39.08 percent for the Block product and to

40.03 percent for the Slice product, effective April 1, 2002. This reduction in Bonneville rates resulted in an automatic reduction of \$0.0007 per kWh in the energy charges of all non-low-income rate classes, and a \$0.0004 per kWh reduction in low-income rates. Average rates were reduced by 1.1 percent as a result of this change. Effective October 1, 2002, Bonneville reduced the Load-Based CRAC to 31.88 percent for the Block product and 32.35 percent for the Slice product. At the same time, Bonneville applied a Financial-Based CRAC adjustment of 10.97 percent through September 30, 2003. Since the effect of the Financial-Based CRAC on the Department was almost exactly offset by the effect of the lower Load-Based CRACs, no adjustment was made to the Department's rates on October 1, 2002.

Bonneville has projected that the following Load-Based CRAC adjustments will be required in the period through September 30, 2006:

	<u>Block</u>	<u>Slice</u>
April 1, 2003, through September 30, 2003	37%	38%
October 1, 2003, through March 31, 2004	28	29
April 1, 2004, through September 30, 2004	30	31
October 1, 2004, through March 31, 2005	25	25
April 1, 2005, through September 30, 2005	31	32
October 1, 2005, through March 31, 2006	27	27
April 1, 2006, through September 30, 2006	31	31

The Department's financial forecast assumes that the Load-Based CRAC adjustments projected by Bonneville will take effect. In addition, the Department has assumed that the Financial-Based CRAC will continue in effect at 11 percent from October 1, 2003, through September 30, 2006; that Bonneville will impose a Safety-Net CRAC adjustment of 12 percent, effective May 1, 2003, and continuing through September 30, 2006; and that the Department will be required to make Slice true-up payments to Bonneville in the following amounts:

2003	\$ 6,807,000
2004	5,982,000
2005	8,457,000
2006	11,758,000
2007	9,282,000
2008 through 2011	9,000,000

The Department's forecast of revenue from retail power sales assumes that the effects of Bonneville's CRAC adjustments will be passed through to the Department's non-low-income retail customer classes through an increase of \$0.0010 per kWh effective January 1, 2003, followed by a decrease of \$0.0014 per kWh, effective January 1, 2004. The rate changes for low-income customers is assumed to be one-half the changes for non-low-income customers. In 2005, 2006 and 2007, when the Department is assumed to set new retail rates pursuant to the financial policies adopted by the City Council in December 2001, the projected costs of the Bonneville contract, including the projected effect of CRAC adjustments, are assumed to be included in the revenue requirements on which rates are based.

While the Department has made the assumptions described above regarding the actual cost and amounts of energy available through the Slice product and the level of Bonneville rates, including the additional charges levied pursuant to the CRAC, each of these factors is subject to uncertainty. Actual prices and quantities may differ from the Department's assumptions. The Department addressed the uncertainties associated with its higher level of Bonneville purchases, and particularly the uncertainties related to the nonfirm component of the Slice product, in its review of financial policies in 2001. See "The Department—Financial Policies."

Energy Northwest (formerly known as the Washington Public Power Supply System). The City is a member of Energy Northwest, which is a municipal corporation and joint operating agency organized under State law that currently has, as members, ten public utility districts and three municipalities, all located within the State. Energy Northwest has the authority to acquire, construct and operate plants, works and facilities for the generation and transmission of electric power.

Energy Northwest was engaged in the construction of five nuclear generating facilities termed Projects Nos. 1, 2, 3, 4, and 5. Project No. 2 was placed in commercial operation in December 1984 and the other projects were terminated in the 1980s. Pursuant to separate Net Billing Agreements with Energy Northwest and Bonneville with respect to Projects Nos. 1, 2 and 3 (the "Net Billed Projects"), the Department is obligated unconditionally to pay Energy Northwest its pro rata share of the total annual costs, including debt service, to finance the cost of construction. The payments are required to be made whether or not construction is completed, delayed or terminated, or operation is suspended or curtailed. Payment by Bonneville to Energy Northwest of the Department's share of its total annual cost of the Net Billed Projects is made by a crediting arrangement whereby Bonneville credits against amounts that the Department owes Bonneville for the purchase of wholesale power an amount equal to the Department's share of the total annual cost of each Net Billed Project. The agreements provide that the Department purchase from Energy Northwest and, in turn, assign to Bonneville a maximum of 8.605 percent, 7.193 percent and 5.043 percent of the capability of Projects Nos. 1 and 2 and Energy Northwest's ownership share of Project No. 3, respectively. The Department's respective shares may be increased by not more than 25 percent upon default of other public agency participants. To the extent the Department's share of such annual costs exceeds amounts owed by the Department to Bonneville, Bonneville is obligated, after certain assignment procedures, to pay the amount of such excess to the Department as reimbursement or to Energy Northwest directly, but only from funds legally available for that purpose.

Under the Net Billing Agreements, the Department's electric revenue requirements are not affected directly by the cost of completion or termination of the Net Billed Projects, but such revenue requirements may be affected to the extent that the costs of such Projects result in increases in the wholesale power rates of Bonneville. Bonneville has been paying principal of and interest on Project No. 1 revenue bonds since 1980, on Project No. 2 revenue bonds since 1977 and on Project No. 3 revenue bonds since 1982. Bonneville, in projecting its revenue requirements and wholesale power rates, includes in its estimate the principal of and interest on those bonds issued and projected to be issued and Energy Northwest's operating expenses for the Net Billed Projects.

Klamath Falls Cogeneration Project. An October 2000 agreement with the City of Klamath Falls, Oregon, provides for the purchase of energy and capacity from the Klamath Falls Cogeneration Project, a 500 MW cogeneration facility consisting of a combined-cycle combustion turbine fueled by natural gas. Under the terms of the contract, the Department will receive 100 MW of capacity from the project beginning on July 28, 2001, the project's on-line date, through June 30, 2006, with an option to renew the contract for an additional five years. The Department expects to receive 697,948 MWh of energy from the plant in 2002.

The City of Klamath Falls has contracted with PacifiCorp Power Marketing, Inc. for management of the plant's operations. PPM is also responsible for providing fuel for the plant. Power from the plant is transmitted to the Department's service area over the Department's share of the Third AC Intertie and the Bonneville system. Energy available under the contract is expected to average 85 MW. The Department may elect to displace all or a portion of the energy it is entitled to receive from the Klamath Falls Cogeneration Project in any given month. Payment for power consists of a fixed capacity charge and variable charges for the cost of fuel, which will be based on a published index of gas prices in Alberta, Canada, and for operations and maintenance costs. The cost of power under the contract is expected to average approximately \$60 per MWh through June 30, 2006. The actual cost of power may vary from the projected level due to, among other factors, variability in the price of natural gas. The Department has entered into a swap agreement with PPM to fix the price of natural gas at \$4.84 per MMBtu for the period from July 1, 2001, through December 31, 2002.

Lucky Peak Hydroelectric Power Plant. The Lucky Peak Hydroelectric Power Plant ("Lucky Peak") was developed by three Idaho irrigation districts and one Oregon irrigation district (the "Districts") and began operation in 1988. Its FERC license expires in 2030. The plant is located on the Boise River, approximately ten miles southeast of Boise, Idaho, at the Lucky Peak Dam and Reservoir. The rated capability of the three generating units at the plant is 101 MW. Energy generation in 2002 is expected to be 288,147 MWh, 85 percent of expected average output of 337,233 MWh. Since generation is concentrated in the summer months, the plant has no peak capability during the Department's winter peak period.

The Department entered into a 50-year power purchase and sales contract in 1984 with the Districts under which the Department will purchase all energy generated by Lucky Peak, in exchange for payment of costs associated with the plant and royalty payments to the Districts. The Department also signed a transmission services agreement with Idaho Power Company (“Idaho Power”) to provide for transmission of power from Lucky Peak to a point of interconnection with the Bonneville system.

Priest Rapids Hydroelectric Plant. Under an agreement effective through October 2005, the Department receives eight percent of the output of the Priest Rapids Hydroelectric Plant (“Priest Rapids”), owned and operated by Public Utility District No. 2 of Grant County (“Grant PUD”). The Priest Rapids facility has an installed capacity of 855 MW, upgraded from 835 MW by FERC in 1998 due to rewinding of three generators. The Department’s share of the development’s one-hour peak capacity is 68 MW and its share of output in 2002 is expected to be 328,626 MWh.

In 1995, certain Idaho and Snake River cooperatives filed a complaint with FERC in which they sought entitlement to allocation of power from Priest Rapids under any new license. FERC ruled in 1998 that 70 percent of the project’s output would be allocated to the new licensee, with the remaining 30 percent available for purchase pursuant to market-based principles by entities in the broad seven-state Northwest region, while giving certain Idaho cooperatives and the current power purchasers a priority right. FERC also issued an order permitting any entity, not just Grant PUD or another Washington public agency, to file a competing license application. These proceedings could impact the amount of power generated at Priest Rapids and the Department’s allocation of power upon expiration of the current contract. See “Environmental Matters—Endangered Species Act Issues.”

Contracts executed in March 2002 with Grant PUD provide for the allocation of power and other benefits from the Priest Rapids and Wanapum Projects to the Department over the period from November 1, 2005, through the end of the new FERC license period for the two projects. Under the terms of these contracts the Department expects to purchase 45,656 MWh of firm and nonfirm power from Grant PUD in calendar year 2006 at a cost of \$347,000. The amount of power available from Grant PUD will decline over time as the PUD’s load, and its claim on the projects’ output, increases. In addition, in 2006 the Department expects to realize \$3.0 million in net revenue from the sale of the 30 percent share of the projects’ output that will be sold pursuant to market-based principles in the seven-state Northwest region under the terms of the FERC order. The Yakama Indian Nation has filed a petition with FERC challenging the new contracts signed by Grant PUD.

Columbia Storage Power Exchange. The Department is one of 41 public and private utilities that, with Bonneville, operate under exchange agreements with the Columbia Storage Power Exchange (“CSPE”). CSPE is responsible for purchasing and marketing Canada’s share of the downstream power benefits that resulted from the development of water storage projects in Canada pursuant to a treaty between the U.S. and Canada. The exchange agreements provide for the transfer and assignment of 12.5 percent of such downstream power benefits to the Department and the transfer and assignment thereof, in turn, by the Department to Bonneville. In return, the Department is entitled to specified amounts of energy and capacity from Bonneville. CSPE is expected to provide the Department with 99,358 MWh in 2002. Power deliveries under the CSPE agreement will terminate in 2003. No payments have been required since 1998 and none will be required in 2002 and 2003.

Grand Coulee Project Hydroelectric Authority. The Department, in conjunction with the City of Tacoma, Department of Public Utilities, Light Division (“Tacoma”), has power purchase agreements with three Columbia Basin irrigation districts for acquisition of the output from five hydroelectric plants under 40-year contracts expiring between 2022 and 2027. These plants, which utilize water released during the irrigation season, are located along irrigation canals in eastern Washington and have a total installed capacity of approximately 129 MW. The plants generate power only in the summer and thus have no winter peak capability. Plant output is shared equally between the Department and Tacoma. In 2002, the Department expects to receive 252,658 MWh from the project.

Box Canyon Hydroelectric Plant. The Department purchases power from the Box Canyon Hydroelectric Plant (“Box Canyon”) owned and operated by Pend Oreille PUD. The purchase contract, which extends until August 1, 2005, is expected to provide the Department with 78,840 MWh of energy in 2002.

West Point Sewage Treatment Plant Cogeneration. In 1982, the Municipality of Metropolitan Seattle (now part of King County) and the Department executed a power purchase contract for the purchase of the electrical production of a cogeneration plant located at the County’s West Point Sewage Treatment Plant. The project uses methane gas produced at the treatment plant to provide approximately 1.2 MW of one-hour peak capability and 10,513 MWh of energy from three reciprocating engines. Under the terms of the agreement, the Department will purchase the total electrical output until termination of the agreement in September 2003. The Department expects to receive 13,478 MWh of energy under the agreement in 2002.

Wind Generation. An October 2001 agreement with PPM provides for the Department’s purchase of energy and associated environmental attributes (such as offsets or emission reduction credits) primarily from the State Line Wind Project in eastern Washington and Oregon. Under the agreement, the Department received wind energy with an aggregate maximum delivery rate of 50 MW per hour from January 1, 2002, through July 31, 2002, and will receive a maximum of 100 MW per hour from August 1, 2002, through December 31, 2021. The Department also expects to receive additional firm energy with an aggregate maximum delivery rate of 25 MW per hour from January 1, 2004, through June 30, 2004, and 50 MW per hour from July 1, 2004, through December 31, 2021, from the State Line Wind Project or other qualifying new wind generation facility. The Department also entered into a ten-year agreement to purchase integration and exchange services from PacifiCorp and a 20-year agreement to sell integration and exchange services to PPM. In 2002, 148,655 MWh of energy is expected to be available to the Department from the project. Energy deliveries are projected to increase to 282,294 MWh in 2003.

Exchange with Idaho Power Company. Under a 1988 agreement, the Department provided a total of 126,000 MWh of energy to Idaho Power in the months of July, August and September and received an equal amount of energy in the months of January, February, November, and December. The Department terminated this agreement effective November 1, 2002.

Exchange with Northern California Power Agency (“NCPA”). The NCPA exchange agreement provides for the Department to deliver 60 MW of capacity and a total of 90,580 MWh of energy to NCPA in the summer. In return, NCPA delivers 46 MW of capacity and 108,696 MWh of energy to the Department in the winter. Deliveries to NCPA started in 1995 and will continue until the agreement is terminated. Either party has the right to terminate the agreement after May 31, 2014.

Exchange with Tacoma. Since 1963, the Department and Tacoma have coordinated system operations pursuant to an agreement which will remain in effect through October 2003. The agreement provides for the delivery of 37,250 MWh of energy to the Department in August in exchange for the same amount of power in October. Deliveries are shaped uniformly throughout all hours of the respective months.

Wholesale Market Sales and Purchases

The Department has historically bought and sold energy in wholesale power markets to balance its loads and resources. The amount of energy purchased or sold in the wholesale market has varied with water conditions and with changes in the Department’s firm resource base. Prior to 1996, when power available to the Department at critical water levels was roughly equal to its load, the Department typically had surplus power available to sell in the wholesale market when water conditions were above critical levels. With the limitation of its Bonneville purchases in 1996 and the sale of the Centralia Steam Plant in 2000, the Department faced energy deficits at critical water levels, and expected to be a net purchaser of energy in the wholesale market under average water conditions. The Department’s new contract with Bonneville, effective October 1, 2001, significantly increased the amount of power available from this source. The acquisition of power from the Klamath Falls Cogeneration Project and the State Line Wind Project further increased the energy resources available to the Department. Demand for power in the Department’s service area fell in response to the 2001 rate increases, the Department’s encouragement of reduction in usage and the downturn in the local economy. Water conditions were close to normal in the water year beginning October 1, 2001. As a result of all of

these factors, the Department had substantial amounts of surplus energy available for sale in the wholesale market in 2002. Sales of surplus power in the wholesale market are expected to continue at high levels over the 2003-2007 period.

The table below displays the actual amounts of energy purchased and sold by the Department in wholesale markets from 1999 through 2001 and the amounts projected to be purchased and sold from 2002 through 2007. With favorable water conditions in 1999, the Department had 1,279,824 MWh of net surplus energy available for sale in the wholesale market, in spite of the fact that its resources had been reduced by the limitation on its Bonneville purchases. In 2000 and 2001, the amount of energy purchased in the wholesale market was substantial due to poor water conditions. The high cost of these purchases reflects high market prices. In 2002, net revenues from wholesale market transactions are expected to total \$99.6 million, based on actual water conditions through September 2002, which have been about average. As of September 30, 2002, the Department had secured \$92.2 million in net revenue from wholesale market transactions, or 92 percent of the amount anticipated in 2002, through wholesale deliveries of energy already completed and sales arranged on a forward basis. Energy sold in the wholesale market in 2002, net of wholesale purchases, is expected to total 4,023,770 MWh. The projection of wholesale market sales and revenue in 2003 and beyond assumes average water conditions and prices based on forward prices for sales at the mid-Columbia hub as of early October 2002. Net energy available for sale in the wholesale market is projected to decline from 2003 through 2006 due to load growth in the Department's service area and a reduction in power available under certain existing contracts. In 2007, available surplus energy is expected to increase as a result of an increase in power purchased from Bonneville. The forecasts for 2002 and 2003 include revenues from energy that the Department has already sold on a forward basis.

WHOLESALE MARKET SALES AND PURCHASES

	Actual			Projected ⁽¹⁾					
	1999	2000	2001	2002	2003	2004	2005	2006	2007
Wholesale Market Purchases (MWh)	1,393,718	2,571,228	2,417,907	752,454	61,317	60,579	154,286	118,921	62,719
Cost of Purchases	\$34,296	\$212,402	\$524,422	\$13,637	\$1,989	\$1,620	\$4,137	\$3,017	\$1,946
Average Cost (\$/MWh)	\$24.61	\$82.61	\$216.89	\$18.12	\$32.43	\$26.73	\$26.81	\$25.37	\$31.03
Wholesale Market Sales (MWh)	2,673,542	2,023,060	524,067	4,776,224	4,335,991	4,406,727	4,061,454	3,536,359	3,956,302
Revenue from Sales	\$51,466	\$103,082	\$75,333	\$113,242	\$126,502	\$138,524	\$128,576	\$111,622	\$130,346
Average Revenue (\$/MWh)	\$19.25	\$50.95	\$143.75	\$23.71	\$29.17	\$31.43	\$31.66	\$31.56	\$32.95
Sales Net of Purchases (MWh)	1,279,824	(548,168)	(1,893,840)	4,023,770	4,274,674	4,346,148	3,907,168	3,417,438	3,893,583
Net Revenue	\$17,170	(\$109,320)	(\$449,089)	\$99,605	\$124,513	\$136,905	\$124,440	\$108,605	\$128,400

(1) Projections for 2002 reflect actual water conditions through September 30, 2002. Projections for the 2003-2007 period assume average water conditions.

Risk Management

Credit Risk. The Department has established a Credit Committee, consisting of the Deputy Superintendent for Power Management and the Department's Finance Director, Director of Customer Accounts and Risk Manager, to manage the credit risk associated with the Department's marketing activities. The Credit Committee meets monthly. Committee staff review the creditworthiness of counterparties with which the Department trades power in the wholesale market and recommends credit limits for each counterparty. Where appropriate, credit enhancements are recommended for counterparties that do not meet standards of creditworthiness adopted by the Committee. Finance and Power Management staff monitor trading activity to ensure that credit limits established by the Committee are not exceeded and provide status reports to the Committee.

Market Risk. The Department's exposure to market risk is managed by a Risk Management Committee ("RMC") consisting of the Superintendent, the Deputy Superintendents for Finance and Administration, Power Management and Generation and the Department's Director of Strategic Planning and Risk Manager. The RMC meets weekly to review and adjust the Department's near-term and long-term strategy for marketing surplus energy or, in periods of deficit, for purchasing energy to meet load. The Department executes trades in the wholesale market to meet load during periods of resource deficit, to dispose of energy that is surplus to the needs of the Department's retail customers and to optimize the value of the Department's hydroelectric resources by purchasing wholesale energy in off-peak hours, when prices generally are low, and selling energy in the peak hours, when prices are generally higher. The Department does not engage in speculative trading in the wholesale market.

Transmission

Department-Owned Transmission. The Department operates 656 miles of transmission facilities. The principal transmission line transmits power from the Skagit Project to the Department's service area. In 1994, the Department signed an agreement with Bonneville for the acquisition of ownership rights to 160 MW of transmission capability over Bonneville's share of the Third AC Intertie, which connects the Northwest region with California and the Southwest. The benefits from this investment include avoidance of Bonneville's transmission charges associated with power sales and exchanges over the Intertie and the ability to enter into long-term firm contracts with out-of-state utilities. The Oregon Department of Revenue has initiated litigation to collect a tax on the Department's rights in the Third AC Intertie. The potential liability is about \$500,000 per year. Preliminary motions are scheduled in Oregon Tax Court in April 2003. An appeal to the Oregon Supreme Court is likely to follow the Tax Court's disposition of the case, and an appeal to the United States Supreme Court is possible.

Regional Transmission Organizations. In 1999, FERC issued its Order 2000, which mandated the formation of regional transmission organizations ("RTOs") and set forth various standards for their organization and operation. In response, Bonneville and nine investor-owned utilities in the Pacific Northwest created "RTO West," a Washington non-profit corporation, to function as the operator of the principal transmission facilities in the Pacific Northwest and provide transmission services under standardized tariffs. In its financial forecast, the Department has assumed that it will begin to purchase transmission services from RTO West on January 1, 2005, the date on which RTO West is assumed to begin operations. See "Recent Developments in the Electric Utility Industry."

Transmission Arrangements with Bonneville. Contracts with Bonneville provide the Department with 1,962 MW of transmission capacity under a point-to-point contract for the period from October 1, 2001, through July 31, 2025. Power supplied to the Department by B.C. Hydro under the High Ross Agreement is transmitted over Bonneville's lines under an agreement extending through 2005. B.C. Hydro reimburses the Department for the cost of this contract. See "Power Resources—The Department's Resources." Additional purchases of transmission on a nonfirm basis may be required in the future in order to accommodate the Department's sales of power in the wholesale market during the spring runoff.

Bonneville's transmission rates applicable to the point-to-point contract are \$1.013 per kW-month, and will remain in effect through September 30, 2003. The Department's financial forecast assumes that RTO West will assume operational responsibility for the regional transmission system beginning in 2005. The

Department's rights under the current point-to-point transmission contract with Bonneville are expected to be preserved under RTO West. However, the rates that will apply to services provided by RTO West are uncertain. In its financial forecast, the Department has assumed that the cost of transmission under RTO West will be 25 percent higher than the cost of transmission under the existing Bonneville contract.

Other Transmission Contracts. The Department also transmits power under contracts with Idaho Power for the transmission of power from the Lucky Peak Project, with Avista for transmission of power from the Grand Coulee Project Hydroelectric Authority; with Puget Sound Energy for transmission of power from the Cedar Falls and South Fork Tolt Projects, with PacifiCorp for transmission of power from the State Line Wind Project, and with other utilities.

Conservation

The Department has pursued a policy of managing as well as meeting energy demand. As a result of the "Energy 1990" study, prepared in 1976, the City decided to pursue conservation as an alternative to participating in Energy Northwest's Projects Nos. 4 and 5. During the 1980s, single-family residential measures dominated the Department's conservation program. Commercial, industrial and multifamily conservation incentive programs were added in the 1990s. Because of their cost-effectiveness, commercial and industrial measures account for the majority of new energy savings acquired in recent years, a trend that is projected to continue into the future. Since 1977, the Department has achieved almost 90 average MW of energy savings through conservation.

The 2000 Strategic Resources Assessment called for the Department to accelerate the pace of energy savings through conservation. In the spring of 2001, a workplan was developed which increased the targeted level of energy savings to be achieved annually through conservation programs from six average MW to nine average MW per year. To meet this higher target, the workplan called for the Department to continue to operate its core conservation initiatives for all customer groups while adding some new programs and services to address service gaps.

The new power sales contract with Bonneville that took effect on October 1, 2001, provides a credit of \$0.50 per MWh against the amounts payable under Bonneville's rate schedules for investments in conservation and renewable resources. The Department estimates that this credit will reduce payments to Bonneville by \$2.2 million per year.

Under a March 2002 agreement with Bonneville, Bonneville will pay the Department almost \$26 million for conservation savings to be achieved over the period from October 1, 2001, through September 30, 2003. Bonneville has also agreed to reimburse the Department for \$750,000 of conservation expenditures made in 2001. The Department's purchases of power from Bonneville in the form of a shaped block have been reduced by 9.8 average MW from April 1, 2002, through September 30, 2002, and by 19.1 average MW from October 1, 2002, through September 30, 2011, to recognize the effect of the anticipated conservation savings on the Department's load. The Department may negotiate additional agreements with Bonneville that will provide payments for conservation savings in the period beyond September 30, 2002, with concomitant reductions in the Department's purchases of power from Bonneville.

CAPITAL IMPROVEMENT AND CONSERVATION IMPLEMENTATION PROGRAMS

The Department maintains long-range capital improvement and conservation implementation programs to ensure the availability of adequate supplies of power and to provide a high level of service reliability to its various customer groups. The six-year Capital Improvement Program ("CIP") for the Department forms a part of the City's Comprehensive Capital Improvement Program, which is mandated by the State's Growth Management Act. The City's biennial budget process determines the annual funding levels for both the CIP and the Conservation Implementation Program.

The Department's six-year CIP emphasizes projects that address the long-term performance and reliability of its hydroelectric generation plants, substations and distribution systems. The Department's Conservation

Implementation Program provides increased funding for investments in the commercial and industrial sectors of the service territory to achieve the Department's long-term energy savings goal.

The sections below describe the CIP and Conservation Improvement Program that was included in the Mayor's September 2002 budget proposal for the 2003-04 Biennium, which is currently under review by the City Council.

Generation

The Department plans to spend \$156.9 million on generation plant improvements over the 2002-2007 period. Expenditures of \$34.1 million are projected to complete the rehabilitation work at the Boundary Project, the Department's largest and most economical generation resource. This rehabilitation is needed to ensure long-term reliability and to prepare for the FERC relicensing of the Boundary Project, which is scheduled for 2011. Expenditures are also planned for the ongoing program of turbine runner replacement at the Boundary Project and the Ross and Gorge Powerhouses. Mitigation measures required under the terms of the renewed FERC License for the Skagit and Newhalem Projects will require expenditures totaling \$38.5 million over the 2002-2007 period.

Transmission

Over the next six years, the Department expects to spend about \$6.8 million for expansion and replacement of transmission plant.

Substations

Substation expansion and improvements are projected to cost \$52.7 million over the 2002-2007 period. Projects include improvements to protective relaying, circuit breaker replacement, switchgear refurbishment, and transformer replacement. These capital projects are designed to maintain reliability and to increase capacity to provide for load growth.

Distribution

The Department plans to spend \$438.0 million over the 2002-2007 period on improvements and additions to its distribution system. Improvements to the downtown network distribution system, service connections and capacity additions account for about 72 percent of these costs. Other projects in this category include replacement of streetlights and floodlights, rebuilding of underground residential distribution systems, meter additions, and replacement of plant and equipment.

General Plant

Programmed expenditures of \$86.3 million will support general plant projects over the 2002-2007 period. Projects include improvements to the North and South Service Centers and other facilities within the service territory. Investments in information technology, including development of Customer Data Services and Work Process Management Systems, are expected to require expenditures totaling \$46.0 million. Communications improvements, including development of a fiber optic network, advanced radio systems and improved energy management and transmission scheduling, are budgeted at \$12.1 million. Special work equipment, office equipment, replacement of vehicles, and miscellaneous building improvements make up a large portion of the remaining costs in the general plan category.

High Ross Dam Amortization

In setting rates for the 2000-2003 period, the City Council directed the Department to amortize the \$21.8 million capital portion of the annual payment to B.C. Hydro under the High Ross Agreement through 2035. (See "Power Resources—The Department's Resources—Ross, Diablo and Gorge Hydroelectric Plants.") Each year from 2000 through the final capital payment in 2020, \$9.1 million of the annual payment will be deferred and \$12.7 million will be recognized as an expense. From 2001 through 2035, the deferred costs will be amortized through annual charges of \$12.7 million. The deferred portion of the payments to B.C. Hydro is treated as a component of capital requirements.

Conservation

Capital requirements also include \$146.0 million for the Conservation Implementation Program over the 2002-2007 period. This level of expenditure is expected to enable the Department to increase its targeted annual energy savings from six to nine average MW by 2003. The emphasis of the conservation programs in this period will be on the commercial and industrial sectors. See "Power Resources—Conservation."

Other Potential Capital Projects

The Department continually reviews the need for capital improvements in its distribution and substation infrastructure in order to maintain system reliability and to provide for future growth in demand. It is possible that projects will be identified in the future that are not included in the current CIP. Construction of a new substation serving the central business district in the City may be required due to load growth in the downtown area. Potential distribution infrastructure improvements also include work associated with the construction of regional transit systems and commercial redevelopment of the South Lake Union area. The Department expects to be reimbursed for capital expenditures required in connection with major transportation infrastructure projects.

Financing

Capital requirements of \$941.3 million from 2002 through 2007 are expected to be financed through a combination of net revenues from operations, contributions in aid of construction, external funding of conservation programs, the remaining proceeds of the 2001 Parity Bonds, and the proceeds of future bond issues. In 2002 and 2003, no net revenue from operations is expected to be available to fund capital requirements. Capital financing will be provided from the remaining proceeds from the 2001 Parity Bonds (\$165.0 million as of December 31, 2001), the proceeds of an additional Parity Bond issue in 2003 (\$90.0 million), and contributions in aid of construction and external conservation funding (\$55.7 million). From 2004 through 2007, net revenue available for capital financing is expected to total \$341.9 million, or 53 percent of capital requirements. The remainder of capital funding in that period is projected to be provided by contributions in aid of construction and external conservation funding (\$64.5 million) and bond proceeds. From 2004 through 2007, Parity Bonds in the amount of \$125.0 million are expected to be issued. Subordinate Lien bond issuances are projected to be \$110.0 million.

IN THE PREPARATION OF THE PROJECTIONS IN THIS OFFICIAL STATEMENT, THE CITY HAS MADE CERTAIN ASSUMPTIONS WITH RESPECT TO CONDITIONS THAT MAY OCCUR IN THE FUTURE. WHILE THE CITY BELIEVES THESE ASSUMPTIONS ARE REASONABLE FOR THE PURPOSE OF THE PROJECTIONS, THEY DEPEND UPON FUTURE EVENTS, AND ACTUAL CONDITIONS MAY DIFFER FROM THOSE ASSUMED. THE CITY DOES NOT REPRESENT OR GUARANTEE THAT ACTUAL RESULTS WILL REPLICATE THE ESTIMATES IN THE VARIOUS TABLES SET FORTH IN THIS OFFICIAL STATEMENT. THE ELECTRIC INDUSTRY HAS UNDEEGONE SIGNIFICANT CHANGES, AS DISCUSSED IN THIS OFFICIAL STATEMENT. POTENTIAL PURCHASERS OF THE BONDS SHOULD NOT RELY ON THE PROJECTIONS IN THIS OFFICIAL STATEMENT AS STATEMENTS OF FACT. SUCH PROJECTIONS ARE SUBJECT TO CHANGE, AND WILL CHANGE, FROM TIME TO TIME. THE CITY HAS NOT COMMITTED ITSELF TO PROVIDE INVESTORS WITH UPDATED FORECASTS OR PROJECTIONS.

PROPOSED CAPITAL IMPROVEMENT AND CONSERVATION PROGRAMS (2002-2007)
(000s)

	2002	2003	2004	2005	2006	2007	Total
Generation							
Turbine Rehabilitation	\$ 5,598	\$ 2,004	\$ 7,089	\$ 1,403	\$ 10,178	\$ 7,538	\$ 33,810
Skagit Mitigation	8,424	10,257	2,516	9,487	3,623	4,242	38,549
Dam Safety	1,655	1,287	386	--	--	--	3,328
Boundary Rehabilitation Project	7,973	9,016	6,499	6,377	2,450	1,778	34,093
All Others	5,722	6,379	6,903	8,269	7,566	12,277	47,116
Total Generation	\$ 29,372	\$ 28,943	\$ 23,393	\$ 25,536	\$ 23,817	\$ 25,835	\$ 156,896
Transmission	\$ 1,973	\$ 930	\$ 957	\$ 969	\$ 992	\$ 1,020	\$ 6,841
Substations	\$ 10,231	\$ 7,313	\$ 9,053	\$ 8,479	\$ 8,682	\$ 8,912	\$ 52,670
Distribution							
Network Additions and Services	\$ 12,073	\$ 17,563	\$ 18,092	\$ 17,321	\$ 17,669	\$ 18,571	\$ 101,288
Service Connections	11,753	12,228	12,933	11,943	12,229	12,554	73,640
Relocations and Capacity Additions	15,647	25,714	26,322	23,960	24,486	25,459	141,589
26KV Conversion	8,754	2,176	2,229	2,636	2,698	2,769	21,262
Regional Transit	--	3,956	3,701	10,130	12,020	478	30,285
Monorail	--	341	450	2,125	2,156	822	5,894
Alaskan Way Viaduct	--	392	510	7,619	8,570	6,924	24,015
Street and Floodlights	1,795	1,573	1,613	1,561	1,598	1,640	9,780
All Others	5,158	5,115	5,273	4,772	4,887	5,012	30,217
Total Distribution	\$ 55,180	\$ 69,058	\$ 71,123	\$ 82,067	\$ 86,313	\$ 74,229	\$ 437,970
General Plant							
Service Center Improvements	\$ 2,838	\$ 143	\$ 185	\$ 623	\$ 637	\$ 652	\$ 5,078
Consolidated Customer Service System	453	2,825	3,249	--	--	--	6,527
Communications Improvements	2,037	1,889	1,989	2,040	2,053	2,076	12,084
Information Technology	8,204	8,088	7,714	6,495	7,386	8,085	45,973
All Others	2,826	2,800	2,651	2,786	3,335	2,221	16,620
Total General Plant	\$ 16,359	\$ 15,745	\$ 15,788	\$ 11,944	\$ 13,411	\$ 13,034	\$ 86,281
Conservation	\$ 21,622	\$ 23,524	\$ 24,321	\$ 24,922	\$ 25,520	\$ 26,130	\$ 146,039
Deferred High Ross Expenses ⁽¹⁾	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 9,103	\$ 54,620
Total Expenditures All Projects	\$ 143,840	\$ 154,616	\$ 153,738	\$ 163,020	\$ 167,838	\$ 158,263	\$ 941,317
Sources of Funds							
Revenue Available for Capital Projects	\$ 0	\$ 0	\$ 78,652	\$ 86,723	\$ 84,672	\$ 91,803	\$ 341,850
Proceeds from Contributions ⁽²⁾	30,668	25,053	15,805	16,079	16,212	16,435	120,253
Decreases/(Increases) in Construction Fund	113,172	40,445	9,698	(8,959)	7,430	(4,186)	157,600
Proceeds from Senior Lien Bonds	--	90,000	--	70,000	--	55,000	215,000
Proceeds from Subordinate Lien Bonds	--	--	50,000	--	60,000	--	110,000
Proceeds to Bond Issue Costs and Discounts	--	(882)	(416)	(823)	(476)	(789)	(3,387)
Total Funding for Capital Projects	\$ 143,840	\$ 154,616	\$ 153,738	\$ 163,020	\$ 167,838	\$ 158,263	\$ 941,317

(1) In adopting rates for the 2000-2003 period, the City Council directed the Department to amortize the capital portion of annual payments to the Province of British Columbia under the High Ross Agreement over a period extending through 2035. From 2000 until the final capital payment is made in 2020, \$9.1 million in High Ross costs will be deferred. See "Power Resources—The Department's Resources."

(2) Includes contributions in aid of construction and customer payments for conservation. Also included in 2002 and 2003 are payments received from Bonneville to purchase conservation savings. See "Power Resources—Conservation."

HISTORICAL AND PROJECTED OPERATING RESULTS

Historical Results—1999-2001

Financial results in 1999, 2000 and 2001 were heavily influenced by water conditions in the Northwest region and by price levels in the wholesale power market. In 1999 precipitation and streamflows in the watersheds supplying the Department's hydroelectric plants were above normal, and the utility had a net surplus of 1,279,824 MWh, which it sold in the wholesale market, generating net revenue of \$17.2 million. Energy available to the Department in 2000 and 2001 was reduced by the sale of the Centralia Steam Plant in May 2000 and by extremely poor water conditions in the water year beginning October 1, 2000. At the same time, wholesale market prices increased to levels never before experienced in the Northwest. In 2000 the Department was forced to purchase 548,168 MWh more than it sold in the wholesale market, at a cost of \$109.3 million. In 2001, net purchases amounted to 1,893,840 MWh at a cost of \$449.1 million.

Revenues from sales of electricity to retail customers in the Department's service area rose from \$366.0 million in 1999 to \$383.7 million in 2000 and \$500.9 million in 2001. The increase from 1999 to 2000 was due to the increase in average rates that took effect on December 24, 1999, and growth of 0.7 percent in the amount of energy sold. In 2001, revenues were 30.5 percent above the 2000 level, reflecting the four rate increases that were implemented in 2001. See "The Department—Retail Rates." The volume of sales actually decreased by 5.1 percent from 2000 to 2001. See "Customers, Energy Sales and Requirements and Peak Loads."

The cost of supplying power to meet load, including wholesale market purchases, long-term purchased power contracts and the operating costs of the Department's hydroelectric facilities, increased from \$151.6 million in 1999 to \$322.9 million in 2000 and \$698.7 million in 2001. The cost of wholesale market purchases increased from \$34.3 million in 1999 to \$212.4 million in 2000 and \$524.4 million in 2001, as a result of poor water conditions and high market prices in 2000 and 2001. In addition to the growth in the cost of wholesale purchases, the increase in power costs in 2001 reflected the Department's new Bonneville contract effective October 1, 2001, and the contract for the purchase of power from the Klamath Falls Cogeneration Project, effective July 1, 2001. The cost of Bonneville power increased from \$34.4 million in 2000 to \$66.8 million in 2001. Power from the Klamath Falls Cogeneration Project cost \$18.5 million in 2001.

Debt service payments on Parity Bonds increased from \$75.4 million in 1999 to \$83.2 million in 2000, but fell to \$61.6 million in 2001. The increase from 1999 to 2000 is attributable to the issuance of \$158.0 million in Parity Bonds in October 1999. The reduction in debt service costs in 2001 reflects the refinancing of certain scheduled payments of principal and interest in 2001, which more than offset the impact of the issuance of \$98.8 million in Parity Bonds in December 2000 and \$503.7 million in March 2001. Also, \$9.8 million in interest costs on the 2001 Parity Bonds were capitalized.

Debt service on Subordinate Lien Bonds increased from \$5.1 million in 1999 to \$6.7 million in 2000, then declined to \$5.7 million in 2001 as short-term interest rates fell to low levels. In 1999 and 2000, net revenue available for debt service was equal to 1.90 and 1.26 times debt service on Parity Bonds, respectively. Coverage of debt service on both Parity and Subordinate Lien Bonds was 1.78 times debt service in 1999 and 1.16 times debt service in 2000.

The City Council has authorized the deferral of \$300 million in excess power costs from 2001 to future years. The Department expects to amortize the deferred costs in equal monthly amounts through December 2004. With net revenue in 2001 adjusted to take account of the deferred power costs, net revenue was equal to 1.42 times debt service on Parity Bonds and 1.30 times debt service on Parity Bonds and Subordinate Lien Bonds in 2001.

Projected Results—2002

Energy consumption by retail customers resumed its historical pattern of growth in the third quarter of 2002. The volume of retail sales in 2002 is now expected to be almost exactly the same as the level recorded in 2001. Revenue from retail sales is expected to increase by 13.0 percent, from \$500.9 million in 2001 to \$566.0 million in 2002, reflecting the staged rate increases that were implemented in 2001.

Wholesale energy sales are expected to generate \$113.2 million in 2002. Purchases of wholesale energy are projected to cost \$13.6 million. Net revenue from wholesale market transactions are therefore estimated at \$99.6 million. The average price of wholesale energy sold is expected to be \$24 per MWh; purchases are expected to be made at an average price of \$18 per MWh. Net revenue from wholesale market transactions is projected to be below normal because cold weather in the spring delayed the runoff in the Columbia Basin by about two months beyond the normal March-June period. When warm weather arrived, streamflows exceeded the hydraulic capacity of the Department's generators at the Boundary Project, and significant amounts of water were spilled. With hydro generation at high levels, prices in the wholesale market fell below \$10 per MWh in June and July.

Other purchased power costs are projected to increase substantially, from \$151.2 million in 2001 to \$220.2 million in 2002. Contracts for the purchase of power from Bonneville, the Klamath Falls Cogeneration Project and the State Line Wind Generation Project account for most of the increase. The contracts with Bonneville and Klamath Falls, which took effect on July 1, 2001, and October 1, 2001, respectively, will be in effect for the entire calendar year 2002. Deliveries of power from the State Line Wind Project began in January 2002. See "Power Resources—Purchased Power Arrangements."

Wheeling costs are expected to be \$31.0 million in 2002, an increase of \$4.6 million over the 2001 level, due mainly to the increase in Bonneville wheeling rates that took effect October 1, 2001. Other operating and maintenance expenses, excluding the cost of power supply and wheeling, are expected to amount to \$116.1 million in 2002, an increase of \$0.5 million from the 2001 level. The level of expense to be recorded in 2002 will be affected by changes in accounting policy. Under the new policy, the Department records as revenues receipts that had been treated as offsets to expense in 2001. This change resulted in an increase of about \$2.0 million in operating and maintenance expense relative to 2001 and a corresponding increase in miscellaneous revenues. Without this change, operating and maintenance expenses would have been lower in 2002 than in 2001.

Debt service payments on Parity Bonds and Subordinate Lien Bonds are projected to increase to \$115.8 million in 2002 from \$67.3 million in 2001. Debt service on Parity Bonds will increase from \$61.6 million in 2001 to \$110.7 million in 2002, when the full impact of the 2001 Parity Bonds will be felt, without the reductions in debt service payments that occurred in 2001. Unspent proceeds from the 2001 Parity Bonds are expected to be sufficient to fund capital expenditures through the first half of 2003. The Department currently does not plan to issue additional long-term debt in 2002.

Net revenue available for debt service in 2002, before recognizing the amortization of deferred power costs, is expected to be equal to 2.63 times debt service on Parity Bonds and 2.52 times debt service on Senior and Subordinate Lien Bonds. If net revenue is adjusted to reflect the amortization of \$100 million in deferred power costs in 2002, coverage would be 1.73 times debt service on Parity Bonds and 1.65 times debt service on Parity Bonds and Subordinate Lien Bonds.

Through September 30, 2002, the Department has accrued net income of \$30.9 million, compared to a loss of \$363.3 million in the same period of the prior year. Expenses through September 30, 2002, include the amortization of \$75.0 million in excess power costs deferred from 2001. A reduction in wholesale market purchases accounts for the difference in net income. In 2001, the Department spent \$513.3 million through September purchasing wholesale power at high prices. Through September 2002, wholesale purchases fell to \$10.4 million.

STATEMENT OF REVENUES, EXPENSES AND NET INCOME
JANUARY 1 THROUGH SEPTEMBER 30
(\$000, UNAUDITED)

	2002	2001	Increase/ (Decrease)
OPERATING REVENUES:			
Retail Power Revenues	\$432,866	\$361,607	\$71,259
Wholesale Power Revenues	102,059	94,437	7,622
Transmission and Other	10,116	5,220	4,896
Subtotal: Operating Revenues	\$545,041	\$461,264	\$83,777
OPERATING EXPENSES:			
Operation and Maintenance Expense *	\$367,216	\$708,384	(\$341,168)
Taxes	46,630	37,794	8,836
Depreciation	52,555	42,346	10,209
Subtotal: Operating Expenses	\$466,401	\$788,524	(\$322,123)
Net Operating Income/(Loss):	\$78,640	(\$327,260)	\$405,900
NONOPERATING REVENUES/(EXPENSES):			
Investment Income	\$7,947	\$9,734	(\$1,787)
Other Income (Expense), Net	6	(185)	191
Interest Expense	(61,446)	(52,087)	(9,359)
Amortization of Debt Expense	(2,135)	(1,555)	(580)
Subtotal: Non-Operating Revenues/(Expenses)	(\$55,628)	(\$44,093)	(\$11,535)
Income/(Loss) before Contributions, Grants, and Transfers	\$23,012	(\$371,353)	\$394,365
CONTRIBUTIONS, GRANTS, AND TRANSFERS:			
Contributions in Aid of Construction	\$7,711	\$8,019	(\$308)
Grants and Transfers	154	-	154
Subtotal: Contributions, Grants, and Transfers	\$7,865	\$8,019	(\$154)
NET INCOME/(LOSS)	\$30,877	(\$363,334)	\$394,211

* At the end of December 2001, \$300 million of purchased power expenses were deferred and are expected to be amortized in 2002, 2003 and 2004 in equal monthly amounts. Through September 30, 2002, purchased power costs include the amortization of \$75 million of deferred purchased power costs.

Projected Results—2003-2007

The Department's current forecast of retail revenue assumes that rates will increase by an average of 1.6 percent on January 1, 2003, to pass through anticipated increases in Bonneville rates. Average rates are expected to fall by 2.2 percent on January 1, 2004, due to projected decreases in Bonneville rates.. The financial policies adopted by the City Council in December 2001 are assumed to be used to set rates effective January 1, 2005. At that point rates are expected to decline by 3.4 percent. The new financial policies require that rates in 2005 and 2006 be sufficient to provide 95 percent confidence that net revenues after payment of all current obligations will be at least \$12.5 million in each year in order to fund a rate stabilization account of \$25 million. In 2007, with the rate stabilization account fully funded and with Bonneville's CRAC adjustments assumed to be removed effective October 1, 2006, rates are assumed to be 13 percent below the 2005 level. See "The Department—Financial Policies."

The forecast of wholesale market sales and purchases assumes average water conditions throughout the 2003-2007 period. Net revenue from wholesale market transactions is expected to range from a high of

\$136.9 million in 2004 to a low of \$108.6 million in 2006. The amount of surplus energy available for sale in the wholesale market is projected to decline from 2003 through 2006, as the energy available from a number of contracted resources declines and as system load increases. In 2007, the amount of surplus energy available is assumed to increase as a result of the increase in energy available under the Bonneville power sales contract, effective October 1, 2006. The average price for wholesale sales is expected to rise from \$24 per MWh in 2002 to \$33 per MWh in 2007. See “Power Resources—Wholesale Market Sales and Purchases.”

Other purchased power costs are projected to increase from \$220.2 million in 2002 to \$235.1 million in 2004 and \$244.7 million in 2005, due primarily to the assumed acquisition of additional renewable resources. The cost of purchased power contracts then declines in stages to \$206.5 million in 2007, as a result of the expiration of contracts with Pend Oreille PUD and the City of Klamath Falls, the assumed elimination of Bonneville’s CRAC adjustments and a reduction in the cost of power from the Lucky Peak Hydroelectric Project.

Wheeling costs are projected to increase from \$31.0 million in 2002 to \$41.3 million in 2007, due to a projected increase of ten percent in Bonneville transmission rates effective October 1, 2003, and the anticipated purchase of additional transmission capacity to accommodate increased purchases of wind energy. In addition, transmission costs are projected to increase by an additional 15 percent when the proposed RTO takes control of regional transmission, which is assumed to occur in 2005.

Other costs of operations and maintenance are projected to increase from \$116.1 million in 2002 to \$134.6 million in 2007. Conservation costs, including the cost of amortizing the Department’s growing conservation investments, are expected to increase throughout the period, from \$11.8 million in 2002 to \$15.6 million in 2007. Excluding conservation, operations and maintenance costs are projected to increase at roughly the rate of inflation.

Financing the Department’s capital requirements is expected to require the issuance of \$90 million of Parity Bonds in 2003 and \$50 million of Subordinate Lien Bonds in 2004. Over the 2005-2007 period, an additional \$125 million of Parity Bonds and \$60 million of Subordinate Lien Bonds are expected to be issued. From 2004 through 2007, approximately 53 percent of capital requirements are expected to be financed from current revenues, with the remainder of the financing coming from bond proceeds, contributions in aid of construction and various conservation funding sources.

Debt service on Parity Bonds is projected to increase from \$110.7 million in 2002 to \$124.5 million in 2007. Debt service on Subordinate Lien Bonds is expected to rise from \$7.6 million in 2002 to \$13.1 million in 2007. Before recognizing the amortization of deferred power costs, coverage in 2003 and 2004 is expected to average 2.59 times debt service on Parity Bonds and 2.46 times the sum of Parity and Subordinate Lien Bonds debt service. If the amortization of deferred power costs is taken into account, coverage in 2003 and 2004 is expected to average 1.72 times Parity Bonds debt service and 1.63 times total debt service. Over the 2005-2007 period, net revenues are expected to be equal to 2.13 times debt service on Parity Bonds and 1.96 times total debt service.

Uncertainty of Projections and Potential Mitigating Actions

In projecting its financial results for the period through 2007, the Department has made a number of assumptions regarding the factors that affect its financial performance. If actual experience differs from the assumptions made with regard to these factors, the Department’s actual financial results could differ significantly from the results projected in its forecast. The factors the Department believes are most likely to affect its financial results are load growth within the Department’s service territory, water conditions in the watersheds of concern to the Department, prices in the wholesale power market, and prices charged by Bonneville under its power sales with the Department.

Load Growth. If load growth in a given year were to exceed the amount projected, the amount of surplus energy available to the Department would be reduced. The Department would receive more revenue from sales to its retail customers and less revenue from sales of surplus energy in the wholesale market. Through 2007 the Department’s average revenue per MWh of retail sales (net of taxes) is projected to be higher than

the average price in the wholesale market. Under these conditions, an increase in load would result in a net financial benefit to the Department. For example, if load in 2003 were one percent higher than projected, the net benefit to the Department would be about \$2.4 million. Conversely, if load were one percent lower than projected, the Department's net revenue would be about \$2.4 million lower than projected. The effect of load variances is expected to diminish in the years beyond 2003 because the difference between the Department's average retail rate and the average market price is projected to narrow.

Water Conditions. The Department expects to have an average of almost 4,000,000 MWh of surplus energy available for sale in the wholesale market over the 2003-2007 period under average water conditions. Under adverse water conditions that would be expected to be exceeded with 95 percent confidence, based on actual water conditions experienced in the 1929-1978 period, the amount of surplus energy available could be as low as 1,400,000 MWh in a given year. Revenues from surplus energy sales in this instance would therefore be approximately \$70 million lower than currently projected. Conversely, under favorable water conditions that would be expected to be exceeded with five percent confidence, revenues would be approximately \$50 million higher than projected.

Wholesale Market Prices. The Department's forecast of wholesale market prices through 2006 is based on forward prices as of September 2002. The price projected for 2007 is the 2006 price plus inflation. The Department expects to sell its surplus energy at average prices ranging from \$29 per MWh in 2003 to \$33 per MWh in 2007. If the actual price in the wholesale market in a given year exceeds these estimates by \$1 per MWh, the Department would realize approximately \$4 million in additional revenue. Conversely, the Department's revenues would be reduced by \$4 million if the wholesale market price were \$1 per MWh below the price assumed in the forecast.

Bonneville Prices. The prices charged by Bonneville under its power sales contract with the Department currently include a surcharge of approximately 32 percent under the cost recovery adjustment clause. The Department is required by City ordinance to pass through the effects of changes in the Bonneville surcharge on its costs by adjusting retail rates. If the Bonneville surcharge were to increase by ten percentage points in a given year, the Department's purchased power costs would increase by about \$10 million, and retail rates would increase by approximately two percent to offset the resulting increase in costs. Conversely, if the surcharge were to decline by ten percentage points, the Department would experience a \$10 million reduction in its costs, and retail rates would be lowered by about two percent. Therefore, any increases or decreases in Bonneville rates would result in increases or decreases in the Department's retail rates, but would not affect net revenue.

The financial planning resolution adopted by the City Council in December 2001 requires the Department to maintain rates at their current levels, unless increased by the City Council, until all short-term debt has been retired and the balance in the Department's operating account has reached a level of \$30 million. The Department projects that this point will be reached by the end of the second quarter of 2004. At that point rates can be set in accordance with the new financial policies adopted by the City Council, which would allow rates to be lowered by 3.4 percent. Any development which has a negative effect on the Department's cash flow would delay the point at which the new financial policies would go into effect. Alternatively, the projected effective date of the new financial policies could be maintained by increasing retail rates in an amount sufficient to offset the effect of the unfavorable developments.

Mitigating Actions. If actual results differ from those assumed in the Department's projections due to the risk factors discussed above, the City has a number of options for dealing with the financial consequences. First, the City could leave rates in effect at their current levels for a longer period of time than now anticipated. Second, the City could increase rates beyond their current levels. Third, the City could mitigate any cash flow problems through the use of temporary loans from the City's Cash Pool. Finally, the City could issue additional short-term debt instruments.

SUMMARY OF HISTORICAL AND PROJECTED OPERATING RESULTS ⁽¹⁾
(\$000)

	Actual			Projected					
	1999	2000	2001	2002	2003	2004	2005	2006	2007
Operating Revenues:									
Retail Energy Sales in Seattle Service Area ⁽²⁾									
Residential	\$ 144,397	\$ 150,773	\$ 187,802	\$ 218,645	\$ 215,403	\$ 210,072	\$ 205,250	\$ 201,366	\$ 181,291
Commercial	138,029	152,085	206,083	232,237	240,372	234,946	230,931	228,103	205,413
Governmental	37,193	33,585	43,958	50,394	53,470	53,630	54,137	54,919	50,813
Industrial	46,341	47,231	63,043	64,678	69,508	76,626	75,891	75,554	68,498
Subtotal	\$365,960	\$383,674	\$500,886	\$565,953	\$578,754	\$575,274	\$566,208	\$559,941	\$506,015
Retail Energy Sales Outside Service Area	1,975	7,904	2,551	--	--	--	--	--	--
Wholesale Power Sales	51,466	103,082	75,333	113,242	126,502	138,524	128,576	111,622	130,346
Power Exchanges and Other ⁽³⁾	3,395	5,050	33,191	10,432	10,476	9,453	10,535	15,074	15,872
Transmission Revenues ⁽⁴⁾	1,508	2,137	9,679	3,202	2,355	2,040	2,090	2,140	2,192
Other Revenue	4,816	3,781	5,946	8,359	9,383	10,181	11,148	14,811	15,140
Total Revenue	\$429,120	\$505,628	\$627,586	\$701,188	\$727,469	\$735,471	\$718,557	\$703,589	\$669,564
Operating Expenses Before Debt Service:									
Wholesale Market Purchases	\$ 34,296	\$ 212,402	\$ 524,422	\$ 13,637	\$ 1,989	\$ 1,620	\$ 4,137	\$ 3,017	\$ 1,946
Other Power Purchases	81,684	79,305	151,213	220,156	235,091	244,675	244,653	230,289	206,503
Production	35,580	31,170	23,077	25,866	27,568	29,424	30,251	31,450	32,315
Wheeling	18,436	18,432	26,346	30,968	30,744	36,839	38,312	40,843	41,291
Other Operating and Maintenance Expenses ⁽⁵⁾	111,217	104,555	115,602	116,107	118,806	124,130	127,897	131,472	134,594
Taxes (excluding City taxes)	16,861	18,845	21,915	26,300	26,910	26,919	26,745	26,782	24,887
Total Operating Expenses Before Debt Service	\$ 298,074	\$ 464,710	\$ 862,575	\$ 433,034	\$ 441,107	\$ 463,606	\$ 471,995	\$ 463,853	\$ 441,536
Net Operating Revenue	\$131,046	\$40,919	(\$234,989)	\$268,154	\$286,362	\$271,865	\$246,563	\$239,736	\$228,028
Add:									
Amortization ⁽⁵⁾	\$ 6,964	\$ 7,825	\$ 8,873	\$ 9,447	\$ 10,036	\$ 11,062	\$ 12,363	\$ 13,816	\$ 14,890
Proceeds of Property Sales ⁽⁶⁾	142	41,464	(8)	3,448	3,745	882	--	350	--
Operating Fees and Grants	230	565	1,382	300	300	300	300	300	300
Other Income	4,954	13,868	12,346	10,277	5,599	6,795	9,573	11,583	11,894
Revenue Available for Debt Service	\$ 143,336	\$ 104,640	(\$212,396)	\$ 291,627	\$ 306,042	\$ 290,905	\$ 268,799	\$ 265,785	\$ 255,112

Footnotes to Table:

- (1) Results for 1999 and 2000 have been restated to comply with recent changes in accounting standards. Several items that are included in revenues in the table above had been treated as offsets to operating expenses prior to the restatements.
- (2) The projection of revenue from retail sales assumes that rates will increase by 1.6 percent effective January 1, 2003, to pass through anticipated increases in Bonneville rates. Rates are assumed to decrease by 2.2 percent effective January 1, 2004, when Bonneville rate adjustments are expected to reduce the Department's costs under the Bonneville contract. Beginning in 2005, rates are assumed to be set in compliance with the new financial policies established by the City Council. Average rates are assumed to decline by 7.9 percent in 2005, 1.9 percent in 2006 and 11.1 percent in 2007. See "The Department—Financial Policies."
- (3) Includes the valuation of energy delivered under seasonal exchanges, revenue from deliveries of energy to Pend Oreille PUD pursuant to Article 49 of the Boundary Project license and other energy credits.
- (4) Includes revenue from the rental of transmission facilities to Bonneville and Snohomish County PUD and revenue from the sale of transmission capacity.
- (5) Includes certain amortization expenses.
- (6) Proceeds from the sale of the Centralia Steam Plant in 2000 amounted to \$41,399,000.

HISTORICAL AND PROJECTED DEBT SERVICE COVERAGE
(\$000)

	Actual			Projected					
	1999	2000	2001	2002	2003	2004	2005	2006	2007
Revenue Available for Debt Service	\$ 143,336	\$ 104,640	\$ (212,396)	\$ 291,627	\$ 306,042	\$ 290,905	\$ 268,799	\$ 265,785	\$ 255,112
Deferral/(Amortization) of Power Costs ⁽¹⁾			300,000	(100,000)	(100,000)	(100,000)			
Adjusted Revenue Available for Debt Service	\$ 143,336	\$ 104,640	\$ 87,604	\$ 191,627	\$ 206,042	\$ 190,905	\$ 268,799	\$ 265,785	\$ 255,112
Debt Service:									
Parity Bonds	75,395	83,206	61,552	110,695	109,722	120,446	120,443	124,526	124,525
Subordinate Lien Bonds	5,085	6,680	5,749	5,097	5,558	7,333	9,952	10,135	13,107
Total Debt Service	\$ 80,480	\$ 89,886	\$ 67,301	\$ 115,792	\$ 115,280	\$ 127,779	\$ 130,395	\$ 134,661	\$ 137,631
Debt Service Ratios (giving effect to deferral/amortization of power costs) :									
Times Covered - Parity Bonds ⁽²⁾	1.90	1.26	1.42	1.73	1.88	1.58	2.23	2.13	2.05
Times Covered - Parity and Subordinate Lien Bonds ⁽³⁾	1.78	1.16	1.30	1.65	1.79	1.49	2.06	1.97	1.85
Debt Service Ratios (without giving effect to deferral/amortization of power costs) :									
Times Covered - Parity Bonds ⁽⁴⁾	1.90	1.26	(3.45)	2.63	2.79	2.42	2.23	2.13	2.05
Times Covered - Parity and Subordinate Lien Bonds ⁽⁵⁾	1.78	1.16	(3.16)	2.52	2.65	2.28	2.06	1.97	1.85

- (1) Deferral of excess power costs in 2001 and amortization of these costs in future years has been authorized by the City Council.
- (2) Determined by dividing Adjusted Revenue Available for Debt Service by Parity Debt Service.
- (3) Determined by dividing Adjusted Revenue Available for Debt Service by the sum of Parity Debt Service and Subordinate Lien Debt Service.
- (4) Determined by dividing Revenue Available for Debt Service by Parity Debt Service.
- (5) Determined by dividing Revenue Available for Debt Service by the sum of Parity Debt Service and Subordinate Lien Debt Service.

ENVIRONMENTAL MATTERS

Impact of Environmental Matters

Environmental responsibility and stewardship are identified as corporate values in the Department's strategic and business planning efforts. The Department manages its legal obligations for environmental protection through programs which ensure compliance with regulations. Although the Department cannot predict the outcome or effect of the matters described in this section, the Department does not expect that any of these matters will affect adversely its ability to pay the principal of and interest on the Bonds.

Waste Management and Disposal Issues

Routine operations in connection with the generation and delivery of electric power are regulated heavily by federal, state and local laws that prescribe standards, work practices and training requirements and require extensive documentation to ensure the protection of the environment and human health. Noncompliance creates the potential for violations that can result in substantial fines. Some of these laws also impose strict liability for environmentally damaging releases, including costs of investigation and cleanup, damages, restoration, and the costs of agency oversight and enforcement.

Department operations generate a variety of wastes including hazardous wastes. However, the Department's reduction efforts have resulted in a significant decline in hazardous waste generation and disposal costs over the past five years. The Department ensures compliance with federal and State hazardous waste regulations through use of operations manuals, staff training and periodic internal inspections or audits. During internal audits, compliance with other laws, including the Toxic Substances Control Act, Clean Water Act and Underground Storage Tank regulations, is monitored.

Through the Department's pollution prevention programs, more than six million pounds of oil contaminated with polychlorinated biphenyls has been removed from the system and pesticide use has been reduced by 80 percent compared to baseline levels.

Contaminated Site Liability

The Department follows the City's due diligence policy in all property transactions. Most of these transactions involve selling property such as retired unit substations. Site assessments are also conducted on all potential property acquisitions.

The City has been named a Potentially Responsible Party ("PRP") by the U.S. Environmental Protection Agency (the "EPA") at ten separate sites in Whatcom, Pierce, Kitsap, Lewis, and Snohomish Counties in Washington State, and at a site in Utah. The City has settled its potential liability at these sites through cash settlements or completion of investigation and cleanup actions at a cost of approximately \$9.2 million. No assurances can be given that EPA or state agencies will not seek additional work at these sites or compensation for damages to natural resources. However, the Department has taken steps, including extensive site restoration, to reduce the risk of legal actions related to natural resources damages.

In 2001, the EPA listed the Lower Duwamish Waterway as a Superfund site. In anticipation of this listing, the City (through the Department and Seattle Public Utilities), King County, the Port of Seattle, and the Boeing Company entered into a voluntary administrative consent order with the EPA and the State Department of Ecology to perform a remedial investigation and feasibility study ("RI/FS") along the Lower Duwamish Waterway. The Department has recorded a \$2,500,000 environmental liability for actual and estimated future costs associated with the RI/FS. This amount will be evaluated annually and is subject to adjustment as developments occur. It is likely that the City will be liable for a portion of the costs of subsequent remediation of the Lower Duwamish site. The Department may be liable for certain of these costs as a result of the ownership and operation of the Georgetown Steam Plant, which was decommissioned in 1980 but which has been owned by the Department from 1951 to the present. The amount of the Department's potential liability cannot be determined at this time; however, it will not include federal claims for natural resources damage because these claims were resolved on behalf of the entire City in 1991.

No assurances can be given that other such sites do not exist or will not be discovered in the future. The Department's policy has been to undertake voluntary cleanup action when contamination is discovered during maintenance and construction.

Endangered Species Act Issues

A number of fish species inhabit the waters where hydroelectric projects are owned by the Department, or from which the Department purchases power. Some species have been, or may be in the future, listed under the Endangered Species Act ("ESA") as either "threatened" or "endangered." The overall long-run implications of these listings are difficult to assess. The two legal mechanisms that typically come into play and that could affect project operation are the Section 7 "consultation" requirement and the Section 9 "take" prohibition. Where an activity that may affect a listed species has a federal "nexus"—that is, where an activity is undertaken, permitted or funded by a federal agency—that agency is required to consult with either the National Marine Fisheries Service ("NMFS") for salmon and steelhead or the U.S. Fish and Wildlife Service ("USFWS") for other species. The purpose of the consultation is to ensure that the activity will not "jeopardize" the continued existence of the species or adversely modify its critical habitat. Biological Opinions are prepared, in appropriate cases, and mandatory conditions may be placed on the conduct of the activity or project in order to avoid causing jeopardy. The ESA's "take" prohibition bars any person from actions that kill or harm listed species, including harming their habitat in a fashion which kills or injures them. There is considerable legal uncertainty concerning the scope of the "take" concept, and particularly concerning the extent to which it may have retroactive application to facilities and operations that are in existence at the time of listing. Notwithstanding the "take" prohibition, incidental take of listed species can be authorized by NMFS or USFWS either through an "incidental take statement" issued through the Section 7 consultation process or through an "incidental take permit" issued under Section 10. Incidental take means take that is incidental to, and not the purpose of, the carrying out of an otherwise legal activity. The Secretary of Commerce or the Interior may issue an incidental take permit if the applicant submits to the Secretary a habitat conservation plan that specifies the impacts that likely will result from the activity in question and the steps the applicant will take to mitigate and minimize the taking, and if the agency determines that the activity will not jeopardize the continued existence of the species.

Columbia and Snake River Anadromous Fish Issues. There are three federal "action agencies" responsible for the operation of the Federal Columbia River Power System: the Corps, the Bureau and Bonneville. These agencies have been engaged in consultation for a number of years, and NMFS has been required as a result of litigation to develop a series of Biological Opinions relating to the Columbia and Snake River fisheries. In 1995, NMFS developed a broad species recovery plan, including recommendations for upstream and downstream passage requirements. These requirements include minimum flow targets for the entire Columbia Basin designed to maximize the survival of downstream migrating juvenile salmon and steelhead and upstream migrating adult salmon and steelhead. In May 1998 and December 2000, NMFS and the US Fish and Wildlife Service developed supplemental plans that identify reasonable and prudent alternatives to protect and recover not only listed salmon and steelhead, but also bull trout and sturgeon that have been listed under the ESA in the Columbia River Basin.

The Department's power generation at its Boundary Project has been affected by the recovery plans and the Biological Opinions on which they were based. Specifically, the Biological Opinions require reservoirs upstream from the Boundary Project to store more water during the winter for release in the spring and summer when it is needed for downstream juvenile fish migration. Generation at the Boundary Project therefore is reduced in the fall and winter, when the region experiences its highest sustained energy demand. Due to the recommendations of the Biological Opinions, more of the Boundary Project's annual generation is shifted to the spring and summer, when system load is lower and supplies of power are generally more abundant. The Biological Opinions also result in a reduction in the Boundary Project's firm capability under the terms of the Coordination Agreement. Other Department-owned projects are not affected by the Biological Opinions. The Department does have contracts to obtain power from the Priest Rapids project and a percentage of the total Bonneville system generation. The Biological Opinions may have similar effects on the firm capability of Priest Rapids and the Bonneville system. It is unknown at present how new Biological Opinions to support recovery plans will affect power generation capabilities at the Boundary Project. However, in the opinion of the Department, it is unlikely that new opinions will result in significant

changes in flows that would affect the Boundary Project, Priest Rapids and Bonneville. Priest Rapids is currently going through a relicensing process and power output could be affected by the terms of the new FERC license.

In the Biological Opinions, the NMFS established a Technical Management Team (the “TMT”) to advise the operating agencies on dam and reservoir operations to optimize passage conditions for juvenile and adult salmonids. The TMT consists of representatives from NMFS, USFWS, the Bureau, the Corps, Bonneville, states, and Native American tribes. The TMT conducts in-season management during the anadromous fish migration season. Recommendations of the TMT are made to the Corps and the Bureau, which have authority to operate the Federal Columbia River Power System projects, and to the Corps and Bonneville, which have the authority to make agreements with Canada regarding storage in Canada. Recommendations of the TMT are made by consensus when possible. If consensus is not reached, issues are elevated to the Implementation Team (the “IT”), which includes senior managers from the same federal agencies, states and tribal governments represented on the TMT. The IT forwards its final recommendations to the operating agencies, and the Corps and/or the Bureau make decisions, which are communicated in writing to the TMT and the IT.

Other Endangered Species Issues. Other fish listings that may affect Department operations include bull trout and chinook salmon in Puget Sound. Bull trout have a wide geographic range in the Pacific Northwest, and sub-populations are present in most of the reservoirs and rivers used for hydroelectric generation, including all three reservoirs of the Skagit Project. These populations are generally recognized as being among the healthiest in the State due to excellent habitat conditions, cold water temperatures and an abundant food supply. Bull trout are also found in the Cedar Falls Hydroelectric Project reservoir. Studies currently are under way to determine the status of the populations and any potential impacts of the hydroelectric projects on bull trout downstream of the Skagit Project and in its reservoirs. The studies will be used to develop management plans in cooperation with State and federal agencies.

Listed chinook salmon are present in the Skagit, Tolt and Cedar Rivers downstream of hydroelectric facilities on those rivers. The hydroelectric facilities are above natural passage barriers in the case of the Skagit and Tolt Rivers. While it is unclear how these listings might affect operations, the Department may be able to minimize adverse impacts on its operations for a number of reasons. On the Cedar River, the Department’s activities are covered by a Habitat Conservation Plan that authorizes operations with regard to all listed species of the Cedar Falls Hydroelectric Project and by an incidental take permit. Both the Skagit and South Fork Tolt River projects were licensed through a collaborative process involving State and federal regulatory agencies, including NMFS and USFWS, and tribes. These agreements include extensive measures to protect fish, including complex flow controls and non-flow measures such as habitat restoration and research and monitoring. In addition, the Department is carrying out an ESA Early Action program that will assist in the recovery of chinook and bull trout and address any further impacts related to these issues.

Clean Water Act Issues

Section 401 of the federal Clean Water Act requires states to provide a “water quality certification” as a precondition for federal actions including licensing of hydroelectric projects. The purpose of the certification is to ensure that the project complies with State water quality standards. These standards address various physical and chemical parameters, and Section 401 also has been interpreted to authorize states to condition their certification on maintenance of a minimum stream flow determined to be necessary to protect fish. An agreement with State and federal agencies was reached on minimum flows for the Newhalem Creek plant, and incorporated into the FERC license issued in 1997. As required by FERC, the Department has installed a new intake system capable of delivering the approved instream flows. The completion of the intake system, including all improvements and testing, was reported to FERC in August 2001. The license for the Boundary project expires in 2011 and the Department is currently preparing for the relicensing process. Water quality studies at the Boundary Project are currently underway in support of that process. It is unknown to what extent these issues may affect power generation capability pursuant to a new license.

Renewable Energy and Carbon Dioxide Mitigation

The City Council has passed resolutions committing the Department to acquire new renewable resources, setting a goal of meeting the electric energy needs of the City with no net greenhouse gas emissions and committing the Department to mitigate fully the greenhouse gases emitted pursuant to its power purchases from the Klamath Falls Cogeneration Project. A consultant to the Department currently is evaluating the Department's greenhouse gas emissions and mitigation commitments under these resolutions. The Department also is working with the Climate Trust (Portland, Oregon) to acquire greenhouse gas offsets (i.e., a reduction in greenhouse gas emissions at one location to compensate for emissions at another location). In addition, the Department has purchased output and associated environmental attributes from the State Line Wind Project in eastern Washington and Oregon. See "Power Resources—Purchased Power Arrangements—Wind Generation." Finally, the Department is offering customers the opportunity to contribute to the acquisition of additional renewable resources, as required by a recent State law. See "The Department—Retail Rates." Customer contributions initially will be used to install solar electricity systems on public facilities, with an emphasis on schools. The Department is currently evaluating additional renewable energy options to pursue with this funding.

Electromagnetic Fields

Many studies have been conducted regarding potential health effects resulting from exposure to power line frequency electric and magnetic fields ("EMF"). A 1999 report to Congress of the National Institute of Environmental Health Sciences ("NIEHS") concluded that the scientific evidence that power frequency EMF poses health risk is weak. The report recommended that because some, albeit weak, evidence suggests there may be some health concerns, there should be a focus on "passive" actions aimed at exposure reduction. The Department has a policy of evaluating ways to minimize EMF in the design and construction of new utility facilities, and provides information and measurements for customers and employees. Since publication of the 1999 NIEHS report, there have not been significant research developments that have changed the NIEHS conclusions.

THE CITY OF SEATTLE

Municipal Government

Incorporated in 1869, the City of Seattle, Washington, is the largest city in the Pacific Northwest and is the county seat of King County (the "County"). The City's elected officials are a mayor, nine City Council members and a city attorney. These officials are elected at large to four-year terms. The City provides four utility services funded by rates and charges: electricity, water, drainage and wastewater, and solid waste.

Financial Management

City financial management functions are provided by the Department of Finance. Dwight D. Dively is the Director of Finance. Mr. Dively is a graduate of Rose-Hulman Institute of Technology, holds a master's degree from Princeton University in public affairs and is a Ph.C. in civil engineering at the University of Washington.

Accounting. The accounting and reporting policies of the City conform to generally accepted accounting principles for municipal governments and are regulated by the State Auditor's Office, Division of Municipal Corporations, which maintains a resident staff at the City to perform a continual current audit as well as the annual post-fiscal year audit of City financial operations. The Department of Finance maintains general supervision over financial transactions of all City funds.

Auditing. The State Auditor is required to examine the affairs of all local governments at least once every three years; the City is audited annually. The examination must include, among other things, the financial condition and resources of the City, compliance with the laws and Constitution of the State, and the methods and accuracy of the accounts and reports of the City. Reports of the Auditor's examinations are required to

be filed in the office of the State Auditor and in the Department of Finance. The City's Comprehensive Annual Financial Report may be obtained from the Department of Finance by calling (206) 684-8300.

Municipal Budget. City operations are guided by a budget prepared under the direction of the Mayor by the City Budget Office within the Department of Finance pursuant to State statute (Chapter 35.32A of the Revised Code of Washington). The proposed budget is submitted to the City Council by the Mayor each year not later than 90 days prior to the beginning of the next fiscal year. Currently the fiscal year of the City is from January 1 through December 31. The City Council considers the proposed budget, holds public hearings on its contents and may alter and revise the budget at its discretion, subject to the State requirement that budgeted revenues must at least equal expenditures. The City Council is required to adopt the budget at least 30 days before the beginning of the next fiscal year.

Investments. **The information in this section does not pertain to pension funds, which are administered by the Seattle City Employees' Retirement System, and some debt issuance proceeds that are administered by trustee service providers.**

All cash-related transactions for the City, including its utilities, are administered by the Treasury Division of the Department of Finance. City cash is deposited into a single bank account and cash expenditures are paid from a consolidated disbursement account. Investments of temporarily idle cash may be made, according to existing City Council-approved policies, by the Treasury Division in the following securities:

- (i) U.S. Treasury and agency issues;
- (ii) bankers' acceptances sold on the secondary market;
- (iii) repurchase and reverse repurchase agreements, when structured with securities eligible for purchase and when executed under an approved Master Repurchase Agreement with selected primary dealers; and
- (iv) commercial paper purchased in the secondary market which has received the highest ratings of at least two nationally recognized rating agencies.

State statutes, City ordinances and Department of Finance policies require the City to minimize market risks by safekeeping all purchased securities according to governmental standards for public institutions and by maintaining safety and liquidity above consideration for returns. Current City investment policies require periodic reporting about the City's investment portfolio to the Mayor and the City Council. The City's investment operations are reviewed by the City Auditor and by the State Examiner.

As of September 30, 2002, the combined investment portfolios of the City totaled \$890.2 million at book value. The City's Cash Pool is constituted solely of City funds. The City does not invest any of its funds in other pools, with the exception of tax collection receipts initially held by the County and funds of the Seattle City Employees' Retirement System and the Deferred Compensation Plan. The year-to-date yield on the City's consolidated pool of investments as of September 30, 2002, was 4.4 percent. As of September 30, 2002, the average maturity date of the portfolio was May 6, 2004. Approximately 33.6 percent, or \$298.7 million, was invested in securities with maturities of three months or less. The City held no securities with maturities longer than 15 years. Investments were allocated as follows:

U.S. Government and Agency Securities	56.4%
Commercial Paper	24.2
Federal Discount Notes	15.6
Certificates of Deposit	1.4
Federal Farm Credit Bank	1.1
Repurchase Agreements	1.1
Mortgage-Backed Securities	0.2

Interfund Loans. City ordinances authorize the Director of Finance to approve interfund loans for a duration of up to 90 days and to establish a rate of interest on such loans. Extension or renewal of interfund loans requires City Council approval by ordinance. The Director of Finance also is authorized by City ordinance to make loans to individual funds participating in a common investment portfolio by carrying funds in a negative cash position for a period of up to 90 days, or for a longer period upon approval by ordinance, to the extent that such loans can be supported prudently by the common investment portfolio and the borrowing fund is reasonably expected to be able to repay the loan. Loans of this type bear interest at the common investment portfolio's rate of return.

Risk Management

The City maintains \$25,000,000 liability insurance, with a \$2,500,000 self-insured retention for each occurrence. The City also maintains \$200,000,000 property insurance, with a \$100,000 deductible for each occurrence, on City-owned buildings with value greater than the deductible, unless insurance of at least equivalent value is provided by other parties. Hydroelectric projects owned by the City are not insured. Workers compensation is insured to statutory limits, with a \$500,000 self-insured retention for each occurrence. In addition, insurance policies are purchased to cover other property and casualty exposure.

Pension System

Nearly all permanent non-uniformed City employees participate in the Seattle City Employees' Retirement System (the "Plan"), a single employer public employee retirement system. The payroll for City employees covered by the Plan for the year ended December 31, 2001, was \$405.0 million; total City payroll was \$619.5 million. Nearly all City employees are required to contribute 8.03 percent of their annual base salary to the Plan, and the City contributes an additional 8.03 percent. As of January 1, 2001, system assets exceeded the accrued actuarial liability. The actuarial present value of future benefits was \$1.988 billion, the actuarial present value of future normal costs for present members was \$497.8 million and the actuarial value of assets available for benefits was \$1.493 billion. Combined employee and employer contributions to the Plan totaled approximately \$69.3 million for the year ending December 31, 2001. Due to changes in interest rates, it is expected that a new actuarial study completed in 2002 will show a deficit.

Labor Relations

The City has 34 separate departments and offices with approximately 13,000 regular and temporary employees. Thirty different unions and 45 bargaining units represent approximately 75 percent of the City's regular employees. The City's contract with the Seattle Police Officers Guild was ratified in July 2000 and extends through the end of 2002. The contract with the Seattle Police Management Association (representing lieutenants and captains in the Police Department) expired at the end of 2001, and negotiations for a successor contract are continuing. The City has recently approved new three-year contracts with the coalition of City unions representing most non-uniformed City employees, and with IBEW Local 77, which represents electrical workers in the City Light and Transportation departments. The City also has recently concluded agreements with Firefighters Local 27 and Fire Chiefs Local 2898. These new contracts generally extend through 2004.

INITIATIVE AND REFERENDUM

State

Under the State Constitution, the voters of the State have the ability to initiate legislation and require the State Legislature to refer legislation to the voters through the powers of initiative and referendum, respectively. Initiatives and referenda are submitted to the voters upon receipt of a petition signed by at least eight percent (initiative) and four percent (referenda) of the number of voters registered and voting for the office of Governor at the preceding regular gubernatorial election. Any law approved in this manner by a majority of the voters may not be amended or repealed by the State Legislature within a period of two years following enactment, except by a vote of two-thirds of all the members elected to each house of the State Legislature. After two years, the law is subject to amendment or repeal by the State Legislature in the same manner as other laws. The initiative power may not be used to amend the State Constitution.

In recent years, a variety of State-wide initiatives have been placed on the ballot and approved by the voters. Certain of these initiatives purported to limit a broad array of taxes and fees, including utility fees, but the measures subsequently were held to be unconstitutional by the Washington Supreme Court. Certain other initiatives, affecting taxes but not utility fees, have been approved by the voters and become law.

Although several State initiatives and referenda were on the November 5, 2002 ballot, none affected the Department. Other tax or fee initiative measures may be filed in the future, but it cannot be predicted whether any such initiatives might gain sufficient signatures to qualify for submission to the State Legislature and/or the voters or, if submitted, whether they ultimately would be approved.

City

Under the City Charter, Seattle voters may initiate local legislation and City Charter amendments and modify existing legislation through the powers of initiative and referendum. There are no pending City measures that affect the Department.

LEGAL AND TAX INFORMATION

Bond Litigation

There is no litigation pending with process properly served on the City questioning the validity of the Bonds or the power and authority of the City to issue the Bonds.

Approval of Counsel

Legal matters incident to the authorization, issuance and sale of the Bonds by the City are subject to the approving legal opinion of Foster Pepper & Shefelman PLLC, Bond Counsel. A form of the opinion of such firm with respect to the Bonds is attached hereto as Appendix B. Bond Counsel will be compensated only upon the issuance and sale of the Bonds.

Tax Exemption

Exclusion from Gross Income. In the opinion of Bond Counsel, under existing federal law and assuming compliance with applicable requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issue date of the Bonds, interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals.

Continuing Requirements. The City is required to comply with certain requirements of the Code after the date of issuance of the Bonds in order to maintain the exclusion of the interest on the Bonds from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Note proceeds and the facilities financed or refinanced with Note proceeds, limitations on investing gross proceeds of the Bonds in higher yielding investments in certain circumstances, and the arbitrage rebate

requirement to the extent applicable to the Bonds. The City has covenanted in the Bond Ordinance to comply with those requirements, but if the City fails to comply with those requirements, interest on the Bonds could become taxable retroactive to the date of issuance of the Bonds.

Corporate Alternative Minimum Tax. While interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, under Section 55 of the Code, tax-exempt interest, including interest on the Bonds, received by corporations is taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations (as defined for federal income tax purposes). Under the Code, alternative minimum taxable income of a corporation will be increased by 75 percent of the excess of the corporation's adjusted current earnings (including any tax-exempt interest) over the corporation's alternative minimum taxable income determined without regard to such increase. A corporation's alternative minimum taxable income, so computed, that is in excess of an exemption of \$40,000, which exemption will be reduced (but not below zero) by 25 percent of the amount by which the corporation's alternative minimum taxable income exceeds \$150,000, is then subject to a 20 percent minimum tax.

For taxable years beginning after December 31, 1997, the corporate alternative minimum tax is repealed for a small business corporation that had average gross receipts of less than \$5 million for the three-year period beginning after December 31, 1994, and such a small business corporation will continue to be exempt from the corporate alternative minimum tax so long as its average gross receipts do not exceed \$7.5 million.

Tax on Certain Passive Investment Income of S Corporations. Under Section 1375 of the Code, certain excess net passive investment income, including interest on the Bonds, received by an S corporation (a corporation treated as a partnership for most federal tax purposes) that has Subchapter C earnings and profits at the close of the taxable year may be subject to federal income taxation at the highest rate applicable to corporations if more than 25 percent of the gross receipts of such S corporation is passive investment income.

Foreign Branch Profits Tax. Interest on the Bonds may be subject to the foreign branch profits tax imposed by Section 884 of the Code when the Bonds are owned by, and effectively connected with a trade or business of, a United States branch of a foreign corporation.

Certain Other Federal Tax Consequences

Bonds Not "Qualified Tax-Exempt Obligations" for Financial Institutions. Section 265 of the Code provides that 100 percent of any interest expense incurred by banks and other financial institutions for interest allocable to tax-exempt obligations acquired after August 7, 1986, will be disallowed as a tax deduction. However, if the tax-exempt obligations are obligations other than private activity bonds, are issued by a governmental unit that, together with all entities subordinate to it, does not reasonably anticipate issuing more than \$10,000,000 of tax-exempt obligations (other than private activity bonds and other obligations not required to be included in such calculation) in the current calendar year, and are designated by the governmental unit as "qualified tax-exempt obligations," only 20 percent of any interest expense deduction allocable to those obligations will be disallowed.

The City is a governmental unit that, together with all subordinate entities, reasonably anticipates issuing more than \$10,000,000 of tax-exempt obligations (other than private activity bonds and other obligations not required to be included in such calculation) during the current calendar year and has not designated the Bonds as "qualified tax-exempt obligations" for purposes of the 80 percent financial institution interest expense deduction. Therefore, no interest expense of a financial institution allocable to the Bonds is deductible for federal income tax purposes.

Reduction of Loss Reserve Deductions for Property and Casualty Insurance Companies. Under Section 832 of the Code, interest on the Bonds received by property and casualty insurance companies will reduce tax deductions for loss reserves otherwise available to such companies by an amount equal to 15 percent of tax-exempt interest received during the taxable year.

Effect on Certain Social Security and Retirement Benefits. Section 86 of the Code requires recipients of certain Social Security and certain Railroad Retirement benefits to take receipts or accruals of interest on the Bonds into account in determining gross income.

Other Possible Federal Tax Consequences. Receipt of interest on the Bonds may have other federal tax consequences as to which prospective purchasers of the Bonds may wish to consult their own tax advisors.

Original Issue Premium. The Bonds maturing on December 1 in the years 2003 through 2012, inclusive, have been sold at prices reflecting original issue premium (“Premium Bonds”). An amount equal to the excess of the purchase price of a Premium Bond over its stated redemption price at maturity constitutes premium on such Premium Bond. A purchaser of a Premium Bond must amortize any premium over such Premium Bond’s term using constant yield principles, based on the purchaser’s yield to maturity. The amount of amortizable premium allocable to an interest accrual period for a Premium Bond will offset a like amount of qualified stated interest on such Premium Bond allocable to that accrual period, and may affect the calculation of alternative minimum tax liability described above. As premium is amortized, the purchaser’s basis in such Premium Bond is reduced by a corresponding amount, resulting in an increase in the gain (or decrease in the loss) to be recognized for federal income tax purposes upon a sale or disposition of such Premium Bond prior to its maturity. Even though the purchaser’s basis is reduced, no federal income tax deduction is allowed. Purchasers of Premium Bonds, whether at the time of initial issuance or subsequent thereto, should consult with their own tax advisors with respect to the determination and treatment of premium for federal income tax purposes and with respect to state and local tax consequences of owning such Premium Bonds.

Original Issue Discount. The Bonds maturing on December 1 in the years 2013 and 2014 have been sold at prices reflecting original issue discount (“Discount Bonds”). Under existing law, the original issue discount in the selling price of each Discount Bond, to the extent properly allocable to each owner of such Discount Bond, is excluded from gross income for federal income tax purposes with respect to such owner. The original issue discount is the excess of the stated redemption price at maturity of such Discount Bond over the initial offering price to the public, excluding underwriters and other intermediaries, at which price a substantial amount of the Discount Bonds of such maturity were sold.

Under Section 1288 of the Code, original issue discount on tax-exempt bonds accrues on a compound basis. The amount of original issue discount that accrues to an owner of a Discount Bond during any accrual period generally equals (i) the issue price of such Discount Bond plus the amount of original issue discount accrued in all prior accrual periods, multiplied by (ii) the yield to maturity of such Discount Bond (determined on the basis of compounding at the close of each accrual period and properly adjusted for the length of the accrual period), less (iii) any interest payable on such Discount Bond during such accrual period. The amount of original issue discount so accrued in a particular accrual period will be considered to be received ratably on each day of the accrual period, will be excluded from gross income for federal income tax purposes, and will increase the owner’s tax basis in such Discount Bond. Any gain realized by an owner from a sale, exchange, payment, or redemption of a Discount Bond will be treated as gain from the sale or exchange of such Discount Bond.

The portion of original issue discount that accrues in each year to an owner of a Discount Bond may result in certain collateral federal income tax consequences. The accrual of such portion of the original issue discount will be included in the calculation of alternative minimum tax liability as described above, and may result in an alternative minimum tax liability even though the owner of such Discount Bond will not receive a corresponding cash payment until a later year.

Owners who purchase Discount Bonds in the initial public offering but at a price different from the first offering price at which a substantial amount of those Discount Bonds were sold to the public, or who do not purchase Discount Bonds in the initial public offering, should consult their own tax advisors with respect to the tax consequences of the ownership of such Discount Bonds. Owners of Discount Bonds who sell or otherwise dispose of such Discount Bonds prior to maturity should consult their own tax advisors with respect to the amount of original issue discount accrued over the period such Discount Bonds have been held

and the amount of taxable gain or loss to be recognized upon that sale or other disposition of Discount Bonds. Owners of Discount Bonds also should consult their own tax advisors with respect to state and local tax consequences of owning such Discount Bonds.

Continuing Disclosure Undertaking

Undertaking to Provide Notice of Material Events. To meet the requirements of United States Securities and Exchange Commission (“SEC”) Rule 15c2-12(b)(5) (the “Rule”), the City will undertake in the Note Resolution (the “Undertaking”) for the benefit of holders of the Bonds, as follows.

Annual Financial Information. The City agrees to provide or cause to be provided to each nationally recognized municipal securities information repository designated by the SEC in accordance with the Rule (each “NRMSIR”) and to a state information depository, if one is established in the State of Washington and recognized by the SEC (the “SID”), annual financial information and operating data regarding the Light System of the type included in this Official Statement as generally described below (“annual financial information”):

- (i) annual financial statements of the Light System prepared in accordance with generally accepted accounting principles applicable to governmental units (except as otherwise noted therein), as such principles may be changed from time to time and as permitted by State law; which financial statements will not be audited, except that if and when audited financial statements are otherwise prepared and available to the City they will be provided;
- (ii) a statement of authorized, issued and outstanding bonded debt secured by Gross Revenues of the Light System;
- (iii) debt service coverage ratios;
- (iv) sources of Light System power and the cost thereof;
- (v) general customer statistics, such as number and type of customer and power consumed, and revenues by customer class; and
- (vi) average revenue per kWh of sales for each customer class.

Annual financial information described above will be provided to each NRMSIR and the SID, not later than the last day of the ninth month after the end of each fiscal year of the City, as such fiscal year may be changed as required or permitted by State law, commencing with the City’s fiscal year ending December 31, 2002. The annual financial information may be provided in a single or multiple documents, and may be incorporated by reference from other documents, including official statements of debt issues with respect to which the City is an obligated person as defined by the Rule, which documents have been filed with each NRMSIR and the SID.

The City has further agreed to provide or cause to be provided to each NRMSIR or the Municipal Securities Rulemaking Board (“MSRB”), and to the SID, timely notice of a failure by the City to provide the required annual financial information on or before the date specified above.

Material Events. The City agrees to provide or cause to be provided to each nationally recognized municipal securities information repository (each a “NRMSIR”) or the Municipal Securities Rulemaking Board (“MSRB”), and to a state information depository, if one is established in the State and recognized by the SEC (the “SID”), timely notice of the occurrence of any of the following events, if applicable and material, with respect to the Bonds, specified by the Rule:

- (i) principal and interest payment delinquencies;
- (ii) non-payment related defaults;
- (iii) unscheduled draws on debt service reserves reflecting financial difficulties;
- (iv) unscheduled draws on credit enhancements reflecting financial difficulties;

- (v) substitution of credit or liquidity providers, or their failure to perform;
- (vi) adverse tax opinions or events affecting the tax-exempt status of the Bonds;
- (vii) modifications to the rights of the holders of the Bonds;
- (viii) Note calls;
- (ix) defeasances;
- (x) release, substitution, or sale of property securing repayment of the Bonds; and
- (xi) rating changes.

For purposes of this section, “Continuing Disclosure Undertaking,” the term “holders of the Bonds” shall have the meaning intended for such term under the Rule.

Amendment of Undertaking. The Undertaking is subject to amendment without the consent of any holder of any Note, or any broker, dealer, municipal securities dealer, participating underwriter, rating agency, NRMSIR, the SID or the MSRB, under the circumstances and in the manner permitted by the Rule.

The City will give notice to each NRMSIR or the MSRB, and the SID, of the substance (or provide a copy) of any amendment to the Undertaking and a brief statement of the reasons for the amendment. If the amendment changes the type of annual financial information to be provided, the annual financial information containing the amended operations data or financial information will include a narrative explanation of the effect of that change on the type of information to be provided.

Termination of Undertaking. The City’s obligations to provide annual financial information and notices of certain events will terminate upon the legal defeasance, prior redemption or payment in full of all of the then outstanding Bonds. In addition, the Undertaking, or any provision thereof, will be null and void if the City obtains an opinion of nationally recognized bond counsel or other counsel familiar with the federal securities laws to the effect that those portions of the Rule which require the Undertaking, or any such provision, are invalid, have been repealed retroactively or otherwise do not apply to the Bonds; and so notifies the SID and either the MSRB or each then existing NRMSIR.

Remedy for Failure to Comply with Undertaking. If the City fails to comply with the Undertaking, the City will proceed with due diligence to cause such noncompliance to be corrected as soon as practicable after the City learns of that failure.

No failure by the City or other obligated person to comply with the Undertaking will constitute a default in respect of the Bonds. The sole remedy of any holder of a Note will be to take such actions as that holder deems necessary and appropriate to compel the City or other obligated person to comply with the Undertaking.

Other Continuing Disclosure Undertakings of the City. The City has entered into undertakings to provide annual information and the notice of the occurrence of certain events with respect to all bonds issued by the City on and after July 3, 1995, subject to the Rule. The City is in compliance with all such undertakings.

OTHER BOND INFORMATION

Bond Insurance

The following information and the municipal bond insurance policy specimen attached as Appendix G have been provided by Financial Security Assurance Inc. The City makes no representation as to the accuracy or completeness thereof. Purchasers of the Bonds should confirm the following with Financial Security Assurance Inc.

Bond Insurance Policy. Concurrently with the issuance of the Bonds, Financial Security Assurance Inc. (“Financial Security”) will issue its Municipal Bond Insurance Policy for the Bonds (the “Policy”). The Policy

guarantees the scheduled payment of principal of and interest on the Bonds when due as set forth in the form of the Policy included as an appendix to this Official Statement.

The Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut or Florida insurance law.

Financial Security Assurance Inc. Financial Security is a New York domiciled insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. (“Holdings”). Holdings is an indirect subsidiary of Dexia, S.A., a publicly held Belgian corporation. Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance in France, Belgium and other European countries. No shareholder of Holdings or Financial Security is liable for the obligations of Financial Security.

At September 30, 2002 Financial Security’s total policyholders’ surplus and contingency reserves were approximately \$1,728,433,000 and its total unearned premium reserve was approximately \$972,390,000 in accordance with statutory accounting principles. At September 30, 2002, Financial Security’s total shareholder’s equity was approximately \$1,928,564,000 and its total net unearned premium reserve was approximately \$814,684,000 in accordance with generally accepted accounting principles.

The financial statements included as exhibits to the annual and quarterly reports filed by Holdings with the Securities and Exchange Commission are hereby incorporated herein by reference. Also incorporated herein by reference are any such financial statements so filed from the date of this Official Statement until the termination of the offering of the Bonds. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc.: 350 Park Avenue, New York, New York 10022, Attention: Communications Department (telephone (212) 826-0100).

The Policy does not protect investors against changes in market value of the Bonds, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. Financial Security makes no representation regarding the Bonds or the advisability of investing in the Bonds. Financial Security makes no representation regarding the Official Statement, nor has it participated in the preparation thereof, except that Financial Security has provided to the City the information presented under this caption for inclusion in the Official Statement.

Ratings on the Bonds

The Bonds have been rated “Aaa” and “AAA” by Moody’s Investors Service and Standard & Poor’s Ratings Group, a Division of McGraw Hill, respectively, based upon the issuance of the Policy by Financial Security simultaneously with the delivery of the Bonds. The corresponding underlying ratings are “Aa3” and “A.” The ratings reflect only the views of the rating agencies, and an explanation of the significance of the ratings may be obtained from each rating agency. No application was made to any other rating agency for the purpose of obtaining an additional rating on the Bonds. There is no assurance that the ratings will be retained for any given period of time or that the ratings will not be revised downward or withdrawn entirely by the rating agencies if, in their judgment, circumstances so warrant. Any such downward revision or withdrawal of the ratings will be likely to have an adverse effect on the market price of the Bonds.

Purchaser of the Bonds

The Bonds are being purchased by Merrill Lynch (the “Purchaser”) at a price of \$91,162,696.21, plus accrued interest, and reoffered at a price of \$91,749,386.30, which reflects the prices or yields set forth on the cover of this Official Statement. The Purchaser may offer and sell the Bonds to certain dealers (including dealers depositing Bonds into investment trusts) and others at prices lower than the initial offering prices set forth on the inside of the cover hereof, and such initial offering prices may be changed from time to time by the purchaser. After the initial public offering, the public offering prices may be varied from time to time.

Official Statement

So far as any statements are made in this Official Statement involving matters of opinion or of estimates, whether or not so expressly stated, they are set forth as such and not as representations of fact, and no representation is made that any of the estimates will be realized. Information concerning the City, the Department and the Light System contained in this Official Statement has been furnished by the City. Neither this Official Statement nor any statement which may have been made orally or in writing is to be construed as a contract with the owners of any of the Bonds.

Neither the delivery of this Official Statement nor any sale of the Bonds will, under any circumstances, create any implication that there has been no change in the affairs of the Department since the date hereof. The City specifically disclaims any obligations to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of this Official Statement, except as otherwise expressly provided under “Legal and Tax Information—Continuing Disclosure Undertaking.”

The execution and delivery of this Official Statement have been duly authorized by the City.

THE CITY OF SEATTLE, WASHINGTON

Director of Finance

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APPENDIX A
BOND ORDINANCE

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THE CITY OF SEATTLE, WASHINGTON
ORDINANCE 120931

AN ORDINANCE relating to the electric system of The City of Seattle; authorizing the issuance and sale of municipal light and power revenue bonds to pay the costs of refunding all or a portion of certain of the City's outstanding municipal light and power revenue bonds and issuing and selling the bonds authorized herein; providing for the terms, conditions, covenants and manner of sale of those bonds; and describing the lien of those bonds.

Passed September 23, 2002

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ORDINANCE 120931

1
2 AN ORDINANCE relating to the electric system of The City of Seattle; authorizing the issuance and
3 sale of municipal light and power revenue bonds to pay the costs of refunding all or a portion of
4 certain of the City's outstanding municipal light and power revenue bonds and issuing and
5 selling the bonds authorized herein; providing for the terms, conditions, covenants and manner
6 of sale of those bonds; and describing the lien of those bonds.

6 WHEREAS, The City of Seattle, Washington (the "City"), owns, operates and maintains an electric
7 system (the "Light System"); and

8 WHEREAS, by Ordinance 116290 and Resolution 28586 the City issued its Municipal Light and
9 Power Revenue Bonds, Series 1992B, dated August 1, 1992 (the "1992B Bonds"), in the
10 original principal amount of Seventy-Five Million Seven Hundred Thirty Thousand dollars
11 (\$75,730,000), and reserved the right to redeem the 1992B Bonds maturing on or after
12 February 1, 2003, prior to their stated maturity dates on or after August 1, 2002, as a whole at
13 any time or in part on any interest payment date, with the maturities to be redeemed to be
14 selected by the City; and

14 WHEREAS, there are presently outstanding Forty-Four Million Six Hundred Twenty-Five Thousand
15 dollars (\$44,625,000) par value of 1992B Bonds maturing or subject to mandatory redemption
16 on February 1 and August 1 of each of the years 2003 through 2010, inclusive, and bearing
17 interest at various rates ranging from 5.400% to 5750%; and

15 WHEREAS, by Ordinance 116706 and Resolution 28751 the City issued its Municipal Light and
16 Power Revenue and Refunding Revenue Bonds, 1993, dated July 1, 1993 (the "1993 Bonds"),
17 in the original principal amount of Four Hundred Fifty-Three Million Three Hundred Fifty-Five
18 Thousand dollars (\$453,355,000), and reserved the right to redeem the 1993 Bonds maturing on
19 or after May 1, 2004, prior to their stated maturity dates on or after November 1, 2003, as a
20 whole or in part at any time, with the maturities to be redeemed to be selected by the City; and

18 WHEREAS, there are presently outstanding One Hundred Eighty-One Million Forty-Five Thousand
19 dollars (\$181,045,000) par value of 1993 Bonds maturing or subject to mandatory redemption
20 on May 1 and November 1 of each of the years 2004 through 2018, inclusive, and bearing
21 interest at various rates ranging from 5.000% to 5.500%; and

20 WHEREAS, after due consideration, it appears to the City Council that all or a portion of the 1992B
21 Bonds and the 1993 Bonds (the "Refundable Bonds") may be refunded by the issuance and sale
22 of the bonds authorized herein (the "Bonds") if the City Council determines by resolution it is in
23 the best interest of the City and the public to issue the Bonds to modify debt service
24 requirements and effect a saving by the difference between the principal and interest costs over
25 the life of the Bonds plus the costs of issuance of the Bonds and the principal and interest costs
26 over the life of the Refundable Bonds to be refunded but for such refunding; NOW,
THEREFORE,

BE IT ORDAINED BY THE CITY OF SEATTLE AS FOLLOWS:

26

1 Section 1. Definitions. As used in this ordinance, the following words and phrases shall
2 have the meanings set forth below.

3 “Accreted Value” means with respect to any Capital Appreciation Bonds (a) as of any
4 Valuation Date, the amount set forth for such date in any Parity Bond Ordinance authorizing such
5 Capital Appreciation Bonds and (b) as of any date other than a Valuation Date, the sum of (i) the
6 Accreted Value on the preceding Valuation Date and (ii) the product of (A) a fraction, the numerator
7 of which is the number of days having elapsed from the preceding Valuation Date and the
8 denominator of which is the number of days from such preceding Valuation Date to the next
9 succeeding Valuation Date, calculated based on the assumption that Accreted Value accrues during
10 any semiannual period in equal daily amounts on the basis of a year of twelve 30-day months, times
11 (B) the difference between the Accreted Values for such Valuation Dates.

12 “Acquired Obligations” means those United States Treasury Certificates of Indebtedness,
13 Notes and Bonds--State and Local Government Series and other direct, noncallable obligations of
14 the United States of America purchased to accomplish the refunding of the Refunded Bonds as
15 authorized by this ordinance.

16 “Adjusted Net Revenue” has the meaning assigned to that term in Section 17(f)(iii).

17 “Annual Debt Service” for any calendar year means the sum of the amounts required in such
18 calendar year to pay:

- 19 (a) the interest due in such calendar year on all Parity Bonds outstanding, excluding
20 interest to be paid from the proceeds of the sale of Parity Bonds or other bonds; and
21 (b) the principal of all outstanding Serial Bonds due in such calendar year; and
22 (c) the Sinking Fund Requirement, if any, for such calendar year.

23 For purposes of this definition, the principal and interest portions of the Accreted Value of
24 Capital Appreciation Bonds becoming due at maturity or by virtue of a Sinking Fund Requirement
25 shall be included in the calculations of accrued and unpaid and accruing interest or principal in such
26

1 manner and during such period of time as is specified in any Parity Bond Ordinance authorizing such
2 Capital Appreciation Bonds.

3 For purposes of calculating and determining compliance with the Reserve Fund Requirement
4 and conditions for the issuance of Future Parity Bonds and/or entering into Parity Payment
5 Agreements from and after the time when no 1992B Bonds remain outstanding:

6 (i) Generally. Except as otherwise provided by subparagraph (ii) with respect to
7 Variable Interest Rate Bonds and by subparagraph (iii) below with respect to Parity Bonds with
8 respect to which a Payment Agreement is in force, interest on any issue of Parity Bonds shall be
9 calculated based on the actual amount of accrued, accreted or otherwise accumulated interest that is
10 payable in respect of that issue taken as a whole, at the rate or rates set forth in the applicable Parity
11 Bond Ordinance;

12 (ii) Interest on Variable Interest Rate Bonds. The amount of interest deemed to be
13 payable on any issue of Variable Interest Rate Bonds shall be calculated on the assumption that the
14 interest rate on those bonds would be equal to the rate that is ninety percent (90%) of the average
15 RBI during the four calendar quarters preceding the quarter in which the calculation is made;

16 (iii) Interest on Parity Bonds With Respect to Which a Payment Agreement is in
17 Force. Debt service on Parity Bonds with respect to which a Payment Agreement is in force shall be
18 based on the net economic effect on the City expected to be produced by the terms of the Parity
19 Bonds and the terms of the Payment Agreement, including but not limited to the effects produced by
20 the following: (A) Parity Bonds that would, but for a Payment Agreement, be treated as obligations
21 bearing interest at a Variable Interest Rate instead shall be treated as obligations bearing interest at a
22 fixed interest rate, and (B) Parity Bonds that would, but for a Payment Agreement, be treated as
23 obligations bearing interest at a fixed interest rate instead shall be treated as obligations bearing
24 interest at a Variable Interest Rate. Accordingly, the amount of interest deemed to be payable on
25 any Parity Bonds with respect to which a Payment Agreement is in force shall be an amount equal to
26 the amount of interest that would be payable at the rate or rates stated in those Parity Bonds plus

1 Payment Agreement Payments minus Payment Agreement Receipts. For the purposes of calculating
2 as nearly as practicable Payment Agreement Receipts and Payment Agreement Payments under a
3 Payment Agreement that includes a variable rate component determined by reference to a pricing
4 mechanism or index that is not the same as the pricing mechanism or index used to determine the
5 variable rate interest component on the Parity Bonds to which the Payment Agreement is related, it
6 shall be assumed that the fixed rate used in calculating Payment Agreement Payments will be equal
7 to 105% of the fixed rate specified by the Payment Agreement and that the pricing mechanism or
8 index specified by the Payment Agreement is the same as the pricing mechanism or index specified
9 by the Parity Bonds. Notwithstanding the other provisions of this subparagraph (iii), the City shall
10 not be required to (but may in its discretion) take into account in determining Annual Debt Service
11 the effects of any Payment Agreement that has a term of ten (10) years or less;

12 (iv) Parity Payment Agreements. No additional debt service shall be taken into
13 account with respect to a Parity Payment Agreement for any period during which Payment
14 Agreement Payments on that Parity Payment Agreement are taken into account in determining
15 Annual Debt Service on related Parity Bonds under subparagraph (iii) of this definition. However,
16 for any period during which Payment Agreement Payments are not taken into account in calculating
17 Annual Debt Service on any outstanding Parity Bonds because the Parity Payment Agreement is not
18 then related to any outstanding Parity Bonds, payments on that Parity Payment Agreement shall be
19 taken into account by assuming:

20 (A) City Obligated to Make Payments Based on Fixed Rate. If the City is
21 obligated to make Payment Agreement Payments based on a fixed rate and the Qualified
22 Counterparty is obligated to make payments based on a variable rate index, that payments by the
23 City will be based on the assumed fixed payor rate, and that payments by the Qualified Counterparty
24 will be based on a rate equal to the average rate determined by the variable rate index specified by
25 the Parity Payment Agreement during the four calendar quarters preceding the quarter in which the
26 calculation is made, and

1 (B) City Obligated to Make Payments Based on Variable Rate Index. If
2 the City is obligated to make Payment Agreement Payments based on a variable rate index and the
3 Qualified Counterparty is obligated to make payment based on a fixed rate, that payments by the
4 City will be based on a rate equal to the average rate determined by the variable rate index specified
5 by the Parity Payment Agreement during the four calendar quarters preceding the quarter in which
6 the calculation is made, and that the Qualified Counterparty will make payments based on the fixed
7 rate specified by the Parity Payment Agreement.

8 "Bond Counsel" means a lawyer or a firm of lawyers, selected by the City, of nationally
9 recognized standing in matters pertaining to bonds issued by states and their political subdivisions.

10 "Bond Register" means the books or records maintained by the Bond Registrar for the
11 purpose of registration of the Bonds.

12 "Bond Registrar" or "Registrar" means the fiscal agency of the State of Washington, or any
13 successor bond registrar selected by the City, whose duties include the registration and
14 authentication of the Bonds, maintenance of the Bond Register, effecting transfer of ownership of
15 the Bonds, and paying the principal of and premium, if any, and interest on the Bonds.

16 "Bond Resolution" means the resolution or resolutions fixing certain provisions of the Bonds
17 and their sale as authorized by Section 2 of this ordinance.

18 "Bonds" means the bonds authorized to be issued pursuant to, under the authority of and for
19 the purposes provided in this ordinance.

20 "1992B Bonds" means the Municipal Light and Power Refunding Revenue Bonds,
21 Series 1992B of the City authorized by Ordinance 116290 and Resolution 28586.

22 "1993 Bonds" means the Municipal Light and Power Revenue and Refunding Revenue
23 Bonds, 1993, of the City authorized by Ordinance 116706, as amended by Ordinance 117300, and
24 Resolution 28751.

25 "1994 Bonds" means the Municipal Light and Power Revenue Bonds, 1994, of the City
26 authorized by Ordinance 117374 and Resolution 29043.

1 "1995 Bonds" means, collectively, the Municipal Light and Power Revenue Bonds, 1995,
2 Series A and B, of the City authorized by Ordinance 117758 and Resolutions 29198 and 29218,
3 respectively.

4 "1996 Bonds" means the Municipal Light and Power Revenue Bonds, 1996, of the City
5 authorized by Ordinance 118282 and Resolution 29477.

6 "1997 Bonds" means the Municipal Light and Power Revenue Bonds, 1997, of the City
7 authorized by Ordinance 118745 and Resolution 29686.

8 "1998A Bonds" means the Municipal Light and Power Refunding Revenue Bonds, 1998,
9 Series A, of the City authorized by Ordinance 118744 and Resolution 29687.

10 "1998B Bonds" means the Municipal Light and Power Refunding Revenue Bonds, 1998,
11 Series B, of the City authorized by Ordinance 119141 and Resolution 29851.

12 "1999 Bonds" means the Municipal Light and Power Revenue Bonds, 1999, of the City
13 authorized by Ordinance 119638 and Resolution 30065.

14 "2000 Bonds" means the Municipal Light and Power Revenue Bonds, 2000, of the City
15 authorized by Ordinance 120131 and Resolution 30274.

16 "2001 Bonds" means the Municipal Light and Power Improvement and Refunding Revenue
17 Bonds, 2001, of the City authorized by Ordinance 120274 and Resolution 30298.

18 "Capital Appreciation Bonds" means any Parity Bonds as to which interest is payable only at
19 the maturity or prior redemption of such Parity Bonds. For the purpose of (a) receiving payment of
20 the redemption premium, if any, of a Capital Appreciation Bond that is redeemed prior to maturity,
21 or (b) computing the principal amount of Parity Bonds held by the owner of a Capital Appreciation
22 Bond in giving to the City or the paying agent for those bonds any notice, consent, request, or
23 demand pursuant to this ordinance or for any purpose whatsoever, the principal amount of a Capital
24 Appreciation Bond shall be deemed to be its Accreted Value.

25 "City" means The City of Seattle, Washington, a municipal corporation duly organized and
26 existing under the laws of the State of Washington.

1 "City Council" means the City Council of the City, as duly and regularly constituted from
2 time to time.

3 "Code" means the Internal Revenue Code of 1986, as amended, or any successor thereto, and
4 all applicable regulations thereunder.

5 "DTC" means The Depository Trust Company, New York, New York, as initial Securities
6 Depository for the Bonds.

7 "Director of Finance" means the Director of Finance of the City, or any successor thereto.

8 "Future Parity Bonds" means any fixed or variable rate revenue bonds of the City (other than
9 the Bonds) issued hereafter having a charge or lien upon the Gross Revenues for payment of the
10 principal thereof and interest thereon equal in priority to the charge or lien upon the Gross Revenues
11 of the Light System for the payment of the principal of and interest on the Outstanding Parity Bonds
12 and the Bonds. From and after the time when no 1992B Bonds remain outstanding, Future Parity
13 Bonds may include Parity Payment Agreements and any other obligations issued in compliance with
14 Section 17(f) or 17(g).

15 "Government Obligations" means direct obligations of, or obligations the principal of and
16 interest on which are unconditionally guaranteed by, the United States Government.

17 "Gross Revenues" means (a) all income, revenues, receipts and profits derived by the City
18 through the ownership and operation of the Light System; (b) the proceeds received by the City
19 directly or indirectly from the sale, lease or other disposition of any of the properties, rights or
20 facilities of the Light System; (c) Payment Agreement Receipts, to the extent that such receipts are
21 not offset by Payment Agreement Payments; and (d) the investment income earned on money held in
22 any fund or account of the City, including any bond redemption funds and the accounts therein, in
23 connection with the ownership and operation of the Light System. Gross Revenues do not include:
24 (A) insurance proceeds compensating the City for the loss of a capital asset; (B) income derived
25 from investments irrevocably pledged to the payment of any defeased bonds payable from Gross
26 Revenues; (C) investment income earned on money in any fund or account created or maintained

1 solely for the purpose of complying with the arbitrage rebate provisions of the Code; (D) any gifts,
2 grants, donations or other funds received by the City from any State or federal agency or other
3 person if such gifts, grants, donations or other funds are the subject of any limitation or reservation
4 imposed by the donor or grantor or imposed by law or administrative regulation to which the donor
5 or grantor is subject, limiting the application of such funds in a manner inconsistent with the
6 application of Gross Revenues hereunder; (E) the proceeds of any borrowing for capital
7 improvements (or the refinancing thereof); and (F) the proceeds of any liability or other insurance
8 (excluding business interruption insurance or other insurance of like nature insuring against the loss
9 of revenues).

10 "Letter of Representations" means the Letter of Representations relating to the Bonds to be
11 delivered by the City to DTC.

12 "Light Fund" means the special fund of the City of that name heretofore created and
13 established by the City Council.

14 "Light System" means the municipal light and power plant and system now belonging to or
15 which may hereafter belong to the City.

16 "Mayor" means the Mayor of the City.

17 "Moody's" means Moody's Investors Service, Inc.

18 "Net Revenue" for any period has the meaning assigned to that term in Section 17(f).

19 "New Covenant Date" means the date on which no 1992B Bonds, 1993 Bonds, 1994 Bonds,
20 1995 Bonds, 1996 Bonds, 1997 Bonds, 1998A Bonds, 1998B Bonds, 1999 Bonds or 2000 Bonds
21 remain outstanding under the respective ordinances authorizing the issuance of such bonds.

22 "Outstanding Parity Bonds" means, collectively, the outstanding 1992B Bonds, 1993 Bonds,
23 1994 Bonds, 1995 Bonds, 1996 Bonds, 1997 Bonds, 1998A Bonds, 1998B Bonds, 1999 Bonds,
24 2000 Bonds, and 2001 Bonds.

25 "Parity Bond Fund" means the Seattle Municipal Light Revenue Parity Bond Fund
26 established pursuant to Ordinance 92938 and now treated as a separate account within the Light Fund.

1 "Parity Bond Ordinance" means any ordinance or resolution passed or adopted by the City
2 Council providing for the issuance of Parity Bonds, and any other ordinance or resolution amending
3 or supplementing the provisions of any Parity Bond Ordinance as originally passed or adopted or as
4 theretofore amended or supplemented.

5 "Parity Bonds" means the Outstanding Parity Bonds, the Bonds and any Future Parity Bonds.

6 "Parity Payment Agreement" means a Payment Agreement entered into on or after the date
7 when no 1992B Bonds remain outstanding, under which the City's obligations are expressly stated
8 to constitute a charge and lien on the Net Revenue of the Light System equal in rank with the charge
9 and lien upon such Net Revenue required to be paid into the Parity Bond Fund to pay and secure the
10 payment of the principal of and interest on Parity Bonds.

11 "Payment Agreement" means a written contract entered into, for the purpose of managing or
12 reducing the City's exposure to fluctuations or levels of interest rates or for other interest rate,
13 investment, asset or liability management purposes, by the City and a Qualified Counterparty on
14 either a current or forward basis as authorized by any applicable laws of the State in connection with,
15 or incidental to, the issuance, incurring or carrying of particular bonds, notes, bond anticipation
16 notes, commercial paper or other obligations for borrowed money, or lease, installment purchase or
17 other similar financing agreements or certificates of participation therein, that provides for an
18 exchange of payments based on interest rates, ceilings or floors on such payments, options on such
19 payments, or any combination thereof or any similar device.

20 "Payment Agreement Payments" means the amounts, periodically required to be paid by the
21 City to the Qualified Counterparty pursuant to a Payment Agreement.

22 "Payment Agreement Receipts" means the amounts periodically required to be paid by the
23 Qualified Counterparty to the City pursuant to a Payment Agreement.

24 "Permitted Investments" means any investments or investment agreements permitted for the
25 investment of City funds under the laws of the State of Washington as amended from time to time.
26

1 "Professional Utility Consultant" means the independent person(s) or firm(s) selected by the
2 City having a favorable reputation for skill and experience with electric systems of comparable size
3 and character to the Light System in such areas as are relevant to the purposes for which they were
4 retained.

5 "Qualified Counterparty" means a party (other than the City or a person related to the City)
6 who is the other party to a Payment Agreement and who is qualified to act as the other party to a
7 Payment Agreement under any applicable laws of the State.

8 "Qualified Insurance" means any municipal bond insurance policy or surety bond issued by
9 any insurance company licensed to conduct an insurance business in any state of the United States
10 (or by a service corporation acting on behalf of one or more such insurance companies) which
11 insurance company or companies, as of the time of issuance of such policy or surety bond, are rated in
12 one of the two highest rating categories by Moody's and S&P or their comparably recognized business
13 successors.

14 "Qualified Letter of Credit" means any letter of credit issued by a financial institution for the
15 account of the City on behalf of the owners of Parity Bonds, which institution maintains an office,
16 agency or branch in the United States and as of the time of issuance of such letter of credit is rated in
17 one of the two highest rating categories by Moody's and S&P or their comparably recognized
18 business successors.

19 "Rate Stabilization Account" means the fund of that name created in the Light Fund for the
20 purposes described in this ordinance.

21 "RBI" means The Bond Buyer Revenue Bond Index or comparable index, or, if no
22 comparable index can be obtained, eighty percent (80%) of the interest rate for actively traded thirty
23 (30) year United States Treasury obligations.

24 "Refundable Bonds" means, the 1992B Bonds and the 1993 Bonds.

25 "Refunded Bonds" means all or that portion of the Refundable Bonds included in a
26 Refunding Plan.

1
2 "Refunded Bond Ordinance" means one or more of the ordinances and resolutions pursuant
3 to which the Refunded Bonds were issued.

4 "Refunding Parity Bonds" means Parity Bonds issued for the purpose of refunding bonds of
5 any prior series of Parity Bonds.

6 "Refunding Plan" means, for any series of Bonds:

7 (a) the placement of sufficient proceeds of the Bonds which, with other money of the
8 City, if necessary, will acquire the Acquired Obligations, if any, to be deposited, with cash, if
9 necessary, with the Refunding Trustee;

10 (b) the payment of the principal of and interest on the Refunded Bonds when due up to
11 and including the date set forth in the Bond Resolution, and the call, payment and redemption on that
12 date of all or a portion of the then-outstanding Refunded Bonds, at the price set forth in the Bond
13 Resolution; and

14 (c) the payment of the costs of issuing the Bonds and the costs of carrying out the
15 foregoing elements of the Refunding Plan.

16 "Refunding Trust Agreement" means the Refunding Trust Agreement between the City and a
17 Refunding Trustee relating to a particular series of Bonds.

18 "Refunding Trustee" means the trustee or escrow agent, or any successor trustee or escrow
19 agent, with respect to a particular series of Bonds, designated by the Director of Finance.

20 "Reserve Fund" means the Municipal Light and Power Bond Reserve Fund established
21 pursuant to Ordinance 71917, as amended, and now treated as a separate account within the Light
22 Fund.

23 "Reserve Fund Requirement" means, at any time, the lesser of (a) the maximum Annual Debt
24 Service on all Parity Bonds then outstanding; and (b) the maximum amount permitted by the Code as
25 a "reasonably required reserve or replacement fund." *Notwithstanding the foregoing, on the New*
26 *Covenant Date, "Reserve Fund Requirement" shall mean, for any issue of Future Parity Bonds, the*

1 *Reserve Fund Requirement specified for that issue, and the Reserve Fund Requirement for all series of*
2 *Future Parity Bonds shall be the sum of the Reserve Fund Requirement for all such Future Parity*
3 *Bonds.*

4 "S&P" means Standard & Poor's Ratings Services, a Division of The McGraw-Hill
5 Companies, Inc.

6 "Securities Depository" means any one of the following registered securities depositories
7 which has been designated by the City: (i) DTC; (ii) Midwest Securities Trust Company, Chicago,
8 Illinois, (iii) Philadelphia Depository Trust Company, Philadelphia, Pennsylvania; or (iv) such other
9 securities depositories as the City may designate in a certificate of the City delivered to the Bond
10 Registrar.

11 "Serial Bonds" means Parity Bonds maturing in specified years, for which no Sinking Fund
12 Requirements are mandated.

13 "Sinking Fund Account" means any account created in the Parity Bond Fund to amortize the
14 principal or make mandatory redemptions of Term Bonds.

15 "Sinking Fund Requirement" means, for any calendar year, the principal amount and
16 premium, if any, of Term Bonds required to be purchased, redeemed, paid at maturity or paid into
17 any Sinking Fund Account for such calendar year as established by the Parity Bond Ordinance
18 authorizing the issuance of such Term Bonds.

19 "State" means the State of Washington.

20 "Subordinate Lien Bonds" means, collectively, the City's outstanding Municipal Light and
21 Power Adjustable Rate Revenue Bonds, 1990, Municipal Light and Power Adjustable Rate Revenue
22 Bonds, 1991, Series A and B, Municipal Light and Power Adjustable Rate Revenue Bonds, 1993,
23 and Municipal Light and Power Revenue Bonds, 1996, and any bonds issued hereafter, having a
24 charge or lien upon the Gross Revenues of the Light System on a parity with those bonds.
25
26

1 "Term Bonds" means any Parity Bonds identified as such in the Parity Bond Ordinance
2 authorizing the issuance thereof, which Parity Bond Ordinance requires that all or a portion of such
3 bonds be purchased, redeemed or paid prior to maturity in a schedule established thereby.

4 "Valuation Date" means, with respect to any Capital Appreciation Bonds, the date or dates
5 set forth in any Parity Bond Ordinance authorizing such Parity Bonds on which specific Accreted
6 Values are assigned to the Capital Appreciation Bonds.

7 "Variable Interest Rate" means any variable interest rate or rates to be borne by any Parity
8 Bonds. The method of computing such a variable interest rate shall be as specified in the Parity
9 Bond Ordinance authorizing or specifying the terms of such Parity Bonds, which Parity Bond
10 Ordinance also shall specify either (i) the particular period or periods of time or manner of
11 determining such period or periods of time for which each value of such variable interest rate shall
12 remain in effect or (ii) the time or times upon which any change in such variable interest rate shall
13 become effective.

14 "Variable Interest Rate Bonds" means, for any period of time, any Parity Bonds that bear a
15 Variable Interest Rate during that period, except that Parity Bonds shall not be treated as Variable
16 Interest Rate Bonds if the net economic effect of interest rates on particular Parity Bonds of an issue
17 and interest rates on other Parity Bonds of the same issue, as set forth in the applicable Parity Bond
18 Ordinance, or the net economic effect of a Payment Agreement with respect to particular Parity
19 Bonds, in either case is to produce obligations that bear interest at a fixed interest rate; and Parity
20 Bonds with respect to which a Payment Agreement is in force shall be treated as Variable Interest
21 Rate Bonds if the net economic effect of the Payment Agreement is to produce obligations that bear
22 interest at a Variable Interest Rate.

23 Section 2. Authorization and Description of Bonds. For the purpose of providing all or
24 part of the funds with which to pay the costs of refunding the Refunded Bonds and of issuing and
25 selling the Bonds, the City shall issue and sell the Bonds in the aggregate principal amount of not to
26 exceed Two Hundred Forty-Five Million dollars (\$245,000,000). The Bonds may be issued in one

1 or more series, except that the final series shall be issued on or before December 31, 2004; may be
2 combined with other Parity Bonds authorized separately; shall be called "The City of Seattle,
3 Washington, Municipal Light and Power Refunding Revenue Bonds, 2002" (unless changed by
4 resolution); may have such different or further designation or designations as determined by the
5 Director of Finance or as the City Council may specify in a resolution or resolutions fixing the terms
6 of and matters relating to the Bonds (collectively, the "Bond Resolution"); shall be dated and shall
7 mature on such date or dates specified in the Bond Resolution, except that the final maturity date of
8 the Bonds shall not extend beyond December 31, 2034; shall be issued in fully registered form; shall
9 be numbered separately in the manner and with any additional designation as the Bond Registrar for
10 the Bonds deems necessary for purposes of identification; shall bear interest at the rate or rates
11 (computed on the basis of a 360-day year of twelve 30-day months) specified in the Bond
12 Resolution, except that the net interest cost shall not exceed a weighted average rate of 7.5% per
13 annum, payable at the times specified in the Bond Resolution; and shall have such denominations,
14 mature on such dates and be subject to optional or mandatory redemption, open market purchase or
15 defeasance on the terms and at the times specified in the Bond Resolution. The Director of Finance
16 may designate Term Bonds with mandatory redemption amounts, all to be provided by the Bond
17 Resolution.

18 Notwithstanding the foregoing, the initial series of Bonds shall be issued in the maximum
19 principal amount of \$130,000,000 for the purpose of refunding all or a portion of the 1992B Bonds
20 and all or a portion of the portion of the 1993 Bonds that may be advance refunded. The Finance
21 Director shall consult with the City Council before any additional series of the Bonds are offered for
22 sale pursuant to this Ordinance.

23 The City Council may adopt the Bond Resolution and may provide therein for the matters
24 described in this ordinance, including the manner of sale of the Bonds, which may include a forward
25 or delayed delivery, and such other matters that the City Council deems necessary and appropriate to
26

1 carry out the purposes of this ordinance. Once adopted, the Bond Resolution shall be deemed a part
2 of this ordinance as if set forth herein.

3 The Bond Resolution may provide for Qualified Insurance or a Qualified Letter of Credit,
4 and conditions or covenants relating thereto, including additional terms, conditions and covenants
5 relating to the Bonds that are required by the bond insurer or letter of credit provider and are
6 consistent with the provisions of this ordinance, including but not limited to restrictions on
7 investments and requirements of notice to and consent of the bond insurer or letter of credit provider.

8 The Bond Resolution may approve and authorize the execution and delivery on behalf of the
9 City of any contracts consistent with the provisions of this ordinance for which the City's approval is
10 necessary or to which the City is a party and that are related or incidental to the initial issuance and
11 sale of the Bonds, the initial establishment of the interest rate or rates on the Bonds and any
12 redemption of the Bonds, including but not limited to Payment Agreements and similar contracts for
13 such purposes.

14 Section 3. Registration and Transfer or Exchange of Bonds. The Bonds shall be issued
15 only in registered form as to both principal and interest and recorded on the Bond Register. The
16 Bond Register shall contain the name and mailing address of the registered owner of each Bond and
17 the principal amount and number of each of the Bonds held by each registered owner.

18 Bonds surrendered to the Bond Registrar may be exchanged for Bonds in any authorized
19 denomination of an equal aggregate principal amount and of the same series, interest rate and
20 maturity. Bonds may be transferred only if endorsed in the manner provided thereon and
21 surrendered to the Bond Registrar. Any exchange or transfer shall be without cost to the registered
22 owner or transferee. The Bond Registrar shall not be obligated to exchange or transfer any Bond
23 during the period between any record date and the next succeeding principal or interest payment or
24 redemption date.

25 The City appoints DTC as initial Securities Depository for the Bonds. For so long as DTC is
26 the Securities Depository for the Bonds, DTC shall be deemed to be the registered owner of the

1 Bonds for all purposes hereunder, and all references in this ordinance or the Bond Resolution to the
2 registered owners of the Bonds shall mean DTC or its nominee and shall not mean the owners of any
3 beneficial interests in the Bonds. Payments of principal of and interest on all outstanding Bonds
4 registered in the name of the nominee of DTC, or its registered assign, shall be made as provided in
5 the Letter of Representations.

6 Bonds executed and delivered in fully immobilized form shall be executed and delivered in
7 the form of one fully-registered immobilized certificate for each series and maturity of the Bonds
8 representing the aggregate principal amount of the Bonds of that series and maturity, which Bonds
9 shall (except as provided below for the discontinuation or substitution of Securities Depository) be
10 registered in the name of the Securities Depository or its nominee. For so long as DTC serves as
11 Securities Depository for the Bonds, the Bonds shall be registered in the name of Cede & Co., as
12 nominee of DTC; however, if DTC shall request that the Bonds be registered in the name of a
13 different nominee, the Bond Registrar shall exchange all or any portion of the Bonds for an equal
14 aggregate principal amount of Bonds registered in the name of such other nominee or nominees of
15 DTC. No person other than DTC or its nominee shall be entitled to receive from the City or the
16 Bond Registrar any Bond or any other evidence of ownership of the Bonds, or any right to receive
17 any payment in respect thereof, unless DTC or its nominee shall transfer record ownership of all or
18 any portion of the Bonds on the Bond Register, in connection with discontinuing the book-entry
19 system as provided below or otherwise.

20 So long as the Bonds are registered in the name of DTC or any nominee thereof, all payments
21 of the principal of, premium, if any, or interest on the Bonds shall be made to DTC or its nominee in
22 immediately available funds on the dates provided for such payments under this ordinance and the
23 Bond Resolution and at such times and in the manner provided in the Letter of Representations.
24 Each such payment to DTC or its nominee shall be valid and effective to fully discharge all liability
25 of the City or the Bond Registrar with respect to the principal of, premium, if any, or interest on the
26 Bonds to the extent of the sum or sums so paid. In the event of the redemption of less than all of the

1 Bonds of any series and maturity, the Bond Registrar shall not require surrender by DTC or its
2 nominee of the Bonds so redeemed, and DTC or its nominee may retain such Bonds and make an
3 appropriate notation thereon as to the amount of such partial redemption. DTC shall deliver to the
4 Bond Registrar, upon request, a written confirmation of such partial redemption. The records
5 maintained by the Bond Registrar shall be conclusive as to the amount of the Bonds of such series
6 and maturity that have been redeemed.

7 All transfers of beneficial ownership interests in Bonds registered in the name of DTC or its
8 nominee shall be effected by the procedures of DTC's participants and/or indirect participants for
9 recording and transferring the ownership of beneficial interests in bonds.

10 The City and the Bond Registrar may treat DTC, or any nominee thereof, as the sole and
11 exclusive registered owner of the Bonds registered in such name for the purposes of payment of the
12 principal of, premium, if any, or interest on those Bonds, selecting Bonds or portions thereof to be
13 redeemed, giving any notice permitted or required to be given to registered owners of Bonds under
14 this ordinance or the Bond Resolution, registering the transfer of Bonds, obtaining any consent or other
15 action to be taken by registered owners of Bonds and for all other purposes whatsoever; and the City
16 and the Bond Registrar shall not be affected by any notice to the contrary. The City and the Bond
17 Registrar shall not have any responsibility or obligation to any direct or indirect DTC participant, any
18 person claiming a beneficial ownership interest in the Bonds under or through DTC or any such direct
19 or indirect participant, or any other person which is not shown on the Bond Register as being a
20 registered owner of Bonds, with respect to: (1) the Bonds; (2) any records maintained by DTC or any
21 such direct or indirect participant; (3) the payment by DTC or any such direct or indirect participant of
22 any principal of, premium, if any, or interest on the Bonds; (4) any notice which is permitted or required
23 to be given to registered owners of Bonds under this ordinance or the Bond Resolution; (5) the selection
24 by DTC or any direct or indirect participant of any person to receive payment in the event of a partial
25 redemption of the Bonds; or (6) any consent given or other action taken by DTC as registered owner of
26 the Bonds.

1 So long as the Bonds are registered in the name of DTC or any nominee thereof, all notices
2 required or permitted to be given to the registered owners of such Bonds under this ordinance or the
3 Bond Resolution shall be given to DTC as provided in the Letter of Representations, in form and
4 content satisfactory to DTC, the City and the Bond Registrar.

5 In connection with any notice or other communication to be provided to registered owners
6 pursuant to this ordinance or the Bond Resolution by the City or the Bond Registrar with respect to
7 any consent or other action to be taken by registered owners of the Bonds, DTC shall consider the
8 date of receipt of notice requesting such consent or other action as the record date for such consent
9 or other action; however, the City or the Bond Registrar may establish a special record date for such
10 consent or other action and shall give DTC notice of such special record date not less than fifteen
11 (15) calendar days in advance of such special record date to the extent possible.

12 Any successor Bond Registrar, in its written acceptance of its duties under this ordinance and
13 the Bond Resolution, shall agree to take any actions necessary from time to time to comply with the
14 requirements of the Letter of Representations.

15 The book-entry system for registration of the ownership of the Bonds in fully immobilized
16 form may be discontinued at any time if: (1) after notice to the City and the Bond Registrar, DTC
17 determines to resign as Securities Depository for the Bonds; or (2) after notice to DTC and the Bond
18 Registrar, the City determines that a continuation of the system of book-entry transfers through DTC (or
19 through a successor Securities Depository) is not in the best interests of the City. In each of such events
20 (unless, in the case described in clause (1) above, the City appoints a successor Securities Depository),
21 the Bonds shall be delivered in registered certificate form to such persons, and in such maturities and
22 principal amounts, as may be designated by DTC, but without any liability on the part of the City or the
23 Bond Registrar for the accuracy of such designation. Whenever DTC requests the City and the Bond
24 Registrar to do so, or whenever the City requests DTC and the Bond Registrar to do so after the
25 determination by the City to replace DTC with a successor Securities Depository, the City and the Bond
26

1 Registrar shall cooperate with DTC in taking appropriate action after reasonable notice to arrange for
2 another Securities Depository to maintain custody of certificates evidencing the Bonds.

3 Section 4. Mutilated, Lost, Stolen and Destroyed Bonds. In case any Bonds issued
4 hereunder shall become mutilated or be destroyed, stolen or lost, the City may, if not then prohibited
5 or otherwise required by law, cause to be executed and delivered a new Bond of like amount, series,
6 interest rate, maturity date and tenor in exchange and substitution for and upon cancellation of such
7 mutilated Bonds, or in lieu of and in substitution for such destroyed, stolen or lost Bonds, upon
8 payment by the registered owner thereof of the reasonable expenses and charges of the City and the
9 Bond Registrar in connection therewith, and in the case of a Bond destroyed, stolen or lost, the filing
10 with the Bond Registrar of evidence satisfactory to the City that such Bond was destroyed, stolen or
11 lost, and of the ownership thereof, and furnishing the City and the Bond Registrar with indemnity
12 satisfactory to each of them. If the mutilated, destroyed, stolen or lost Bond already has matured or
13 been called for redemption in accordance with its terms it shall not be necessary to issue a new Bond
14 prior to payment.

15 Section 5. Payment of Bond Principal and Interest. Principal of, premium, if any, on and
16 interest on the Bonds shall be payable in lawful money of the United States of America. Interest on
17 the Bonds shall be paid by checks or drafts mailed by the Bond Registrar on the interest payment
18 date to the registered owners at the addresses appearing on the Bond Register on the fifteenth day of
19 the month preceding the interest payment date (or other record date established in the Bond
20 Resolution, the "Record Date") or, at the request of the registered owner of One Million dollars
21 (\$1,000,000) or more in aggregate principal amount of Bonds, by wire transfer to an account in the
22 United States designated in writing by such registered owner prior to the Record Date. Principal of
23 and premium, if any, on the Bonds shall be payable upon presentation and surrender of the Bonds by
24 the registered owners at either of the principal corporate trust office or offices of the Bond Registrar
25 at the option of the owners. Notwithstanding the foregoing, payment of any Bonds registered in the
26 name of DTC or its nominee, shall be made in accordance with the Letter of Representations.

1 The Bonds shall be payable solely out of the Parity Bond Fund and shall not be general
2 obligations of the City.

3 Section 6. Redemption and Open Market Purchase of Bonds.

4 (a) Optional Redemption. All or some of the Bonds may be subject to redemption at the
5 option of the City at the times and on the terms set forth in the Bond Resolution.

6 (b) Mandatory Redemption. The City shall redeem any Term Bonds, if not redeemed
7 under the optional redemption provisions set forth in the Bond Resolution or purchased in the open
8 market under the provisions set forth below, by lot (or in such other manner as the Bond Registrar
9 shall determine) at par plus accrued interest on the dates and in the years and principal amounts as
10 set forth in the Bond Resolution.

11 If the City redeems Term Bonds under the optional redemption provisions set forth in the
12 Bond Resolution or purchases Term Bonds in the open market as set forth below, the Term Bonds so
13 redeemed or purchased (irrespective of their redemption or purchase price) shall be credited at the
14 par amount thereof against the remaining mandatory redemption requirements in a manner to be
15 determined by the Director of Finance or, if no such determination is made, on a pro-rata basis.

16 (c) Partial Redemption. Whenever less than all of the Bonds of a single maturity are to
17 be redeemed, the Bond Registrar shall select the Bonds or portions thereof to be redeemed from the
18 Bonds of that maturity by lot, or in such other manner as the Bond Registrar shall determine, except
19 that, so long as the Bonds are registered in the name of DTC or its nominee, DTC shall select the
20 Bonds or portions thereof to be redeemed in accordance with the Letter of Representations. In no
21 event shall any Bond be outstanding in a principal amount that is not an authorized denomination.

22 Portions of the principal amount of any Bond, in integral multiples of Five Thousand dollars
23 (\$5,000), may be redeemed, unless otherwise provided in the Bond Resolution. If less than all of the
24 principal amount of any Bond is redeemed, upon surrender of that Bond at either of the principal
25 offices of the Bond Registrar, there shall be issued to the registered owner, without charge therefor, a
26 new Bond (or Bonds, at the option of the registered owner) of the same series, maturity and interest

1 rate in any of the denominations authorized by the Bond Resolution in the aggregate total principal
2 amount remaining unredeemed.

3 (d) Open Market Purchase. The City reserves the right and option to purchase any or all
4 of the Bonds in the open market at any time at any price acceptable to the City plus accrued interest
5 to the date of purchase.

6 (e) Bonds to be Cancelled. All Bonds purchased or redeemed under this Section 6 shall
7 be cancelled.

8 Section 7. Notice of Redemption. The City shall cause notice of any intended
9 redemption of Bonds to be given not less than thirty (30) nor more than sixty (60) days prior to the
10 date fixed for redemption by first-class mail, postage prepaid, to the registered owner of any Bond to
11 be redeemed at the address appearing on the Bond Register at the time the Bond Registrar prepares
12 the notice, and the requirements of this sentence shall be deemed to have been fulfilled when notice
13 has been mailed as so provided, whether or not it is actually received by the registered owner of any
14 Bond. Interest on Bonds called for redemption shall cease to accrue on the date fixed for redemption
15 unless the Bond or Bonds called are not redeemed when presented pursuant to the call. In addition,
16 the redemption notice shall be mailed by the Bond Registrar within the same period, postage
17 prepaid, to Moody's and S&P at their offices in New York, New York, or their successors, to any
18 bond insurer for the Bonds, and to such other persons and with such additional information as the
19 Director of Finance shall determine or as specified in the Bond Resolution, but these additional
20 mailings shall not be a condition precedent to the redemption of Bonds.

21 Section 8. Failure to Redeem Bonds. If any Bond is not redeemed when properly
22 presented at its maturity or call date, the City shall be obligated to pay interest on that Bond at the
23 same rate provided in the Bond from and after its maturity or call date until that Bond, principal,
24 premium, if any, and interest, is paid in full or until sufficient money for its payment in full is on
25 deposit in the Parity Bond Fund and the Bond has been called for payment by giving notice of that
26 call to the registered owner of each of those unpaid Bonds.

1 which are a charge or lien upon the Gross Revenues of the Light System subordinate to the payments
2 required to be made therefrom into the Parity Bond Fund and the accounts therein.

3 Section 12. Execution of Refunding Plan(s).

4 (a) Appointment of Refunding Trustee. The Refunding Trustee, if any, for each series of
5 Refunded Bonds shall be designated by the Director of Finance and confirmed by the Bond
6 Resolution.

7 (b) Use of Bond Proceeds; Acquisition and Substitution of Acquired Obligations. Sufficient
8 proceeds of the sale of the Bonds shall be deposited immediately upon the receipt thereof with the
9 Bond Registrar for the Refunded Bonds or with the Refunding Trustee, as specified in the Bond
10 Resolution, and used to discharge the obligations of the City relating to the Refunded Bonds to be
11 refunded therewith under the respective Refunded Bond Ordinances by providing for the payment of
12 the amounts required to be paid by the Refunding Plan. The Refunding Plan shall be carried out, and
13 proceeds of the Bonds allocable to the refunding purposes shall be applied, in accordance with this
14 ordinance, the respective Refunded Bond Ordinances, the Bond Resolution and the laws of the State.
15 To the extent practicable, such obligations shall be discharged fully by the Refunding Trustee's
16 simultaneous purchase of the Acquired Obligations, bearing such interest and maturing as to
17 principal and interest in such amounts and at such times so as to provide, together with a beginning
18 cash balance, if necessary, for the payment of the amount required to be paid by the Refunding Plan.
19 The Acquired Obligations shall be listed and more particularly described in a schedule attached to
20 the Refunding Trust Agreement, but are subject to substitution as set forth below.

21 Prior to the purchase of any such Acquired Obligations, the City reserves the right to
22 substitute other Government Obligations for any of the Acquired Obligations and to use any savings
23 created thereby for any lawful City purpose if, (a) in the opinion of Bond Counsel, the interest on the
24 Bonds and the Refunded Bonds will remain excluded from gross income for federal income tax
25 purposes under Sections 103, 148 and 149(d) of the Code, and (b) such substitution shall not impair
26

1 the timely payment of the amounts required to be paid by the Refunding Plan, as verified by a
2 nationally recognized firm of independent certified public accountants.

3 After the purchase of the Acquired Obligations by the Refunding Trustee, the City reserves
4 the right to substitute therefor cash or Government Obligations subject to the conditions that such
5 money or securities held by the Refunding Trustee shall be sufficient to carry out the Refunding
6 Plan, that such substitution will not cause the Bonds or the Refunded Bonds to be arbitrage bonds
7 within the meaning of Section 148 of the Code and regulations thereunder in effect on the date of
8 such substitution and applicable to obligations issued on the issue date of the Bonds, and that the
9 City obtain: (1) verification by a nationally recognized independent certified public accounting firm
10 reasonably acceptable to the Refunding Trustee confirming that the payments of principal of and
11 interest on the Government Obligations, if paid when due, and any other money held by the
12 Refunding Trustee will be sufficient to carry out the Refunding Plan; and (2) an opinion from Bond
13 Counsel to the effect that the disposition and substitution or purchase of such securities, under the
14 statutes, rules and regulations then in force and applicable to the Bonds, will not cause the interest on
15 the Bonds or the Refunded Bonds to be included in gross income for federal income tax purposes
16 and that such disposition and substitution or purchase is in compliance with the statutes and
17 regulations applicable to the Bonds. Any surplus money resulting from the sale, transfer, or other
18 disposition or redemption of the Acquired Obligations and the substitutions therefor shall be released
19 from the trust estate and transferred to the Light Fund to be used for any lawful purpose.

20 (c) Administration of Refunding Plan. The Refunding Trustee is authorized and directed to
21 purchase the Acquired Obligations (or substitute obligations) and to make the payments required to
22 be made by the Refunding Plan from the Acquired Obligations (or substitute obligations) and money
23 deposited with the Refunding Trustee pursuant to this ordinance. All Acquired Obligations (or
24 substitute obligations) and the money deposited with the Refunding Trustee and any income
25 therefrom shall be held irrevocably, invested and applied in accordance with the provisions of the
26 respective Refunded Bond Ordinances, this ordinance, the Bond Resolution, chapter 39.53 RCW and

1 other applicable statutes of the State of Washington and the Refunding Trust Agreement. All
2 necessary and proper fees, compensation and expenses of the Refunding Trustee and all other costs
3 incidental to the setting up of the escrow to accomplish the refunding of the Refunded Bonds and
4 costs related to the issuance and delivery of the Bonds, including bond printing, verification fees,
5 Bond Counsel's fees and other related expenses, shall be paid out of the proceeds of the Bonds.

6 (d) Authorization for Refunding Trust Agreement. To carry out the Refunding Plan provided
7 for by this ordinance, the Director of Finance is authorized and directed to execute and deliver to the
8 Refunding Trustee, in connection with each series of Bonds, a Refunding Trust Agreement
9 substantially in the form approved by the Bond Resolution setting forth the duties, obligations and
10 responsibilities of the Refunding Trustee in connection with the payment, redemption and retirement
11 of the Refunded Bonds as provided herein and in the Bond Resolution and stating that the provisions
12 for payment of the fees, compensation and expenses of such Refunding Trustee set forth therein are
13 satisfactory to it. Prior to executing the Refunding Trust Agreement, the Director of Finance is
14 authorized to make such changes therein which do not change the substance and purpose thereof or
15 which assure that the escrow provided therein and the Bonds are in compliance with the
16 requirements of federal law governing the exclusion of interest on the Bonds from gross income for
17 federal income tax purposes.

18 Section 13. Calls for Redemption of the Refunded Bonds. As a part of the Refunding
19 Plan, the City shall call the Refunded Bonds for redemption on the dates and at the prices set forth in
20 the Bond Resolution. Such calls for redemption of the Refunded Bonds shall be irrevocable after the
21 delivery to the initial purchaser thereof of the applicable series of Bonds. The dates on which the
22 Refunded Bonds are called for redemption shall be the earliest dates on which those bonds may be
23 called for redemption.

24 The proper officials of the City are authorized and directed to give or cause to be given such
25 notices as required, at the times and in the manner required pursuant to the respective Refunded
26 Bond Ordinances in order to effect the redemption prior to maturity of the Refunded Bonds.

1 Section 14. City Findings with Respect to Refunding. The refunding of the Refunded
2 Bonds, or any portion thereof, shall be carried out only if the City Council finds and determines by
3 the Bond Resolution that the issuance and sale of Bonds will effect savings to the City and its
4 ratepayers and/or otherwise will be in the best interest of the City and in the public interest. In
5 making such findings and determinations, the City Council shall give consideration to the fixed
6 maturities and scheduled redemptions of the Bonds, the costs of issuance of the Bonds and the
7 known earned income from the investment of the proceeds of the issuance and sale of the Bonds and
8 other money, if any, of the City used in the refunding pending payment and redemption of the
9 Refunded Bonds.

10 The refunding of the Refunded Bonds, or any portion thereof, shall be carried out only if the
11 City Council further finds and determines that the money to be deposited with the Bond Registrar for
12 the Refunded Bonds and/or the Refunding Trustee in accordance with this ordinance and the Bond
13 Resolution will discharge and satisfy the obligations of the City with respect to the Refunded Bonds
14 under the respective Refunded Bond Ordinances, and the pledges, charges, trusts, covenants and
15 agreements of the City therein made or provided for as to the Refunded Bonds, and that the
16 Refunded Bonds shall no longer be deemed to be outstanding under such ordinances immediately
17 upon the deposit of such money.

18 Section 15. City Findings of Sufficiency of Revenues. The Bonds shall be issued only if
19 the City Council finds and determines by the Bond Resolution that the issuance and sale of the
20 Bonds is in the best interest of the City and in the public interest. In making such findings and
21 determinations, the City Council shall give due regard to the cost of operation and maintenance of
22 the Light System and to any portion of the Gross Revenues pledged for the payment of any bonds,
23 warrants or other indebtedness, and shall find and determine that the Gross Revenues, at the rates
24 established from time to time consistent with Section 17(c) of this ordinance, will be sufficient, in
25 the judgment of the City Council, to meet all expenses of operation and maintenance of the Light
26

1 System and to provide the amounts previously pledged for the payment of all outstanding obligations
2 payable out of the Gross Revenue and pledged herein for the payment of the Bonds.

3 Section 16. Security for the Bonds. The Bonds shall be special limited obligations of the
4 City payable from and secured solely by the Gross Revenues and by money in the Parity Bond Fund
5 and the Reserve Fund. The Gross Revenues are pledged to make the payments into the Parity Bond
6 Fund and the Reserve Fund required by Section 17(a) and (b) of this ordinance, which pledge shall
7 constitute a charge upon such Gross Revenues prior and superior to all other charges whatsoever,
8 save and except reasonable charges for maintenance and operation of the Light System.

9 The Bonds shall not in any manner or to any extent constitute general obligations of the City,
10 the State of Washington or any political subdivision of the State of Washington or a charge upon any
11 general fund or upon any money or other property of the City, the State of Washington or any
12 political subdivision of the State of Washington not specifically pledged thereto by this ordinance.

13 Section 17. Bond Covenants.

14 (a) Parity Bond Fund. A special fund of the City known as the "Seattle Municipal Light
15 Revenue Parity Bond Fund" (the "Parity Bond Fund") has heretofore been created by
16 Ordinance 92938, and is now maintained as a separate account within the Light Fund, for the sole
17 purpose of paying the principal of and interest on the bonds therein authorized and future bonds
18 issued on a parity therewith as the same shall become due. The Bonds shall be payable, principal,
19 premium, if any, and interest, out of the Parity Bond Fund.

20 From and after the issuance of the Bonds, and so long thereafter as obligations are
21 outstanding against the Parity Bond Fund (including any Payment Agreement Payments required to
22 be made under any Parity Payment Agreements), the Director of Finance shall set aside and pay into
23 the Parity Bond Fund on or prior to the respective dates on which the interest on or principal of and
24 interest on the Bonds shall become due and payable certain fixed amounts out of the Gross Revenues
25 sufficient to pay such interest or principal and interest as the same shall become due.
26

1 Money in the Parity Bond Fund shall, to the fullest extent practicable and reasonable, be
2 invested and reinvested at the direction of the Director of Finance solely in, and obligations
3 deposited in such accounts shall consist of, Permitted Investments. Earnings on money and
4 investments in the Parity Bond Fund shall be deposited in and used for the purposes of that fund.

5 (b) Reserve Fund. A special fund of the City known as the "Municipal Light and Power
6 Bond Reserve Fund" (the "Reserve Fund") has heretofore been created by Ordinance 71917, as
7 amended, and is now maintained as a separate account within the Light Fund, for the purpose of
8 securing the payment of the principal of and interest on all Parity Bonds outstanding (including
9 amounts due under any Parity Payment Agreements).

10 The City covenants and agrees that it will pay into the Reserve Fund out of any money
11 legally available therefor, within five (5) years from the date of issuance of the Bonds, the amount
12 required to fund the Reserve Fund to the Reserve Fund Requirement.

13 Money held in the Reserve Fund shall, to the fullest extent practicable and reasonable, be
14 invested and reinvested at the direction of the Director of Finance solely in, and obligations
15 deposited in such accounts shall consist of, Permitted Investments. Earnings on money and
16 investments in the Reserve Fund shall be deposited in that fund and credited against amounts
17 required to be deposited therein until the Reserve Fund is fully funded, and thereafter such earnings
18 shall be deposited in the Parity Bond Fund.

19 (i) Reserve Fund Requirement.

20 (A) The City shall provide in the Parity Bond Ordinance authorizing the
21 issuance of any Future Parity Bonds for deposit into the Reserve Fund out of the Gross Revenues (or
22 out of any other funds of the City on hand and legally available therefor, including the proceeds of
23 the Future Parity Bonds being issued or any other Future Parity Bonds) of periodic payments so that
24 by five (5) years from the date of such Future Parity Bonds there will have been paid into the
25 Reserve Fund an amount which, together with the money already on deposit therein, will be at least
26

1 equal to the Reserve Fund Requirement for all Parity Bonds outstanding at the end of that five-year
2 period.

3 (B) Notwithstanding the foregoing, any Parity Bond Ordinance may
4 provide for the City to obtain Qualified Insurance or a Qualified Letter of Credit for specific
5 amounts required to be paid into the Reserve Fund. The amount available to be drawn upon under
6 such Qualified Insurance or Qualified Letter of Credit shall be credited against the amounts required
7 to be maintained in the Reserve Fund by Section 17(b)(i)(A).

8 (C) Such Qualified Letter of Credit or Qualified Insurance shall not be
9 cancelable on less than five (5) years' notice. In the event of receipt of any such notice of
10 cancellation, the City shall substitute Qualified Insurance or a Qualified Letter of Credit in the
11 amount required pursuant to Section 17(b)(i)(A) or in the alternative shall create a special account in
12 the Light Fund and deposit therein, on or before the twenty-fifth (25th) day of each of the sixty
13 (60) succeeding calendar months, one sixtieth (1/60th) of the amount sufficient, together with other
14 money and investments on deposit in the Reserve Fund, to equal the Reserve Fund Requirement on
15 the date any such cancellation shall become effective. Such amounts shall be transferred from
16 money in the Light Fund (after making provision for payment of operating and maintenance
17 expenses and for the required payments into the Parity Bond Fund). Amounts on deposit in such
18 special account shall not be available to pay debt service on Parity Bonds or for any other purpose of
19 the City, and shall be transferred to the Reserve Fund on the effective date of any cancellation of a
20 Qualified Letter of Credit or Qualified Insurance to make up the deficiency caused thereby.

21 (D) If the amount in the Reserve Fund shall be less than the Reserve Fund
22 Requirement (taking into account the five (5) year period referred to in Section 17(b)(i)(A)), the City
23 shall transfer to the Reserve Fund money in an amount sufficient to restore the Reserve Fund to the
24 Reserve Fund Requirement within twelve (12) months after the date of such deficiency. The City
25 shall transfer such amounts first from money in the Light Fund (after making provision for payment
26 of operating and maintenance expenses and for the required payments into the Parity Bond Fund)

1 and only thereafter from money in the Construction Fund, first taking money from the unrestricted
2 portion thereof, then taking money from the restricted portion thereof. If the amount in the Reserve
3 Fund shall be greater than the Reserve Fund Requirement, then and only then may the City withdraw
4 such excess from the Reserve Fund and deposit such excess in the Light Fund.

5 (ii) Use of Reserve Fund for Refunding Bonds. If any Parity Bonds are refunded,
6 the money set aside in the Reserve Fund to secure the payment of such Parity Bonds may be used to
7 retire such Parity Bonds or may be transferred to any reserve fund or account which may be created
8 to secure the payment of any bonds issued to refund such Parity Bonds, as long as the money left
9 remaining in the Reserve Fund is at least equal, together with any Qualified Insurance or Qualified
10 Letters of Credit, to the Reserve Fund Requirement.

11 (iii) Use of Reserve Fund for Payment of Debt Service. If the money in the Parity
12 Bond Fund is insufficient to meet maturing installments of either interest on or principal of and
13 interest on the Parity Bonds payable out of the Parity Bond Fund (including amounts payable under
14 any Parity Payment Agreements), such deficiency shall be made up from the Reserve Fund by the
15 withdrawal of money or proceeds of Qualified Insurance or Qualified Letters of Credit therefrom, as
16 the case may be. Any deficiency created in the Reserve Fund by reason of any such withdrawal or
17 claim against Qualified Insurance or a Qualified Letter of Credit shall then be made up out of the
18 Gross Revenues (or out of such other funds of the City on hand and legally available therefor), after
19 making necessary provision for the payments required to be made for operation and maintenance of
20 the Light System and debt service on any obligations payable from such Gross Revenues.

21 (iv) Withdrawals From Reserve Fund. Money in the Reserve Fund may be
22 withdrawn by the City for any lawful purpose as long as the aggregate of any money, Qualified
23 Insurance and Qualified Letters of Credit left remaining on deposit in the Reserve Fund is at least
24 equal to the Reserve Fund Requirement for the Parity Bonds then outstanding.

1 The City reserves the right to substitute Qualified Insurance or a Qualified Letter of Credit
2 for money previously deposited in the Reserve Fund and to withdraw such money to the extent
3 described in the preceding paragraph.

4 Any withdrawals from subaccounts within the Reserve Fund shall be made on a pro rata
5 basis except when the provider of a Qualified Letter of Credit or Qualified Insurance requires all
6 cash and investments in the Reserve Fund to be withdrawn before draws on the Qualified Letter of
7 Credit or Qualified Insurance, or unless the City receives an opinion of Bond Counsel to the effect
8 that such pro rata withdrawal is not required to maintain the exclusion of interest on the Parity Bonds
9 then outstanding from gross income.

10 (v) The City may dispose of all or substantially all of the Light System if the City
11 simultaneously causes all of the Parity Bonds to be, or deemed to be, no longer outstanding.

12 (vi) Except as provided below, the City will not dispose of any part of the Light
13 System in excess of 5% of the value of the net utility plant of the Light System in service unless
14 prior to such disposition:

15 (A) there has been filed with the Director of Finance a certificate of the
16 Professional Utility Consultant stating that such disposition will not impair the ability of the City to
17 comply with the rate covenant set forth in Section 17(c); or

18 (B) provision is made for the payment, redemption or other retirement of a
19 principal amount of Parity Bonds equal to the greater of the following amounts:

20 (I) An amount which will be in the same proportion to the net
21 principal amount of Parity Bonds then outstanding (defined as the total principal amount of Parity
22 Bonds then outstanding less the amount of cash and investments in the Parity Bond Fund) that the
23 Gross Revenues for the twelve (12) preceding months attributable to the part of the Light System
24 sold or disposed of bears to the total Gross Revenues for such period; or

25 (II) An amount which will be in the same proportion to the net
26 principal amount of Parity Bonds then outstanding that the book value of the part of the Light

1 System sold or disposed of bears to the book value of the entire Light System immediately prior to
2 such sale or disposition.

3 (vii) The City may dispose of any portion of the Light System that has become
4 unserviceable, inadequate, obsolete, worn out or unfit to be used or no longer necessary, material to
5 or useful in the operation of the Light System.

6 (viii) If the ownership of all or part of the Light System is transferred from the City
7 through the operation of law, the City shall reconstruct or replace the transferred portion using any
8 proceeds of the transfer unless the City Council determines that such reconstruction or replacement
9 is not in the best interests of the City and the owners of the Parity Bonds, in which case any proceeds
10 shall be used to retire Parity Bonds prior to maturity.

11 (c) Rates and Charges. The City will establish from time to time and maintain such rates
12 for electric energy as will maintain the Light System in sound financial condition and provide
13 sufficient revenues to permit the payment of sums into the special fund which the City has pledged
14 to be set aside for the payment of principal and interest, as herein provided, to be applied to the
15 payment of the principal of and interest on the Parity Bonds until the Parity Bonds shall have been
16 paid in full, and in addition thereto, will pay all costs of operation and maintenance, and all bonds,
17 warrants and indebtedness for which any revenues of the Light System shall have been heretofore
18 pledged.

19 (d) Maintenance and Operation of the Light System. The City will proceed with all
20 reasonable dispatch to complete the Project; will operate the properties of the Light System in an
21 efficient manner and at a reasonable cost; and will maintain, preserve and keep, or cause to be
22 maintained, preserved and kept, the properties of the Light System and every part and parcel thereof
23 in good repair, working order and condition; and from time to time will make or cause to be made all
24 necessary and proper repairs, renewals and replacements thereto so that at all times the business
25 carried on in connection therewith will be properly and advantageously conducted.

1 (e) Books and Financial Statements. The City will keep and maintain proper books of
2 account for the Light System in accordance with generally accepted accounting principles applicable
3 to governmental utilities, and will generally adhere to the uniform system of accounts prescribed by
4 the Division of Municipal Corporations of the State Auditor's Office and the Federal Energy
5 Regulatory Commission; and will prepare, on or before one hundred twenty (120) days after each
6 calendar year, annual financial statements showing reasonable detail, including a balance sheet, an
7 income statement and a statement of cash flows or other such statement. Copies of such financial
8 statements shall be placed on file in the office of the Director of Finance and shall be open to
9 inspection at any reasonable time by any owner (or beneficial owner) of any Parity Bonds. A copy
10 of such financial statements shall be sent to any owner (or beneficial owner) of Parity Bonds, upon
11 request in writing setting forth the name and address to which such financial statements may be sent.

12 (f) Issuance of Future Parity Bonds. Except as provided in Section 17(g) of this
13 ordinance for the issuance of Refunding Parity Bonds, Future Parity Bonds may be issued (and
14 Parity Payment Agreements may be entered into), from time to time in one or more series for any
15 lawful purpose of the City's Light Department, only if at the time of the delivery of each series of
16 Future Parity Bonds to the initial purchasers thereof (or on the effective date of the Parity Payment
17 Agreement):

18 (i) There is no deficiency in the Parity Bond Fund or in any of the accounts
19 therein and provision has been made to meet the Reserve Fund Requirement for all Parity Bonds
20 then outstanding plus such proposed series of Parity Bonds; and

21 (ii) There shall have been filed with the City either:

22 (A) a certificate of the Director of Finance stating that Net Revenue in any
23 twelve (12) consecutive months out of the most recent twenty-four (24) months preceding the
24 delivery of the Parity Bonds then proposed to be issued (the "Base Period") was not less than one
25 hundred twenty-five percent (125%) of maximum Annual Debt Service in any future calendar year
26 on all Parity Bonds then outstanding and the Parity Bonds then proposed to be issued (except that if

1 any adjustment in the rates, fees and charges for the services of the Light System shall be effective at
2 any time on or prior to the date of delivery of the Parity Bonds then proposed to be issued or within
3 six (6) months after the delivery of such Parity Bonds, the Director of Finance shall reflect in his or
4 her certificate the Net Revenue he or she calculates would have been collected in the Base Period if
5 such new rates, fees and charges had been in effect for the entire Base Period), or

6 (B) a certificate of the Professional Utility Consultant setting forth:

7 (I) the amount of the Adjusted Net Revenue computed as
8 provided in paragraph (C) below;

9 (II) the amount of maximum Annual Debt Service in any calendar
10 year thereafter on account of all Parity Bonds to be outstanding in such calendar year, including the
11 Parity Bonds proposed to be issued, and stating that the amount shown in paragraph (B)(I) above is
12 not less than one hundred twenty-five percent (125%) of the amount shown in this paragraph (B)(II).

13 "Net Revenue" as used in this Section 17(f) means that amount determined by deducting
14 from the Gross Revenues the expenses of operation, maintenance and repair of the Light System,
15 *except that on the New Covenant Date, "Net Revenue" as used in this Section 17(f) shall mean that*
16 *amount determined by deducting from the Gross Revenues the expenses of operation, maintenance*
17 *and repair of the Light System and further deducting any deposits into the Rate Stabilization*
18 *Account, and by adding to Gross Revenues any withdrawals from the Rate Stabilization Account..*

19 (iii) For the purposes of the certificate required by paragraph (ii) above, Adjusted
20 Net Revenue shall be computed by the Professional Utility Consultant as follows:

21 The Net Revenue for the Base Period shall be adjusted by any or all of the following
22 conditions and requirements as may be appropriate to the circumstances:

23 (A) If the Parity Bonds are being issued for the purpose of acquiring
24 operating electric utility properties having an earnings record, the Professional Utility Consultant
25 shall estimate the effect on the Net Revenue for the Base Period of the acquisition of such electric
26 utility properties and the integration thereof into the Light System, and shall adjust the Net Revenue

1 for the Base Period to give effect to such estimate. Any such estimate shall be based upon the
2 operating experience and records of the City and upon any available financial statements and records
3 relating to the earnings of such electric utility properties to be acquired.

4 (B) If any changes have been adopted by the City Council and are in effect
5 on the date of sale of the Parity Bonds or are to go into effect not later than twelve (12) months after
6 such date, in any rates and charges imposed by the City on sales of power and energy and other
7 services furnished by the Light System which were not in effect during the entire Base Period, the
8 Professional Utility Consultant may, if such changes resulted in increases in such rates and charges,
9 and shall, if such changes resulted in reductions in such rates and charges, adjust the Net Revenue
10 for the Base Period to reflect any change in such Net Revenue which would have occurred if the
11 changed rates and charges had been in effect during the entire Base Period.

12 (C) If the purpose for which the Parity Bonds are being issued is to acquire
13 or construct generation or transmission facilities required to furnish or make available to the Light
14 System additional power and energy, or transmission facilities required to enable the City to sell
15 additional power and energy, the Professional Utility Consultant may adjust the Net Revenue for the
16 Base Period by (a) deducting the amount of the estimated increase in Operating Expenses resulting
17 from the acquisition or construction of such facilities in their first year of full operation, (b) adding
18 any additional revenues to be derived from the sale or transmission of such additional power and
19 energy pursuant to executed power sales contracts, and (c) adding an amount equal to the estimated
20 cost of the power and energy which would have been replaced or displaced by such facilities had
21 such additional power and energy in excess of the power and energy to be sold pursuant to clause
22 (b) above been used in the Light System during the Base Period.

23 (D) If there were any customers added to the Light System during the Base
24 Period or thereafter and prior to the date of the Professional Utility Consultant's certificate, the Net
25 Revenue may be adjusted on the basis that such added customers were customers of the Light
26 System during the entire Base Period.

1 (E) If extensions of or additions to the Light System (not described in
2 subparagraph (C) above) are in the process of construction on the date of the Professional Utility
3 Consultant's certificate, or if the proceeds of the Parity Bonds being issued are to be used to acquire
4 or construct extensions of or additions to the Light System (not described in subparagraph
5 (C) above), the Net Revenue for the Base Period may be adjusted by adding any additional revenues
6 not included in the preceding paragraphs that will be derived from such additions and extensions and
7 deducting the estimated increase in operating and maintenance expenses resulting from such
8 additions and extensions.

9 (F) The Net Revenue for the Base Period may be adjusted by excluding
10 from the determination of expenses of operation, maintenance and repair of the Light System any
11 extraordinary, nonrecurring expenses of the Light System or any judgments or amounts to be paid in
12 settlement of claims against the Light System.

13 (iv) In rendering any certificate under this Section 17(f), the Professional Utility
14 Consultant may rely upon, and such certificate shall have attached thereto, (A) financial statements
15 of the Light System, certified by the Director of Finance, showing income and expenses for the
16 period upon which the same are based and a balance sheet as of the end of such period, (B) similar
17 certified statements by the Division of Municipal Corporations of the Office of the State Auditor of
18 the State (or any successor thereto), or (C) similar certified statements by a Certified Public
19 Accountant for as much of such period as any examination by them has been made and completed.
20 If two or more of such statements are inconsistent with each other, the Professional Utility
21 Consultant shall rely on the statement described under clause (A) in this Section 17(f)(iv).

22 (g) Issuance of Refunding Parity Bonds.

23 (i) Without complying with the provisions of Section 17(f) of this ordinance, the
24 City may at any time and from time to time issue one or more series of Refunding Parity Bonds, but
25 only if there shall have been filed with the City a certificate of the Director of Finance stating that
26 Annual Debt Service immediately after the issuance of such Refunding Parity Bonds (calculated by

1 including debt service on the Refunding Parity Bonds but excluding debt service on the bonds to be
2 refunded with the proceeds thereof) does not exceed the Annual Debt Service immediately prior to
3 the issuance of the Refunding Parity Bonds (calculated by including debt service on the bonds to be
4 refunded but excluding debt service on the Refunding Parity Bonds) by more than Five Thousand
5 dollars (\$5,000) in any calendar year that any then-outstanding Parity Bonds are anticipated to be
6 outstanding.

7 (ii) Parity Bonds of any one or more series or one or more maturities within a
8 series may be refunded by a single series of Refunding Parity Bonds, which Parity Bonds to be
9 refunded shall be specified in the Parity Bond Ordinance providing for the issuance of the Refunding
10 Parity Bonds, and the principal amount of such Refunding Parity Bonds may include amounts
11 necessary to pay the principal of the Parity Bonds to be refunded, interest thereon to the date of
12 payment or redemption thereof, any premium payable thereon upon such payment or redemption and
13 the costs of issuance of such Refunding Parity Bonds. The proceeds of the Refunding Parity Bonds
14 shall be held and applied in such manner as is provided in the Parity Bond Ordinance providing for
15 the issuance of such Refunding Parity Bonds, so that upon the delivery of such Refunding Parity
16 Bonds the Parity Bonds to be refunded thereby shall be deemed to be no longer outstanding in
17 accordance with the provisions of the Parity Bond Ordinance providing for the issuance of those
18 bonds.

19 (iii) Refunding Parity Bonds may also be issued upon compliance with the
20 provisions of Section 17(f) of this ordinance.

21 (iv) Nothing contained in this ordinance shall prohibit or prevent, or be deemed or
22 construed to prohibit or prevent, the City from issuing Refunding Parity Bonds to fund or refund
23 maturing Parity Bonds of the City for the payment of which money is not otherwise available.

24 Section 18. Preservation of Tax Exemption for Interest on Bonds. The City covenants
25 that it will take all actions consistent with the terms of the Bonds, this ordinance and the Bond
26 Resolution, reasonably within its power and necessary to prevent interest on the Bonds from being

1 included in gross income for federal income tax purposes, and it will neither take any action nor
2 make or permit any use of proceeds of the Bonds or other funds of the City treated as proceeds of the
3 Bonds at any time during the term of the Bonds which will cause interest on the Bonds to be
4 included in gross income for federal income tax purposes.

5 The City has not been notified of any listing or proposed listing by the Internal Revenue
6 Service to the effect that it is a bond issuer whose arbitrage certifications may not be relied upon.

7 Section 19. Bonds Negotiable. The Bonds shall be negotiable instruments to the extent
8 provided by RCW 62A.8-102 and 62A.8-105.

9 Section 20. Advance Refunding or Defeasance of Bonds. The City may issue advance
10 refunding bonds pursuant to the laws of the State or use money available from any other lawful
11 source to pay when due the principal of and premium, if any, and interest on the Bonds, or any
12 portion thereof included in a refunding or defeasance plan, and to redeem and retire, release, refund
13 or defease those Bonds (the "Defeased Bonds") and to pay the costs of such refunding or defeasance.
14 If money and/or Government Obligations sufficient in amount, together with known earned income
15 from the investments thereof, to redeem and retire, release, refund or defease the Defeased Bonds in
16 accordance with their terms, are set aside in a special trust fund or escrow account irrevocably
17 pledged to that redemption, retirement or defeasance (the "Trust Account"), then all right and
18 interest of the owners of the Defeased Bonds in the covenants of this ordinance and in the Gross
19 Revenue and the funds and accounts pledged to the payment of the Defeased Bonds, other than the
20 right to receive the funds so set aside and pledged, thereafter shall cease and become void. Such
21 owners thereafter shall have the right to receive payment of the principal of and interest or
22 redemption price on the Defeased Bonds from the Trust Account. The City shall include in the
23 refunding or defeasance plan such provisions as the City deems necessary for the random selection
24 of any Defeased Bonds that constitute less than all of a particular maturity of the Bonds, for notice of
25 the defeasance to be given to the owners of the Defeased Bonds and to such other persons as the City
26 shall determine, and for any required replacement of Bond certificates for defeased Bonds.

1 After the establishing and full funding of such a Trust Account, the Defeased Bonds shall be
2 deemed no longer outstanding and the City may apply any money in any other fund or account
3 established for the payment or redemption of the Defeased Bonds to any lawful purposes as it shall
4 determine, subject only to the rights of the owners of any other Parity Bonds.

5 If the refunding plan provides that the Defeased Bonds be secured by money and/or
6 Government Obligations pending the prior redemption of the Defeased Bonds and if such refunding
7 plan also provides that certain money and/or Government Obligations are pledged irrevocably for
8 the prior redemption of the Defeased Bonds included in that refunding plan, then only the debt
9 service on the Bonds which are not Defeased Bonds and the refunding bonds, the payment of which
10 is not so secured by the refunding plan, shall be included in the computation of the coverage
11 requirement for the issuance of Future Parity Bonds and for determining compliance with rate
12 covenants.

13 Section 21. Amendments.

14 (a) Amendments Without Bond Owners' Consent. The City Council from time to time
15 and at any time may pass a resolution or resolutions, or ordinance or ordinances, supplemental
16 hereto, which resolution or resolutions, ordinance or ordinances thereafter shall become a part of this
17 ordinance, for any one or more of the following purposes:

18 (i) To add to the covenants and agreements of the City contained in this
19 ordinance other covenants and agreements thereafter to be observed which shall not adversely affect
20 the interests of the owners of any Parity Bonds then outstanding, or to surrender any right or power
21 herein reserved to or conferred upon the City.

22 (ii) To make such provisions for the purpose of curing any ambiguities or of
23 curing, correcting or supplementing any defective provision contained in this ordinance in regard to
24 matters or questions arising under this ordinance as the City Council may deem necessary or
25 desirable and not inconsistent with this ordinance and which shall not adversely affect the interests
26 of owners of any Parity Bonds then outstanding in any material respect.

1 (iii) To make such changes as are necessary to permit the Bonds to be held in
2 registered certificate form or in fully immobilized form by a Securities Depository other than DTC.

3 Any such supplemental resolution or ordinance of the City may be passed without the
4 consent of the owners of any Parity Bonds at any time outstanding, notwithstanding any of the
5 provisions of Section 21(b) of this ordinance, but only upon receipt by the City of an opinion of
6 Bond Counsel to the effect that the amendment is permitted by the terms of this ordinance. The City
7 shall deliver a copy of any such supplemental resolution or ordinance to Moody's, S&P or any other
8 rating agency then maintaining a rating on any Parity Bonds then outstanding prior to its passage by
9 the City.

10 (b) Amendments With Bond Owners' Consent. The City Council may, with the consent
11 of the owners of not less than sixty percent (60%) in aggregate principal amount of the Parity Bonds
12 then outstanding, pass a resolution or resolutions or ordinance or ordinances supplemental hereto for
13 the purpose of adding any provisions to or changing in any manner or eliminating any of the
14 provisions of this ordinance or of any supplemental resolution or ordinance, except no such
15 supplemental resolution or ordinance shall:

16 (i) Extend the fixed maturity of any Parity Bonds, or reduce the rate of interest
17 thereon, or extend the times of payment of interest from their respective due dates, or reduce the
18 amount of the principal thereof, or reduce any premium payable on the redemption thereof, without
19 the consent of the owner of each Parity Bond so affected; or

20 (ii) Reduce the aforesaid percentage of bond owners required to approve any such
21 supplemental resolution or ordinance, without the consent of the owners of all of the Parity Bonds
22 then outstanding.

23 For purposes of determining whether the owners of the requisite percentage of principal
24 amount of Parity Bonds have consented to any amendment to this ordinance, the Accreted Value of
25 Capital Appreciation Bonds shall be deemed to be the principal amount thereof.

1 It shall not be necessary for the consent of bond owners under this Section 21(b) to approve
2 the particular form of any proposed supplemental ordinance or resolution, but it shall be sufficient if
3 such consent shall approve the substance thereof.

4 (c) Effect of Amendment. Upon the passage of any supplemental resolution or ordinance
5 pursuant to the provisions of this section, this ordinance shall be deemed to be modified and
6 amended in accordance therewith, and the respective rights, duties and obligations of the City under
7 this ordinance shall thereafter be determined, exercised and enforced thereunder, subject in all
8 respects to such modification and amendments, and all the terms and conditions of any such
9 supplemental resolution or ordinance shall be deemed to be a part of the terms and conditions of this
10 ordinance for any and all purposes.

11 (d) Notation on Bonds. Parity Bonds executed and delivered after the execution of any
12 supplemental resolution or ordinance passed pursuant to the provisions of this Section 21 may have a
13 notation as to any matter provided for in such supplemental resolution or ordinance, and if such
14 supplemental resolution or ordinance shall so provide, new bonds modified to conform, in the
15 opinion of the City Council, to any modification of this ordinance contained in any such
16 supplemental resolution or ordinance may be prepared by the City and delivered without cost to the
17 owners of any affected Parity Bonds then outstanding, upon surrender for cancellation of such bonds
18 in equal aggregate principal amounts.

19 Section 22. Rate Stabilization Account. There is hereby established in the Light Fund a
20 Rate Stabilization Account. On the New Covenant Date, the City may at any time deposit in the
21 Rate Stabilization Account, Gross Revenue and any other money received by the Light System and
22 available to be used therefor. Thereafter, the City may withdraw any or all of the money from the
23 Rate Stabilization Account for inclusion in the Net Revenue for any fiscal year of the City. Such
24 deposits or withdrawals may be made up to and including the date ninety (90) days after the end of
25 the fiscal year for which the deposit or withdrawal will be included as Net Revenue.
26

1 Section 23. Sale of Bonds. The Director of Finance may provide for the sale of the Bonds
2 by public sale or by a negotiated sale, limited offering or private placement, with the successful
3 underwriter, placement agent or purchaser, as applicable, chosen through a selection process
4 acceptable to the Director of Finance. The terms of that sale, which may include a forward or
5 delayed delivery of the Bonds, shall be consistent with this ordinance and the Bond Resolution, and
6 shall be confirmed by the Bond Resolution. The Bonds will be delivered to the purchasers as
7 provided in the Bond Resolution, immediately upon payment to the City of the purchase price plus
8 accrued interest to the date of closing in immediately available federal funds in Seattle, Washington,
9 at the City's expense or at another place upon which the Director of Finance and the purchaser may
10 mutually agree at the purchaser's expense.

11 CUSIP numbers (if required) will be printed on the Bonds, but neither failure to print CUSIP
12 numbers on any Bond nor error with respect thereto shall constitute cause for a failure or refusal by
13 the purchasers to accept delivery of and pay for the Bonds in accordance with the purchase offer.
14 All expenses in relation to the printing of CUSIP numbers on the Bonds shall be paid by the City,
15 but the fee of the CUSIP Service Bureau for the assignment of those numbers shall be the
16 responsibility of and shall be paid by the purchasers.

17 The City will cause the Bonds to be typed, photocopied, printed or lithographed, sealed and
18 executed and will furnish the approving legal opinion of Bond Counsel regarding the Bonds, the
19 opinion also being printed on each Bond unless the Bond is typed or photocopied.

20 Section 24. Continuing Disclosure. The City shall undertake to provide for the benefit of
21 holders of the Bonds disclosure of certain financial information and operating data of the type
22 included in the final official statement, if any, for the Bonds, as well as disclosure of certain material
23 events respecting the Bonds, in the manner and to the extent required by United States Securities and
24 Exchange Commission Rule 15c2-12. The particular terms of the undertaking shall be set forth in
25 the Bond Resolution.
26

APPENDIX B
FORM OF BOND COUNSEL OPINION

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FORM OF APPROVING LEGAL OPINION

The City of Seattle, Washington

Re: The City of Seattle, Washington, \$87,735,000 Municipal Light and Power Refunding Revenue Bonds, 2002

We have served as bond counsel to The City of Seattle, Washington (the "City"), in connection with the issuance of the above-referenced bonds (the "Bonds"), and in that capacity have examined such law and such certified proceedings and other documents as we have deemed necessary to render this opinion.

The Bonds are issued pursuant to the laws of the State of Washington and Ordinance 120931 and Resolution 30549 of the City (collectively, the "Bond Legislation") to provide all or part of the funds to pay the costs of refunding the Refunded Bonds and pay the costs of issuance and sale of the Bonds, all as set forth in the Bond Legislation.

Reference is made to the Bond Legislation for the definitions of the capitalized terms used and not otherwise defined herein.

The Bonds are dated December 1, 2002, and are in the denominations, bear interest payable on the dates and at the rates, mature at the times and in the amounts, and have such prepayment or redemption and other provisions as are set forth in the Bonds and in the Bond Legislation.

The Bonds are special limited obligations of the City payable from and secured solely by the Gross Revenues of the Light System and by money in the Seattle Municipal Light Revenue Parity Bond Fund (the "Parity Bond Fund") and the Municipal Light and Power Bond Reserve Fund (the "Reserve Fund"). The Gross Revenues have been pledged to make the required payments into the Parity Bond Fund and the Reserve Fund, which pledge constitutes a charge on the Gross Revenues prior and superior to all other charges whatsoever, except reasonable charges for maintenance and operation of the Light System, and except that the Bonds shall have a lien and charge upon such Gross Revenues on a parity with the lien and charge of the Outstanding Parity Bonds and any Future Parity Bonds.

1111 THIRD
AVENUE
Suite 3400
SEATTLE
Washington
98101-3299

Telephone
(206) 447-4400
Facsimile
(206) 447-9700
Website
WWW.FOSTER.COM

ANCHORAGE
Alaska

PORTLAND
Oregon

SEATTLE
Washington

SPOKANE
Washington

The City of Seattle
[Closing Date]

Under the Internal Revenue Code of 1986, as amended (the “Code”), the City is required to comply with certain requirements after the date of issuance of the Bonds in order to maintain the exclusion of the interest on the Bonds from gross income for federal income tax purposes, including, without limitation, requirements concerning the qualified use of Bond proceeds and the facilities financed or refinanced with Bond proceeds, limitations on investing gross proceeds of the Bonds in higher yielding investments in certain circumstances and the arbitrage rebate requirement to the extent applicable to the Bonds. The City has covenanted in the Bond Legislation to comply with those requirements, but if the City fails to comply with those requirements, interest on the Bonds could become taxable retroactive to the date of issuance of the Bonds. We have not undertaken and do not undertake to monitor the City’s compliance with such requirements.

As of the date of initial delivery of the Bonds to the purchaser thereof and full payment therefor, it is our opinion that under existing law:

1. The City is a duly organized and legally existing first class city under the laws of the State of Washington;
2. The City has duly authorized and approved the Bond Legislation, and the Bonds are issued in full compliance with the provisions of the Constitution and laws of the State of Washington, the Bond Legislation and other ordinances and resolutions of the City relating thereto;
3. The Bonds constitute valid obligations of the City payable solely out of the Gross Revenues of the Light System and money in the Parity Bond Fund and the Reserve Fund, except only to the extent that enforcement of payment may be limited by bankruptcy, insolvency or other laws affecting creditors' rights and principles of equity if equitable remedies are sought;
4. The Bonds are not general obligations of the City; and
5. Assuming compliance by the City after the date of issuance of the Bonds with applicable requirements of the Code, the interest on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the alternative minimum tax applicable to individuals; however, while interest on the Bonds also is not an item of tax preference for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by corporations is to be taken into account in the computation of adjusted current earnings for purposes of the alternative minimum tax applicable to corporations, interest on the Bonds received by certain S corporations may be subject to tax, and interest on the Bonds received by foreign corporations with United States branches may be subject to a foreign branch profits tax. We express no opinion regarding any other federal tax consequences of receipt of interest on the Bonds.

The City of Seattle
[Closing Date]

We express no opinion herein concerning the completeness or accuracy of any official statement, offering circular or other sales or disclosure material relating to the issuance of the Bonds or otherwise used in connection with the Bonds.

We bring to your attention the fact that the foregoing opinions are expressions of our professional judgment on the matters expressly addressed and do not constitute guarantees of result.

Respectfully submitted,

FOSTER PEPPER & SHEFELMAN PLLC

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APPENDIX C

2001 AUDITED FINANCIAL STATEMENTS OF THE DEPARTMENT

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**CITY OF SEATTLE –
CITY LIGHT DEPARTMENT**

FINANCIAL STATEMENTS FOR THE
YEARS ENDED DECEMBER 31, 2001 AND 2000, AND
INDEPENDENT AUDITORS' REPORT

Deloitte & Touche LLP

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

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INDEPENDENT AUDITORS' REPORT

Superintendent
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, 2001 and 2000, and the related statements of operations and changes in retained earnings and of cash flows for the years then ended. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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, 2001 and 2000, and the results of its operations 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 was required to adopt Statement of Financial Accounting Standards (SFAS) No. 133, *Accounting for Derivative Instruments and Hedging Activities*, SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities* an amendment of FASB Statement No. 133, and Governmental Accounting Standards Board No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, effective January 1, 2001.

A handwritten signature in black ink that reads "Deloitte & Touche LLP".

March 29, 2002

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

BALANCE SHEETS

DECEMBER 31, 2001 AND 2000

<u>ASSETS</u>	<u>2001</u>	<u>2000</u>
UTILITY PLANT, at original cost:		
Plant in service, excluding land	\$ 1,954,842,829	\$ 1,811,151,094
Less accumulated depreciation	<u>(808,183,648)</u>	<u>(756,498,165)</u>
	1,146,659,181	1,054,652,929
Construction work-in-progress	115,321,307	152,981,465
Nonoperating property, net of accumulated depreciation	7,216,228	6,613,263
Land and land rights	<u>30,838,923</u>	<u>27,919,760</u>
	1,300,035,639	1,242,167,417
CAPITALIZED PURCHASED POWER COMMITMENT	56,947,942	65,855,587
RESTRICTED ASSETS:		
Municipal Light & Power Bond Reserve Account:		
Cash and equity in pooled investments	70,993,458	53,087,023
U.S. government securities	-	13,348,344
Bond proceeds and other:		
Cash and equity in pooled investments	63,559,476	3,969,797
Investments	102,274,374	-
Special deposits and other	<u>6,605,501</u>	<u>3,375,745</u>
	243,432,809	73,780,909
CURRENT ASSETS:		
Cash and equity in pooled investments	3,759,018	19,041,923
Accounts receivable (net of allowance of \$6,110,000 and \$3,590,000)	53,187,620	68,780,916
Unbilled revenues	61,366,163	35,437,430
Energy contracts	14,526,178	-
Materials and supplies at average cost	21,810,750	21,548,144
Prepayments, interest receivable, and other	<u>1,185,687</u>	<u>1,321,039</u>
	155,835,416	146,129,452
OTHER ASSETS:		
Deferred conservation costs, net	97,179,553	79,936,854
Other deferred charges, net	<u>357,530,128</u>	<u>33,818,445</u>
	454,709,681	113,755,299
TOTAL	<u>\$ 2,210,961,487</u>	<u>\$ 1,641,688,664</u>

See notes to financial statements.

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

STATEMENTS OF OPERATIONS AND CHANGES IN RETAINED EARNINGS

YEARS ENDED DECEMBER 31, 2001 AND 2000

	<u>2001</u>	<u>2000</u>
OPERATING REVENUES		
Retail power revenues	\$ 503,437,272	\$ 391,578,285
Wholesale power revenues	108,523,610	108,132,297
Transmission and other	<u>15,625,381</u>	<u>5,918,117</u>
	627,586,263	505,628,699
OPERATING EXPENSES:		
Long-term purchased power	151,213,357	79,304,610
Short-term wholesale power purchases	224,421,729	212,402,254
Power marketing and system control	6,064,682	5,504,322
Generation	17,012,159	25,665,927
Transmission	30,260,132	21,726,234
Distribution	36,493,212	34,523,307
Customer service	27,532,059	22,179,214
Conservation	8,522,651	6,972,547
Administrative and general	39,140,392	37,020,250
City of Seattle occupation tax	30,648,911	24,002,685
Other taxes	21,916,749	18,857,370
Depreciation	<u>61,538,960</u>	<u>55,498,917</u>
	<u>654,764,993</u>	<u>543,657,637</u>
Net operating loss	(27,178,730)	(38,028,938)
NONOPERATING REVENUES (EXPENSES):		
Investment income	13,486,717	9,753,106
Interest expense	(72,109,397)	(48,097,827)
Amortization of debt expense	(1,786,694)	(5,054,837)
Gain on sale of Centralia Steam Plant	-	29,639,799
Other expense, net	<u>(1,048,013)</u>	<u>(240,039)</u>
	(61,457,387)	(13,999,798)
FEES, GRANTS, AND TRANSFERS		
Capital	13,372,688	-
Operating	<u>1,923,022</u>	<u>-</u>
	<u>15,295,710</u>	<u>-</u>
NET LOSS	(73,340,407)	(52,028,736)
RETAINED EARNINGS:		
Beginning of the year	<u>247,990,953</u>	<u>300,019,689</u>
End of the year	<u>\$ 174,650,546</u>	<u>\$ 247,990,953</u>

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2001 AND 2000

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

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

STATEMENTS OF CASH FLOWS *(continued)*

YEARS ENDED DECEMBER 31, 2001 AND 2000

	<u>2001</u>	<u>2000</u>
RECONCILIATION OF NET OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net operating loss	\$ (27,178,730)	\$ (38,028,938)
Adjustments to reconcile net operating loss to net cash provided by (used for) operating activities:		
Depreciation and amortization	70,412,288	63,510,859
Cash provided by (used for) changes in operating assets and liabilities:		
Accounts receivable	32,957,358	(8,420,793)
Unbilled revenues	(25,928,733)	(3,277,080)
Other deferred charges	(316,162,037)	3,484,498
Materials and supplies	315,615	(1,524,255)
Prepayments, interest receivable, and other	10,087,199	5,062,837
Provision for injuries and damages	(327,102)	476,094
Accounts payable, taxes and other	(65,068,412)	53,005,566
Compensated absences	761,547	376,388
Other	<u>9,862,885</u>	<u>(117,881)</u>
 NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	 <u>\$ (310,268,122)</u>	 <u>\$ 74,547,295</u>
 CASH AND EQUITY IN POOLED INVESTMENTS AT DECEMBER 31 CONSISTS OF:		
Cash and cash equivalents	\$ 13,653,054	\$ 25,871,777
Equity in pooled investments	<u>131,264,399</u>	<u>53,602,712</u>
	 <u>\$ 144,917,453</u>	 <u>\$ 79,474,489</u>

CITY OF SEATTLE – CITY LIGHT DEPARTMENT

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2001 AND 2000

NOTE 1: OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

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

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

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

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

Nonexchange transactions: In December 1998, GASB issued Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, that requires reporting nonexchange transactions as

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

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

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

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

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

Compensated absences: Permanent employees of the Department earn vacation time in accordance with length of service. A maximum of 480 hours may be accumulated and, upon termination, employees are entitled to compensation for unused vacation. At retirement, employees receive compensation equivalent

to 25% of their accumulated sick leave. The Department accrues all costs associated with compensated absences, including payroll taxes.

Accounts payable and other: The composition of accounts payable and other is as follows:

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

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

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

	<u>2001</u>	<u>2000</u>
Residential	37.3 %	38.2 %
Commercial	41.6	41.0
Industrial	12.3	12.1
Governmental	<u>8.8</u>	<u>8.7</u>
	<u>100.0 %</u>	<u>100.0 %</u>

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

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

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

NOTE 2: JOINTLY OWNED PLANT

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

NOTE 3: CASH AND EQUITY IN POOLED INVESTMENTS AND INVESTMENTS

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

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

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

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

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

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

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

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

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

NOTE 4: LONG-TERM DEBT

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

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

In December 2000, the Department issued \$98.8 million in ML&P Revenue Bonds that bear interest at rates ranging from 4.5% to 5.625% and mature serially from December 1, 2006, through 2025. Proceeds

from the 2000 bond issue were used to finance a portion of the Department's ongoing capital improvement and conservation program.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

NOTE 5: SEATTLE CITY EMPLOYEES' RETIREMENT SYSTEM

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

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

SCERS provides retirement, death, and disability benefits. Retirement benefits vest after five years of credited service, while death and disability benefits vest after 10 years of service. Retirement benefits are

calculated, generally, as 2% multiplied by years of creditable service, multiplied by average salary, based on the highest 24 consecutive months, excluding overtime. The benefit is actuarially reduced for early retirement.

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

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

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

Actuarial data

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

Actuarial assumptions*

Percentage

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

* Underlying price inflation at 4.0%.

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

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

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

NOTE 6: DEFERRED COMPENSATION

The Department's employees may contribute to the City of Seattle's Voluntary Deferred Compensation Plan (the Plan). The Plan, available to City employees and officers, permits participants to defer a portion of their

salary until future years. The deferred compensation is paid to participants and their beneficiaries upon termination, retirement, death, or unforeseeable emergency.

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

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

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

NOTE 7: LONG-TERM PURCHASED POWER AND WHOLESALE POWER TRANSACTIONS

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

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

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

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

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

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

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

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

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

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

Wind generation: In October 2001, the Department entered into an agreement with PacifiCorp Power Marketing, Inc. (PPMI) for the purchase of energy and associated environmental attributes primarily from

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

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

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

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

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

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

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

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

NOTE 8: OTHER ASSETS

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

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

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

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

NOTE 9: DEFERRED CREDITS

Deferred credits consist of the following at December 31:

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

NOTE 10: PROVISION FOR INJURIES AND DAMAGES

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

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

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

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

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

NOTE 11: COMMITMENTS AND CONTINGENCIES

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

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

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

Minimum payments under the leases are:

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

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

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

Some fish species that inhabit waters where hydroelectric projects are owned by the Department or where the Department purchases power have been listed under the ESA as either threatened or endangered. In 1995, the National Marine Fisheries Service (NMFS) developed a broad species recovery plan for the Columbia River Basin and supplemental plans in 1998 and 2000, based on Biological Opinions relating to the Columbia and Snake River fisheries. As a result, the Department’s power generation at its Boundary Project has been reduced in the fall and winter when the region experiences its highest sustained energy demand, and the Boundary Project’s firm capability has also been reduced. In addition, the Department now receives power under a contract with the BPA that provides the City with a percentage of the total BPA generation and the Department would thus be affected by changes in flows required in the Biological Opinions. In the opinion of the Department, it is unlikely that new Biological Opinions will result in significant changes in flows that would affect the Boundary Project, Priest Rapids, and BPA system. While it is unclear how other fish listings, including bull trout and chinook salmon, may affect the Department’s hydroelectric projects and operations, the Department has entered into agreements that include extensive measures to protect fish and were intended to mitigate potential impacts of its projects on the Cedar, Skagit, and South Fork Tolt rivers. In addition, the Department is conducting research on these species to monitor their population health and identify potential impacts. The Department is carrying out an ESA Early Action program that will assist in the recovery of chinook and bull trout and address any further impacts on these species.

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

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

APPENDIX D
DEMOGRAPHIC AND ECONOMIC INFORMATION

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DEMOGRAPHIC AND ECONOMIC INFORMATION

King, Snohomish and Island Counties constitute the Seattle-Bellevue-Everett Primary Metropolitan Statistical Area (the "Seattle PMSA"), the fourth-largest metropolitan center on the West Coast. The City of Seattle, encompassing 92 square miles, is the largest city in the Pacific Northwest and is the center of King County's economic activity. Of the State's population, nearly 30 percent reside in King County, and of the County's population, 33 percent live in the City.

Population

The 1990 and 2000 U.S. Census population figures and recent population estimates for the City, King County and the Seattle PMSA are as follows:

Year	Seattle	King County	Seattle PMSA
2001 ⁽ⁱⁱ⁾	568,100	1,758,300	NA
2000 ⁽ⁱ⁾	563,374	1,737,034	2,414,616
1999 ⁽ⁱⁱ⁾	540,500	1,677,000	2,333,600
1998 ⁽ⁱⁱ⁾	539,700	1,665,800	2,306,400
1997 ⁽ⁱⁱ⁾	536,600	1,646,200	2,269,000
1996 ⁽ⁱⁱ⁾	534,700	1,628,800	2,237,200
1990 ⁽ⁱ⁾	516,259	1,507,319	1,972,961

(i) Source: U.S. Census

(ii) Source: Washington State Office of Financial Management, Forecasting Division

Per Capita Income

The following table presents per capita personal income. Per capita income for the State of Washington in 2001 was \$31,582.

	2000	1999	1998	1997	1996
Seattle PMSA	\$ 40,686	\$ 38,858	\$ 35,880	\$ 32,766	\$ 30,775
King County	45,536	43,201	39,335	35,382	33,316
State of Washington	31,230	29,819	28,285	26,469	25,015

Source: U.S. Bureau of Economic Analysis, U.S. Department of Commerce

Building Permit Value

The table below lists the value of housing construction for which building permits have been issued by the City of Seattle. The value of public construction is not included in this table.

CITY OF SEATTLE BUILDING PERMITS

Year	New Single Family		New Multifamily		Total Value
	Units	Value	Units	Value	
2002*	164	\$ 25,724,832	878	\$ 64,527,015	\$ 90,251,847
2001	484	73,945,951	3,162	222,190,662	296,136,613
2000	449	64,587,520	4,403	286,312,450	350,899,970
1999	480	65,696,744	3,065	191,087,633	256,784,377
1998	530	71,640,186	3,534	219,183,170	290,823,356
1997	469	68,601,487	1,930	147,134,120	215,735,607

* Through May 2002.

Source: *Building Permit Activity of City and County in the State of Washington, BP Logistics*

Retail Activity

The following table presents taxable retail sales in Seattle and King County.

THE CITY OF SEATTLE AND KING COUNTY TAXABLE RETAIL SALES (000)

Year	The City of Seattle	King County
2002*	\$ 2,943,543	\$ 8,042,808
2001	12,942,596	36,003,190
2000	13,625,486	37,383,541
1999	12,728,470	34,810,738
1998	11,452,958	31,749,546
1997	10,633,522	29,154,617

* Through first quarter of 2002.

Source: *Washington State Department of Revenue*

Industry and Employment

The table below shows employment by sector and unemployment for the Seattle PMSA.

**SEATTLE-BELLEVUE-EVERETT PMSA
(KING, SNOHOMISH AND ISLAND COUNTIES)
RESIDENT CIVILIAN LABOR FORCE AND EMPLOYMENT
AND NONAGRICULTURAL WAGE AND SALARY EMPLOYMENT**

	Average Annual ⁽¹⁾				
	2001 ⁽²⁾	2000 ⁽³⁾	1999	1998	1997
Civilian Labor Force					
Employment	1,292,600	1,344,500	1,357,200	1,337,300	1,297,500
Unemployment	<u>70,400</u>	<u>52,000</u>	<u>47,600</u>	<u>42,700</u>	<u>44,800</u>
Total Civilian Labor Force	1,362,900	1,396,500	1,404,800	1,380,000	1,342,300
Unemployment Rate ⁽⁴⁾	5.2%	3.7%	3.4%	3.1%	3.3%
Nonagricultural Employment					
Manufacturing					
Aircraft and parts	83,600	82,400	95,100	108,200	101,100
Misc. trans. equipment	6,900	9,100	9,500	9,300	8,800
Food products	14,300	15,200	14,900	16,100	17,000
Wood products and paper	11,900	12,100	12,100	12,500	12,400
Machinery and electrical	21,600	22,100	22,200	21,700	20,700
Instruments	11,500	11,700	11,900	12,100	11,800
Textiles, apparel and leather	4,100	4,400	4,500	4,900	5,100
Printing and publishing	13,600	14,400	13,700	13,800	14,100
Other manufacturing categories	<u>27,900</u>	<u>29,300</u>	<u>30,100</u>	<u>29,700</u>	<u>27,800</u>
Total manufacturing	195,400	200,700	214,000	228,200	218,800
Nonmanufacturing					
Mining and quarrying	1,100	1,100	700	700	700
Contract construction	80,100	84,300	78,400	73,300	66,500
Transp., commun. and utilities	87,100	87,900	84,000	81,000	77,700
Wholesale and retail trade	324,700	335,900	325,000	315,500	304,000
Finance, insurance and real estate	87,400	84,000	84,600	81,500	76,700
Services	429,900	438,000	408,700	390,800	371,400
Government	<u>195,800</u>	<u>190,500</u>	<u>187,000</u>	<u>183,000</u>	<u>178,100</u>
Total nonmanufacturing	1,206,100	1,221,700	1,168,400	1,125,600	1,075,100
Total Nonagricultural Employment	1,401,500	1,422,400	1,382,400	1,353,800	1,293,900

(1) Columns may not add to totals due to rounding.

(2) Preliminary.

(3) Revised.

(4) Unemployment rate as of August 2002 estimated at 6.4 percent.

Source: Washington State Department of Employment Security

The following table presents employment data for major employers in the Puget Sound area, which is defined for the purposes of this section as King, Kitsap, Pierce, and Snohomish Counties, Washington.

**PUGET SOUND AREA
MAJOR EMPLOYERS**

<u>Employer</u>	<u>Employees</u>
The Boeing Company	62,600 ⁽¹⁾
Microsoft	25,235 ⁽²⁾
University of Washington	23,500
King County	13,500
City of Seattle	11,200
Safeway	11,000
Group Health Cooperative	9,700
Sisters of Providence Health	8,150
Fred Meyer	8,100
Alaska Air Group	6,000

(1) State-wide employment as of October 2002. (The Puget Sound area is the location for almost all of the Boeing employment within the State.)

(2) As of July 2002.

Source: Individual employers, April 2002.

The Boeing Company (“Boeing”) had revenues of \$58.0 billion in 1999, \$51.3 billion in 2000 and \$58.2 billion in 2001. Total airplane deliveries in 2001 were 527, compared to 489 in 2000. Boeing remains the largest employer in the Puget Sound area, although total employment within the company dropped from 238,600 to 168,400 and employment within the State dropped from 103,420 to 62,600 between February 1998 and October 2002. In September 2001, Boeing moved its corporate headquarters to Chicago, Illinois. Subsequent to the events of September 11, 2001, Boeing has laid off or given notices of layoffs to more than 30,000 employees (as partially reflected in the table above), and recently announced there may be additional layoffs. A total of 25,000 people have been laid off this year; approximately 16,000 of those were the Puget Sound area.

Microsoft, which is headquartered in Redmond, is the region’s largest high technology employer with more than 48,000 employees worldwide, including 24,700 in the Puget Sound area as of January 1, 2002. Microsoft is a developer and manufacturer of computer operating systems and software. Microsoft’s fiscal year 2002 revenues were \$28.4 billion, compared to \$25.3 billion in fiscal year 2001.

Other Information

A variety of additional issues may have an effect on the economy of the Seattle area, including but not limited to transportation infrastructure, endangered species listings, the commercial real estate market, higher energy costs, limits on residential development and resulting housing costs, and the September 11, 2001, terrorist attacks and their effect on aerospace, tourism and travel. The effects of these issues are interdependent and cannot be quantified.

APPENDIX E
BOOK-ENTRY TRANSFER SYSTEM

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BOOK-ENTRY TRANSFER SYSTEM

The following information has been provided by DTC. The City makes no representation as to the accuracy or completeness thereof. Actual purchasers of the Bonds (the “Beneficial Owners”) should confirm the following with DTC or its participants (the “Participants”).

DTC will act as securities depository for the Bonds. The Bonds will be issued as fully registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Bond certificate will be issued for each maturity of the Bonds in the principal amount of such maturity and will be deposited with DTC.

DTC, the world’s largest depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over two million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of Bonds under the DTC system, in Authorized Denominations, must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC’s records. The ownership interest of each actual purchaser of each Bond (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co. or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC’s records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

When notices are given, they shall be sent by the Bond Registrar to DTC only. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices will be sent to DTC. If less than all of the Bonds are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the City as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, distribution and dividend payments on the Bonds will be made to Cede & Co. or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Bond Registrar, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC (nor its nominee), the Bond Registrar or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions and dividend payments to Cede & Co. (or any other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or the Bond Registrar, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Bonds at any time by giving reasonable notice to the Bond Registrar or the City. Under such circumstances, in the event that a successor securities depository is not obtained, new certificates are required to be printed and delivered.

The City may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered.

The preceding information concerning DTC and DTC's book-entry system has been obtained from sources the City believes to be reliable, but the City takes no responsibility for the accuracy thereof.

The following information has been provided by the City.

Neither the City nor the Bond Registrar will be required to transfer or exchange Bonds during the period between a record date and the next succeeding interest payment date or redemption date. For purposes hereof, record date will mean in the case of each interest payment date, the Bond Registrar's close of business on the 15th day of the month preceding the interest payment date.

With respect to Bonds registered on the Bond Register in the name of Cede and Co., as nominee of DTC, the City and the Bond registrar will have no responsibility or obligation to any Participant or to any person on behalf of whom a Participant holds an interest in the Bonds with respect to (i) the accuracy of the records of DTC, Cede and Co. or any Participant with respect to any ownership interest in the Bonds, (ii) the delivery to any Participant or any other person, other than a bond owner as shown on the Bond Register, of any notice with respect to the Bonds, including any notice of redemption, (iii) the payment to any Participant or any other person, other than a bond owner as shown on the Bond Register, of any amount with respect to principal of or interest on the Bonds, (iv) the selection by DTC or any Participant of any person to receive payment in the event of a partial redemption of the Bonds; (v) any consent given or action taken by DTC as registered owner, or (vi) any other matter. The City and the Bond Registrar may treat and consider Cede and Co., in whose name each Bond is registered on the Bond Register, as the holder and absolute owner of such Bond for the purpose of payment of principal and interest with respect to such Bond, for the purpose of giving notices of redemption and other matters with respect to such Bond, for the purpose of registering transfers with respect to such Bond, and for all other purposes whatsoever.

The City's obligations under the Bond Resolution and the Bonds are to the registered owner or owners of the Bonds, and the City will not be liable to the Participants or Beneficial Owners of Bonds registered in the name of any nominee of DTC or a successor depository, for any acts or omissions of DTC or such successor depository.

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APPENDIX F
MUNICIPAL BOND INSURANCE POLICY SPECIMEN

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**FINANCIAL
SECURITY
ASSURANCE®**

**MUNICIPAL BOND
INSURANCE POLICY**

ISSUER:

BONDS:

Policy No.: -N

Effective Date:

Premium:

FINANCIAL SECURITY ASSURANCE INC. ("Financial Security"), for consideration received, hereby UNCONDITIONALLY AND IRREVOCABLY agrees to pay to the trustee (the "Trustee") or paying agent (the "Paying Agent") (as set forth in the documentation providing for the issuance of and securing the Bonds) for the Bonds, for the benefit of the Owners or, at the election of Financial Security, directly to each Owner, subject only to the terms of this Policy (which includes each endorsement hereto), that portion of the principal of and interest on the Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

On the later of the day on which such principal and interest becomes Due for Payment or the Business Day next following the Business Day on which Financial Security shall have received Notice of Nonpayment, Financial Security will disburse to or for the benefit of each Owner of a Bond the face amount of principal of and interest on the Bond that is then Due for Payment but is then unpaid by reason of Nonpayment by the Issuer, but only upon receipt by Financial Security, in a form reasonably satisfactory to it of (a) evidence of the Owner's right to receive payment of the principal or interest then Due for Payment and (b) evidence, including any appropriate instruments of assignment, that all of the Owner's rights with respect to payment of such principal or interest that is Due for Payment shall thereupon vest in Financial Security. A Notice of Nonpayment will be deemed received on a given Business Day if it is received prior to 1:00 p.m. (New York time) on such Business Day; otherwise, it will be deemed received on the next Business Day. If any Notice of Nonpayment received by Financial Security is incomplete, it shall be deemed not to have been received by Financial Security for purposes of the preceding sentence and Financial Security shall promptly so advise the Trustee, Paying Agent or Owner, as appropriate, who may submit an amended Notice of Nonpayment. Upon disbursement in respect of a Bond, Financial Security shall become the owner of the Bond, any appurtenant coupon to the Bond or right to receipt of payment of principal or interest on the Bond and shall be fully subrogated to the rights of the Owner, including the Owner's right to receive payments under the Bond, to the extent of any payment by Financial Security hereunder. Payment by Financial Security to the Trustee or Paying Agent for the benefit of the Owners shall, to the extent thereof, discharge the obligation of Financial Security under this Policy.

Except to the extent expressly modified by an endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "Business Day" means any day other than (a) a Saturday or Sunday or (b) a day on which banking institutions in the State of New York or the Insurer's Fiscal Agent are authorized or required by law or executive order to remain closed. "Due for Payment" means (a) when referring to the principal of a Bond, payable on the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity unless Financial Security shall elect, in its sole discretion, to pay such principal due upon such acceleration together with any accrued interest to the date of acceleration and (b) when referring to interest on a Bond, payable on the stated date for payment of interest. "Nonpayment" means, in respect of a Bond, the failure of the Issuer to have provided sufficient funds to the Trustee or, if there is no Trustee, to the Paying Agent for payment in full of all principal and interest that is Due for Payment on such Bond. "Nonpayment" shall also include, in respect of a Bond, any payment of principal or interest that is Due for Payment made to an Owner by or on behalf of the Issuer which has been recovered from such Owner pursuant to the

United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction. "Notice" means telephonic or teletyped notice, subsequently confirmed in a signed writing, or written notice by registered or certified mail, from an Owner, the Trustee or the Paying Agent to Financial Security which notice shall specify (a) the person or entity making the claim, (b) the Policy Number, (c) the claimed amount and (d) the date such claimed amount became Due for Payment. "Owner" means, in respect of a Bond, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof, except that "Owner" shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Bonds.

Financial Security may appoint a fiscal agent (the "Insurer's Fiscal Agent") for purposes of this Policy by giving written notice to the Trustee and the Paying Agent specifying the name and notice address of the Insurer's Fiscal Agent. From and after the date of receipt of such notice by the Trustee and the Paying Agent, (a) copies of all notices required to be delivered to Financial Security pursuant to this Policy shall be simultaneously delivered to the Insurer's Fiscal Agent and to Financial Security and shall not be deemed received until received by both and (b) all payments required to be made by Financial Security under this Policy may be made directly by Financial Security or by the Insurer's Fiscal Agent on behalf of Financial Security. The Insurer's Fiscal Agent is the agent of Financial Security only and the Insurer's Fiscal Agent shall in no event be liable to any Owner for any act of the Insurer's Fiscal Agent or any failure of Financial Security to deposit or cause to be deposited sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Financial Security agrees not to assert, and hereby waives, only for the benefit of each Owner, all rights (whether by counterclaim, setoff or otherwise) and defenses (including, without limitation, the defense of fraud, whether acquired by subrogation, assignment or otherwise, to the extent that such rights and defenses may be available to Financial Security) to avoid payment of its obligations under this Policy in accordance with the express provisions of this Policy.

This Policy sets forth in full the undertaking of Financial Security, and shall not be modified, altered or affected by any other agreement or instrument, including any modification or amendment thereto. Except to the extent expressly modified by an endorsement hereto, (a) any premium paid in respect of this Policy is nonrefundable for any reason whatsoever, including payment, or provision being made for payment, of the Bonds prior to maturity and (b) this Policy may not be canceled or revoked. THIS POLICY IS NOT COVERED BY THE PROPERTY CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Policy to be executed on its behalf by its Authorized Officer.

[Countersignature]

FINANCIAL SECURITY ASSURANCE INC.

By _____

By _____
Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.
350 Park Avenue, New York, N.Y. 10022-6022

(212) 826-0100

Form 500NY (5/90)